



March 4, 2016

1909 K Street NW • Suite 510
Washington, DC 20006
202.204.7900
www.bdamerica.org

VIA ELECTRONIC MAIL

Ronald W. Smith
Corporate Secretary
Municipal Securities Rulemaking Board
1300 I Street, NW Suite 1000
Washington, DC 20005

RE: MSRB Notice 2016-02: Request for Comment on Amendments to MSRB Rule G-12 on Close-Out Procedures

Dear Mr. Smith:

On behalf of the Bond Dealers of America (“BDA”), I am pleased to submit this letter in response to Municipal Securities Rulemaking Board (“MSRB”) Notice 2016-02, on its proposed amendments (“Proposed Amendments”) to Rule G-12, on uniform practice, to update the close-out procedures to specifically require a municipal securities transaction to be closed-out no later than 30 calendar days after the transaction’s original settlement date. BDA is the only DC-based group representing the interests of middle-market securities dealers and banks focused on the U.S. fixed income markets and we welcome this opportunity to present our comments.

The BDA supports the MSRB’s amendments to make the close-out process a requirement

BDA understands these regulatory changes are part of a broader, industry-wide initiative supported by the Securities and Exchange Commission (“SEC”) and the Financial Industry Regulatory Authority (“FINRA”) to improve overall market efficiencies. Additional changes, including the initiative to shorten the settlement cycle may also reduce the amount of inter-dealer fails. The BDA urges the MSRB to consider the following three requests related to the Proposed Amendments which we expand upon below: 1) Provide more detailed guidance for comparable securities or alternatives for municipal securities which do not trade frequently 2) Provide additional guidance with respect to the operational and implementation of the proposed amendments, and 3) Provide a 180-calendar day grace period for current outstanding inter-dealer fails to allow dealers ample time to resolve aged fails.

We appreciate the common sense approach the MSRB has taken in regard to the proposed amendments. Presently, there are three remedies available if the selling dealer fails to deliver to the purchasing dealer. While these remedial options provide a basic framework for the purchasing dealer to initiate a close-out, they could be improved to provide dealers with more latitude, which would further benefit municipal securities investors.

Concerns with the proposals three options for closing out a transaction

As you know, the municipal securities marketplace is unique and the reality is that some securities trade infrequently. For example, just a few investors may hold the preponderance of a small

serial maturity within a larger issuance. For the purposes of close-out procedures this creates issues that are unique to the municipal securities market that do not exist in the corporate taxable bond market or equity market.

A dealer may not be able to exercise purchaser’s “Option One” if the securities are not available for purchase in the market within the proposed close-out timeframes. If that is the case, the dealer would be able to choose “Option Two”, to “accept from the seller a ‘comparable’ security,” which creates the customer-focused question of finding a ‘comparable’ security that is acceptable to the investor’s particular interests or investment strategy. The proposed amendments to Rule G-12 are helpful to BDA members and other dealers in providing a shorter period closer to the original trade date for firms to find matching or comparable bonds. However, it is important to note that BDA members will incur costs to find such bonds, to purchase the matching or comparable bonds, or to use CNS/DTCC to find a particular security, any or all of which could potentially be cost prohibitive and especially to the small and middle market dealer.

Finally, “Option Three” is focused on the inter-dealer transaction and requires the selling dealer to repurchase the securities back from the purchasing dealer for a price that includes accrued interest and any changes in market price. The BDA believes the MSRB should add to “Option Three,” a requirement for the selling dealer to deliver securities to its customer within 30 days. If the purchasing dealer cannot deliver the securities to its customer within the specified timeframe, the purchasing dealer must repurchase the bonds from its customer at a price that includes accrued interest and any change in market price. See Figure 1 below:

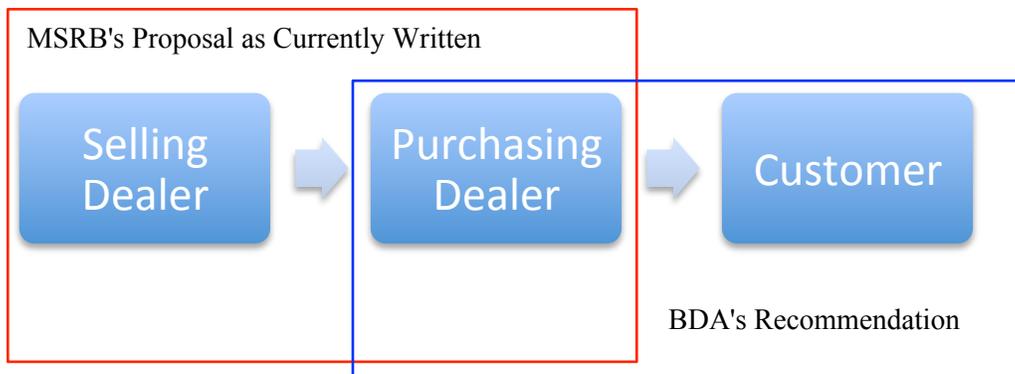


Figure 1 – It is the selling dealer failing to deliver to the purchasing dealer, who sold to the customer. It is the sale from the purchasing dealer to the customer that is being covered by the recommended language from the BDA to Option Three.

Implementation and Operational Concerns

Operationally speaking, BDA members generally support this initiative, which should decrease the costs and risks associated with interdealer fails. BDA-member firms do have concerns with how the proposal’s close-out processes will interact with current systems in place and seek additional clarity for two systems in particular.

First, the Reconfirmation and Pricing Service (“RECAPS”) is NSCC’s automated fail clearance system for eligible securities. BDA member firms have concerns that applying a municipal security fail through the RECAPS process raises questions for firms about which settlement date should be used for calculating the time frames for close-outs. The RECAPS process is intended to reset the settlement date of a fail for the purposes of determining the age of the fail to calculate the net capital computation under 15c3-3. While footnote 10 in MSRB Notice 2016-02 states, “for close-out purposes, dealers should continue to use the original settlement date for calculating applicable time frames,” we urge this information be featured more prominently within the rule itself or provided in future supplementary guidance.

Second, the Automated Customer Account Transfer Service (“ACATS”) system facilitates the transfer of securities from one trading account to another at a different brokerage firm or bank. BDA member firms would like to see additional information in G-12, or supplementary rule guidance, on how ACATS fails should be resolved. The proposed timeframes in the proposed amendments to Rule G-12 work well for ACATS generally, but the terminology in the rule, as currently drafted, does not fit the reality for transfer scenarios, as there is no trade date for a transfer.

BDA recommends 180-calendar day grace period

BDA recommends the MSRB provide a 180-day grace period to allow the municipal markets industry ample time to resolve aged fails. In reality, every fail can be closed out with a buy back. However, negotiating the terms of the buy back is potentially difficult, especially for very aged fails. Dealers may experience the difficulty in determining a “fair” price for a buy back, or at least a price acceptable to the selling and purchasing dealer, which could further contribute to a large loss when executing a buy back transaction. Furthermore, dealers would have to negotiate to determine who would take the loss, or how it would be apportioned between each dealer. There is even additional complexity when you add a retail customer to this scenario.

Therefore, BDA recommends that MSRB provide a 180-day period for dealers to make reasonable efforts to close out existing inter-dealer fails, which we believe will give the industry time to work through the complex process we describe above.

Again, we appreciate the opportunity to comment on this proposal and we would be happy to answer any questions you have in relation to our recommendations.

Sincerely,



Mike Nicholas
Chief Executive Officer