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Stakeholders

Municipal Securities
Dealers

Notice Type

Approval Notice

Category

Uniform Practice

Affected Rules

[Rule G-12](#), [Rule G-15](#)

MSRB to Amend Rules to Define Two-Day Settlement Cycle

Overview

The Municipal Securities Rulemaking Board (MSRB) received approval from the Securities and Exchange Commission (SEC) on April 29, 2016 to amend MSRB Rules G-12, on uniform practice, and G-15 on confirmation, clearance, settlement and other uniform practice requirements with respect to transactions with customers, to define regular-way settlement for municipal securities transactions as occurring on a two-day settlement cycle (“T+2”) and technical conforming amendments.¹ The MSRB will announce the compliance date of the amendments in a notice to be published on the MSRB website, which date will correspond with the broader industry transition to a T+2 regular-way settlement, which is dependent upon the SEC making corresponding amendments to Exchange Act Rule 15c6-1(a).

Background

In early 2015 the securities industry launched a voluntary initiative to shorten the settlement cycle for securities transactions to reduce counterparty risk, decrease clearing capital requirements, reduce liquidity demands, and harmonize the settlement cycle globally. The industry-led initiative to shorten the current regular-way settlement cycle defined as a three-day settlement cycle (“T+3”) to a T+2 settlement cycle is being led by the Shortened Settlement Cycle Industry Steering Committee (ISC) which is jointly chaired by the Investment Company Institute (ICI) and the Securities Industry and Financial Markets Association (SIFMA).² The ISC announced its proposal in a white paper (the “white paper”), which outlined the timeline and activities required to move to a T+2 settlement cycle in the U.S. for

¹ See Securities Exchange Act of 1934 (“Exchange Act”) Release No. 77744 (April 29, 2016), File No. SR-MSRB-2016-04 (Mar. 1, 2016)

² Shortening the Settlement Cycle: The Move to T+2, available at, <http://www.ust2.com/pdfs/ssc.pdf>. Other participating industry associations include: The Association of Global Custodians, The Association of Institutional Investors, The Securities Transfer Association, Inc., and The Depository Trust & Clearing Corporation (DTCC).



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equities, corporate and municipal bonds, and unit investment trust trades.³ The ISC's white paper identified all SEC and self-regulatory organization (SRO) rule changes that the ISC believed would be necessary to support a T+2 settlement cycle.

On June 18, 2015, concurrent with the white paper, SIFMA and ICI jointly submitted a letter to SEC Chair Mary Jo White to express support for the industry's efforts "to shorten the settlement cycle for equities, corporate and municipal bonds, unit investment trusts and financial instruments comprised of these products traded on the secondary market."⁴ The ICI/SIFMA letter specifically identified MSRB Rule G-12(b)(ii)(B)-(D) and Rule G-15(b)(ii)(B)-(C), as essential to facilitating the move to T+2, because, prior to the amendments, these rules defined regular-way settlement as occurring on T+3. As generally noted in ISC's white paper, the migration to T+2 settlement is expected to provide significant benefits to the financial industry broadly. The benefits to the industry include the mitigation of counterparty risk, a decrease in margin requirements for National Securities Clearing Corporation's (NSCC) clearing members, a reduction in pro-cyclical margin and liquidity demands especially during periods of market volatility, and an increase in global settlement harmonization by aligning the U.S. markets with other major markets, such as the European Union.⁵

Description of Amendments

Proposed Amendments to MSRB Rules G-12 and G-15

MSRB Rule G-12, on uniform practice, establishes uniform industry practices for processing, clearance and settlement of transactions in municipal securities between a broker, dealer or municipal securities dealer and any other broker, dealer or municipal securities dealer. Rule G-12(b)(ii), on settlement dates, defines "regular way" settlement as occurring on a T+3 basis. The amendments amend Rule G-12(b)(ii)(B)-(D) to shorten the

³ *Id.*

⁴ See Letter from Paul Schott Stevens, President & CEO, ICI ("Stevens"), and Kenneth E. Bentsen, Jr., President and CEO, SIFMA ("Bentsen"), to Mary Jo White, Chair, SEC (June 18, 2015) ("ICI/SIFMA letter").

⁵ See Equity Settlement Cycle for Top 10 Exchanges by Market Capitalization, Figure 2, page 9 (depicting global settlement harmonization for equities pre- and post-migration to T+2), available at, <http://www.ust2.com/pdfs/ssc.pdf>.

settlement period by one business day and define “regular way” settlement as occurring on a T+2 basis.

MSRB Rule G-15, on confirmations, clearance, settlement and other uniform practice requirements, requires municipal securities brokers and municipal securities dealers to provide customers with written confirmations of transactions, containing specified information; and prescribes certain uniform practice procedures for dealers that transact municipal securities business with customers. Rule G-15(b)(ii), on settlement dates, likewise defines “regular way” settlement as occurring on a T+3 basis. The amendments amend Rule G-15(b)(ii)(B)-(C) to define “regular way” settlement as occurring on a T+2 basis.

Technical Amendments

The MSRB also made technical changes to Rules G-12(b)(i)(B), G-15(b)(i)(B) and G-15(g)(ii)(B). Rules G-12(b)(i)(B) and G-15(b)(i)(B) were amended to replace the reference to “National Association of Securities Dealers, Inc.” with the “Financial Industry Regulatory Authority.” Rule G-15(g)(ii)(B) was also revised to replace the reference to “NASD Conduct Rule 2260(g),” which is retired, and replaced with the current relevant rule, “FINRA Rule 2251(g).”

Compliance Date

Both the ISC and the ICI/SIFMA letter identified Exchange Act Rule 15c6-1(a) as the primary SEC rule that would need to be amended to facilitate the industry’s transition to T+2. Exchange Act Rule 15c6-1 defines regular-way settlement as occurring on T+3 for equities and corporate bonds. Although Exchange Act Rule 15c6-1 does not apply to transactions in municipal securities, the MSRB has previously stated that the regular-way settlement cycle for municipal securities transactions in the secondary markets should be consistent with that for equity and corporate bond transactions.⁶ Among other reasons, this ensures that investors will not encounter differing settlement cycles when replacing equity or corporate bonds with municipal securities. The MSRB will coordinate implementation of a T+2 regular-way settlement cycle for municipal securities transactions with other securities regulators’ implementation of a T+2 regular-way settlement cycle for equities and corporate bonds, which is contingent on the SEC adopting amendments to Exchange Act Rule 15c6-1(a) to establish T+2 as the standard for regular-way settlement.

⁶ See, e.g., “T+3 Settlement, Amendments Filed: Rules G-12 and G-15,” MSRB Reports, Vol. 14, No. 4 (August 1994) at 3; and “Report of the Municipal Securities Rulemaking Board on T+3 Settlement for the Municipal Securities Market” (March 17, 1994).

Therefore, the compliance date of the amendments is not yet determined and will be announced by the MSRB in a notice published on the MSRB website, which date will correspond with the industry's transition to a T+2 regular-way settlement.

May 2, 2016

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Text of Amendments*

Rule G-12: Uniform Practice

(a) No change.

(b) *Settlement Dates*.

(i) *Definitions*. For purposes of this rule, the following terms shall have the following meanings:

(A) *Settlement Date*. The term "settlement date" shall mean the day used in price and interest computations, which shall also be the day delivery is due unless otherwise agreed by the parties.

(B) *Business Day*. The term "business day" shall mean a day recognized by the ~~National Association of Securities Dealers, Inc.~~ Financial Industry Regulatory Authority as a day on which securities transactions may be settled.

(ii) *Settlement Dates*. Settlement dates shall be as follows:

(A) for "cash" transactions, the trade date;

(B) for "regular way" transactions, the ~~third~~ second business day following the trade date;

(C) for "when, as and if issued" transactions, a date agreed upon by both parties, which date: (1) with respect to transactions required to be compared in an automated comparison system under rule G-12(f)(i), shall not be earlier than two business days after notification of initial settlement date for the issue is provided to the registered clearing agency by the managing underwriter for the issue as required by rule G-34(a)(ii)(D)(2); and (2) with respect to transactions not eligible for automated comparison, shall not be earlier than the

* Underlining indicates new language; strikethrough denotes deletions.

~~third~~ second business day following the date that the confirmation indicating the final settlement date is sent; and

(D) for all other transactions, a date agreed upon by both parties, *provided, however*, that a broker, dealer or municipal securities dealer shall not effect or enter into a transaction for the purchase or sale of a municipal security (other than a "when, as and if issued" transaction) that provides for payment of funds and delivery of securities later than the ~~third~~ second business day after the date of the transaction unless expressly agreed to by the parties, at the time of the transaction.

(c) – (j) No change.

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Rule G-15: Confirmation, Clearance, Settlement and Other Uniform Practice Requirements with Respect to Transactions with Customers

(a) No change.

(b) *Settlement Dates.*

(i) Definitions. For purposes of this rule, the following terms shall have the following meanings:

(A) Settlement Date. The term "settlement date" shall mean the day used in price and interest computations, which shall also be the day delivery is due unless otherwise agreed by the parties.

(B) Business Day. The term "business day" shall mean a day recognized by the ~~National Association of Securities Dealers, Inc.~~ Financial Industry Regulatory Authority as a day on which securities transactions may be settled.

(ii) Settlement Dates. Settlement dates shall be as follows:

(A) for "cash" transactions, the trade date;

(B) for "regular way" transactions, the ~~third~~ second business day following the trade date;

(C) for all other transactions, a date agreed upon by both parties; *provided, however*, that a broker, dealer or municipal securities dealer shall not effect or enter into a transaction for the purchase or sale of a municipal security (other than a "when, as and if issued" transaction) that provides for payment of funds and delivery of securities later than the ~~third~~ second business day after the date of the transaction unless expressly agreed to by the parties, at the time of the transaction.

(c) – (f) No change.

(g) *Forwarding Official Communications*

(i) No change.

(ii) In determining whether reasonable efforts have been made to retransmit official communications, the following considerations are relevant:

(A) No change.

(B) *Compensation.* A broker, dealer or municipal securities dealer shall not be required by this rule to retransmit official communications without an offer of adequate compensation. If compensation is explicitly offered in or with the official communication, the broker, dealer or municipal securities dealer shall effect the retransmission and seek compensation concurrently; provided, however, that if total compensation would be more than \$500.00, the broker, dealer or municipal securities dealer may, in lieu of this procedure, promptly contact the party offering compensation, inform it of the amount of compensation required, obtain specific agreement on the amount of compensation and wait for receipt of such compensation prior to proceeding with the retransmission. In determining whether compensation is adequate, the broker, dealer or municipal securities dealer shall make reference to the suggested rates for similar document transmission services found in “Suggested Rates of Reimbursement” for expenses incurred in forwarding proxy material, annual reports, information statements and other material referenced in ~~NASD Conduct Rule 2260(g)~~ FINRA Rule 2251(g), taking into account revisions or amendments to such suggested rates as may be made from time to time.

(C) – (F) No change.

(iii) No change.