



Municipal Securities Rulemaking Board

July 25, 2016

Mr. Brent J. Fields
Secretary
U.S. Securities and Exchange Commission
100 F Street, NE
Washington, DC 20540-1090

Re: Amendment No. 1 to SR-MSRB-2016-07

Dear Secretary:

On May 11, 2016, the Municipal Securities Rulemaking Board (“MSRB”) filed with the Securities and Exchange Commission (“SEC”) a proposed rule change consisting of amendments to MSRB Rule G-12, on Uniform Practice, Regarding Close-Out Procedures for Municipal Securities (the “original proposed rule change”). The SEC published notice of the original proposed rule change on May 25, 2016,¹ and notice was then published in the Federal Register on June 1, 2016.² The SEC received three comment letters on the original proposed rule change. In response to those comments on July 25, 2016 the MSRB filed a partial amendment (“Amendment No. 1”) to the original proposed rule change to shorten the close-out deadline from 20 calendar days to 10 calendar days with an allowance for an additional 10 calendar day extension at the buyer’s discretion, as well as technical corrections to the rule text.

A copy of Amendment No. 1 is attached to this letter, and Exhibit 4 thereto shows changes to the original proposed rule text.

If you have any questions regarding this matter, please contact me or Gail Marshall, Associate General Counsel, at (202) 838-1500.

Sincerely,

A handwritten signature in black ink, appearing to read "Michael Cowart", written in a cursive style.

Michael Cowart
Deputy Director, Professional Qualifications –
Assistant General Counsel

¹ See Exchange Act Release No. 77903 (May 25, 2016).

² See 81 FR 35111 (June 1, 2016).

The Municipal Securities Rulemaking Board (“MSRB”) is filing this partial amendment (“Amendment No. 1”) to File No. SR-MSRB-2016-07, originally filed with the Securities and Exchange Commission (the “Commission”) on May 11, 2016, with respect to a proposed rule change regarding close-out procedures for municipal securities (the “original proposed rule change” and, together with Amendment No. 1, the “proposed rule change”). The SEC published notice of the original proposed rule change on May 25, 2016,¹ and notice was then published in the Federal Register on June 1, 2016.² The SEC received three comment letters in response to the original proposed rule change.³ The MSRB intends to implement the proposed rule change 90 days following the date of Commission approval.

The original proposed rule change consists of proposed amendments to MSRB Rule G-12, on Uniform Practice, Regarding Close-Out Procedures for Municipal Securities. Currently, MSRB Rule G-12(h) does not require a purchasing dealer to initiate a close-out or to execute a close-out notice it has initiated nor does it provide the selling dealer with the right to force a close-out of the transaction. Rule G-12(h) provides the close-out options of substitution and mandatory repurchase because municipal securities often are not available for a buy-in within a reasonable period of time. If the purchasing dealer chooses not to initiate a close-out within 90 business days of the original contract settlement date (and ultimately execute it) then that dealer loses its right to use the Rule G-12(h) procedure, and the transaction remains open until it is resolved by agreement of the parties or through arbitration. Until the transaction is closed-out, the selling dealer is subject to market risk for any increase in the price of the municipal securities.

The MSRB submitted the original proposed rule change to modernize Rule G-12 and significantly compress the timing for initiating and completing a close-out by allowing a close-out notice to be issued the day after the purchaser’s original settlement date, with the last day by which the purchasing dealer must complete a close-out on an open transaction being reduced from an optional 90 day close-out period, to a mandatory close-out within 20 calendar days.

In the comments received to the original proposed rule change, SIFMA and BDA collectively suggest tightening the time frame to resolve a fail within 10 calendar days, with SIFMA emphasizing that “failed transactions don’t get better with age.”⁴ Additionally, both

¹ See Exchange Act Release No. 77903 (May 25, 2016).

² See 81 FR 35111 (June 1, 2016).

³ See comment letters submitted to the SEC by Michael Nicholas, CEO, Bond Dealers of America (“BDA”), dated June 22, 2016; David T. Bellaire, Esq., Executive Vice President & General Counsel, Financial Services Institute (“FSI”), dated June 22, 2016; and Leslie Norwood, Managing Director and Associate General Counsel, the Securities Industry and Financial Markets Association (“SIFMA”), dated June 23, 2016.

⁴ SIFMA letter dated June 23, 2016.

SIFMA and BDA suggest that the rule permit the buyer to grant the seller a one-time 10 calendar day extension, for an aggregate total of 20 calendar days to close-out an inter-dealer fail.⁵

In response to these comments the MSRB is proposing to amend the original proposed rule change to require firms to resolve an inter-dealer fail from 20 calendar days to 10 calendar days and permit the buyer to grant the seller a one-time 10 calendar day extension, which would allow the buyer flexibility, while still ensuring that inter-dealer fails would be closed-out in a maximum of 20 calendar days. The MSRB stated in its original filing with the SEC that “a more timely resolution of inter-dealer fails would ultimately benefit customers by providing greater certainty that their fully paid for securities are in fact owned in their account and not allocated to a firm short, and would also benefit dealers by reducing the risk and costs associated with inter-dealer fails.”⁶ The MSRB believes that 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 inter-dealer fails.

The MSRB believes the Commission has good cause, pursuant to Section 19(b)(2) of the Securities and Exchange Act of 1934, for granting accelerated approval of Amendment No. 1. Specifically, the only substantive change to the proposal seeks to shorten the close-out period from 20 calendar days to 10 calendar days, with the buyer having an option to grant the seller a one-time 10 calendar day extension, which was made to address concerns raised during the comment period. In light of the goal of the original proposal to compress the timing for initiating and completing a close-out, the revisions are consistent with the original proposal and are unlikely to be controversial.

The changes made by Amendment No. 1 to the original proposed rule change are indicated as attached in Exhibit 4. Material proposed to be added is underlined. Material proposed to be deleted is enclosed in brackets.

The text of the proposed rule change is attached as Exhibit 5. Material proposed to be added is underlined. Material proposed to be deleted is enclosed in brackets.

⁵ The MSRB also received comments regarding self-directed customer accounts and the Automated Customer Account Transfer Service (“ACATS”) process. Both of the comments received are beyond the scope of the original proposed rule change and current proposed rule change.

⁶ See supra n.1.

Rule G-12: Uniform Practice

(a) – (g) No change.

(h) *Close-Out*. Transactions which have been compared or otherwise agreed upon by both parties but which have not been completed shall be closed out in accordance with this section, or cancelled by the parties, no later than [20] 10 calendar days after settlement date.

(i) *Close-Out by Purchaser*. With respect to a transaction which has not been completed by the seller according to its terms and the requirements of this rule, the purchaser may close out the transaction in accordance with the following procedures:

(A) *Notice of Close-Out*. If the purchaser elects to close out a transaction, the purchaser shall, not earlier than the first business day following the purchaser's original transaction settlement date, notify the seller via an inter-dealer communication system of the registered clearing agency through which the transaction was compared of the purchaser's intention to close out the transaction ("notice").

(1) The purchaser's notice shall state:

(a) No change.

(b) the period of time, during which the purchaser intends to execute the close-out transaction, provided that the close-out transaction initiated by the notice (or subsequent notices) must be completed and settled no later than the [twentieth business] tenth calendar day following the purchaser's original transaction settlement date; and

(c) No change.

(B) *Retransmittal*. Any party receiving a notice of close-out may retransmit the notice to another broker, dealer or municipal securities dealer from whom the securities are due ("obliged party"). The retransmitting party shall, not later than 5:15 p.m. EST of the first business day following its receipt of the notice from the originating party:

(1) No change.

(2) retransmit the notice to the obliged party, which shall contain the requirements specified in section (C)(2) below; and

(3) No change.

(C) *Contents of Notices.* Notices sent in accordance with the requirements of subparagraphs (A) or (B) above shall contain the following information:

(1) The notice of close-out required under subparagraph (A) above shall set forth:

(a) – (i) No change.

(j) the name and telephone number of the person at the broker, dealer, or municipal securities dealer originating the notice to contact concerning the close-out.

(2) The notice of retransmittal required under subparagraph (B) above shall set forth:

(a) – (j) No change.

(k) the name and telephone number of the person at the broker, dealer, or municipal securities dealer retransmitting the notice to contact concerning the retransmittal.

(3) The notice of extension of dates required under subparagraph (B) above shall set forth:

(a) – (i) No change.

(j) the name and telephone number of the person at the broker, dealer, or municipal securities dealer retransmitting the notice to contact concerning the close-out.

(D) No change.

(E) *Purchaser's Options.* If the securities described in the notice of close-out are not delivered to the originating purchaser by the date specified in the original notice, or the extended date resulting from a retransmittal, such purchaser may, at its discretion, grant the seller one 10 calendar day extension. [close out the transaction in accordance with the terms of the notice.] To close out a transaction in accordance with the terms of the notice as provided herein the purchaser may, at its option, take one of the following actions:

(1) – (3) No change.

A purchaser executing a close-out shall, upon execution, notify the selling dealer for whose account and liability the transaction was closed out, stating the means of close-out utilized. The purchaser shall immediately thereafter confirm such notice in writing, sent return receipt requested, and forward a copy of the confirmation of the executed transaction. A retransmitting party shall give

immediate notice of the execution of the close-out, in accordance with the procedure set forth herein, to the party to whom it retransmitted the notice.

A close-out will operate to close out all transactions covered under retransmitted notices. Any moneys due on the transaction, or on the close-out of the transaction, shall be forwarded to the appropriate party within five business days of the date of execution of the close-out notice. A buy-in may be executed from a long position in customers' accounts maintained with the party executing the buy-in or, with the agreement of the seller, from the purchaser's contra-party. In all cases, the purchaser must be prepared to defend the price at which the close-out is executed relative to market conditions at the time of the execution.

If the purchasing dealer has multiple transactions in fail status with multiple counterparties, the purchasing dealer may utilize the FIFO (first-in-first-out) method for determining the contract date for the failing quantity.

(F) No change.

(ii) Close-Out by Seller. If a seller makes good delivery according to the terms of the transaction and the requirements of this rule and the purchaser rejects delivery, the seller may close out the transaction in accordance with the following procedures:

(A) No change.

(B) *Content of Notice*. The written notice sent in accordance with the requirements of subparagraph (A) above shall set forth:

(1) – (8) No change.

(9) the date by which the delivery of the securities must be accepted, which shall be completed within [20] 10 calendar days; and

(10) the name and telephone number of the person at the broker, dealer, or municipal securities dealer originating the notice to contact regarding the close-out.

(C) – (D) No change.

(iii) – (iv) No change.

(i) – (j) No change.

Rule G-12: Uniform Practice

(a) – (g) No change.

(h) *Close-Out*. Transactions which have been [confirmed] compared or otherwise agreed upon by both parties but which have not been completed [may] shall be closed out in accordance with this section, or [as otherwise agreed] cancelled by the parties, no later than 10 calendar days after settlement date.

(i) *Close-Out by Purchaser*. With respect to a transaction which has not been completed by the seller according to its terms and the requirements of this rule, the purchaser may close out the transaction in accordance with the following procedures:

(A) *Notice of Close-Out*. If the purchaser elects to close out a transaction [in accordance with this paragraph (i)], the purchaser shall, not earlier than the [fifth] first business day following the purchaser's original transaction settlement date, notify the seller [by telephone of the purchaser's intention to close out the transaction] via an inter-dealer communication system of the registered clearing agency through which the transaction was compared of the purchaser's intention to close out the transaction ("notice").

(1) The purchaser's notice shall state [that unless the transaction is completed by a specified]:

(a) the date and time[,], by which the transaction must be completed, which shall not be earlier than 5:15 p.m. EST [the close] of the [tenth] third business day following the date [the telephonic] notice is given (the [fifth] first business day, in the case of a second or subsequent notice):[,]

(b) [the transaction may be closed out in accordance with this section at any time during] the period of time, during which the purchaser intends to execute the close-out transaction, provided that the close-out transaction initiated by the notice (or subsequent notices) must be completed and settled no later than the tenth calendar day following the purchaser's original transaction settlement date; and [which shall not be more than five business days, specified by the purchaser for such purpose. The purchaser shall immediately thereafter send, return receipt requested, a written notice of close-out to the seller. Such notice shall]

(c) contain the information specified in item (1) of subparagraph (C) below.

(B) *Retransmittal*. Any party receiving a notice of close-out may retransmit the notice to another [party] broker, dealer or municipal securities dealer from whom the securities are due (“obliged party”). The retransmitting party shall, not later than 5:15 p.m. EST of the first business day following its receipt of the [telephone] notice from the originating party:

(1) provide the obliged party [of close-out, notify the party to whom it is retransmitting by telephone of its intention to retransmit such notice, specifying] the name of the originating party and note the dates applicable to the notice are extended by one business day;

(2) retransmit the notice to the obliged party, which shall contain the requirements specified in section (C)(2) below; and [originator and the applicable dates for delivery and effectiveness of the notice. The retransmitting party shall immediately thereafter send, return receipt requested, a written notice of retransmittal which shall contain the information specified in item (2) of subparagraph (C) below. The first such retransmittal shall extend the dates for close-out by five business days, and the first retransmitting party shall specify the extended dates on its notice of retransmittal.]

(3) notify the originating party, of the retransmittal notice of extension dates, which shall include the information specified in section (C)(3) below. [The first retransmitting party shall, on the date telephone notice of the retransmittal is given, notify the purchaser originating the notice by telephone of the extended dates and immediately thereafter send, return receipt requested, a notice of extension of dates which shall contain the information specified in item (3) of subparagraph (C) below. Any party subsequently retransmitting such notice shall, on the date telephonic notice of the retransmittal is given, notify the purchaser originating the notice by telephone of such retransmittal, and immediately thereafter send a copy of the retransmittal notice to such originating purchaser.]

(C) *Contents of Notices*. [Written] N[n]otices sent in accordance with the requirements of subparagraphs (A) or (B) above shall contain the following information:

(1) The notice of close-out required under subparagraph (A) above shall set forth:

(a) the [name and address] identity of the broker, dealer or municipal securities dealer originating the notice;

(b) the [name and address] identity of the broker, dealer or municipal securities dealer to whom the notice is being sent;

- (c) the [name of the person] contact to whom the originator provided the required [telephonic] notice;
- (d) the date of such [telephonic] notice;
- (e) the par value and description of the securities involved in the transaction with respect to which the close-out notice is given;
- (f) the trade date and settlement date of the transaction;
- (g) the price and total dollar amount of the transaction;
- (h) the date by which the securities must be received by the originating dealer, which shall be completed within 10 calendar days of the purchaser's original transaction settlement date;
- (i) the date or dates during which the notice of close-out may be executed; and
- (j) the name and telephone number of the person at the broker, dealer, or municipal securities dealer originating the notice to contact concerning the close-out.

(2) The notice of retransmittal required under subparagraph (B) above shall set forth:

- (a) the [name and address] identity of the broker, dealer or municipal securities dealer retransmitting the notice;
- (b) the [name and address] identity of the broker, dealer or municipal securities dealer to whom the notice is being retransmitted;
- (c) the [name] identity of the broker, dealer or municipal securities dealer originating the notice;
- (d) the [name of the person] contact to whom the retransmitting party provided the required [telephonic] notice;
- (e) the date of such [telephonic] notice;
- (f) the par value and description of the securities involved in the transaction with respect to which the retransmittal notice is given;
- (g) the trade date and settlement date of the transaction;
- (h) the price and total dollar amount of the transaction;

(i) the date by which the securities must be received by the dealer originating the notice (as extended due to the retransmittal);

(j) the date or dates during which the notice of close-out may be executed (as extended due to the retransmittal); and

(k) the name and telephone number of the person at the broker, dealer, or municipal securities dealer retransmitting the notice to contact concerning the retransmittal.

(3) The notice of extension of dates required under subparagraph (B) above shall set forth:

(a) the [name and address] identity of the broker, dealer or municipal securities dealer originating the notice of close-out;

(b) the [name and address] identity of the broker, dealer or municipal securities dealer retransmitting the notice;

(c) the [name] identity of the broker, dealer or municipal securities dealer to whom the notice is being retransmitted;

(d) the [name of the person] contact to whom the retransmitting party provided the required telephonic notice of the extension of dates;

(e) the date of such [telephonic] notice;

(f) the par value and description of the securities involved in the transaction with respect to which the notice is given;

(g) the date specified by the originating dealer as the date by which delivery of such securities must be made;

(h) the date by which such delivery must be made, as extended due to the retransmittal;

(i) the effective date or dates for the notice of close-out, as extended due to the retransmittal; and

(j) the name and telephone number of the person at the broker, dealer, or municipal securities dealer retransmitting the notice to contact concerning the close-out.

(D) Seller's Responsibilities. Once the seller receives a notice it is required to use its best efforts to locate the securities referenced in the notice.

([D]E) *Purchaser's Options*. If the securities described in the notice of close-out are not delivered to the originating purchaser by the date specified in the original notice, or the extended date resulting from a retransmittal, such purchaser may, [close out the transaction in accordance with the terms of the notice.] at its discretion, grant the seller one 10 calendar day extension. To close out a transaction in accordance with the terms of the notice as provided herein the purchaser may, at its option, take one of the following actions:

- (1) purchase ("buy-in") at the current market all or any part of the securities necessary to complete the transaction, [for the account and liability of the seller;] with the seller bearing any burden from any change in the market price, and any benefit from any change in the market price remaining with the purchaser; or
- (2) accept from the seller in satisfaction of the seller's obligation under the original contract (which shall be concurrently cancelled) a transaction in [the delivery of] municipal securities which are comparable to those originally bought in quantity, quality, yield or price, and maturity, with any additional expenses or any additional cost of acquiring such substituted securities being borne by the seller; or
- (3) require the seller to repurchase the securities in a transaction on terms which provide that the seller pay an amount which includes accrued interest and bear the burden of any change in market price or yield.

A purchaser executing a close-out shall, upon execution, notify the selling dealer for whose account and liability the transaction was closed out [by telephone}, stating the means of close-out utilized. The purchaser shall immediately thereafter confirm such notice in writing, sent return receipt requested, and forward a copy of the confirmation of the executed transaction. A retransmitting party shall give immediate notice of the execution of the close-out, in accordance with the procedure set forth herein, to the party to whom it retransmitted the notice.

A close-out will operate to close out all transactions covered under retransmitted notices. Any moneys due on the transaction, or on the close-out of the transaction, shall be forwarded to the appropriate party within [ten] five business days of the date of execution of the close-out notice. A buy-in may be executed from a long position in customers' accounts maintained with the party executing the buy-in or, with the agreement of the seller, from the purchaser's contra-party. In all cases, the purchaser must be prepared to defend the price at which the close-out is executed relative to market conditions at the time of the execution.

If the purchasing dealer has multiple transactions in fail status with multiple counterparties, the purchasing dealer may utilize the FIFO (first-in-first-out) method for determining the contract date for the failing quantity.

[(E) *Close-Out Not Completed*. If a close-out pursuant to a notice of close-out is not completed in accordance with the terms of the notice and the provisions of this rule, the notice shall expire. Additional close-out notices may be issued, provided that a close-out procedure with respect to a transaction may not be initiated later than the ninetieth business day following the settlement date of such transaction, regardless of the number of close-out notices issued. Notwithstanding the foregoing, in the case of a transaction on which a delivery of securities has been reclaimed pursuant to the provisions of subparagraphs (g)(iii)(C) or (g)(iii)(D) of this rule and which remains uncompleted, the purchaser may initiate one or more close-out procedures with respect to such transaction at any time during a period of fifteen business days following the date of reclamation. The first such procedure shall be considered an initial procedure for purposes of subparagraph (A) above.]

[(F) *Completion of Transaction*. If, at any time prior to the execution of a close-out pursuant to this paragraph (i), the seller, or any subsequent selling party to whom a notice has been retransmitted, can complete the transaction within two business days, such party shall give immediate notice to the purchaser originating the notice of close-out that the securities will be delivered within such time period. If the originating purchaser receives such notice, it shall not execute the close-out for two business days following the date of such notice; the period specified for the execution of the close-out shall be extended by two business days or, in the event that the notice is given on the last day specified for execution of the close-out, by three business days. Delivery of the securities in accordance with such notice shall cancel the close-out notice outstanding with respect to the transaction.]

[(G)]E) *"Cash" Transactions*. The purchaser may close out transactions made for "cash" or made for or amended to include guaranteed delivery at the close of business on the day delivery is due.

(ii) Close-Out by Seller. If a seller makes good delivery according to the terms of the transaction and the requirements of this rule and the purchaser rejects delivery, the seller may close out the transaction in accordance with the following procedures:

(A) *Notice of Close-Out*. If the seller elects to close out a transaction in accordance with this paragraph (ii), the seller shall at any time not later than the close of business on the [fifth] first business day following receipt by the seller of notice of the rejection, notify the purchaser [by telephone] via an inter-dealer communication system of the registered clearing agency through which the transaction was compared of the purchaser's intention to close out the transaction of the seller's intention to close out the transaction.

(1) The seller's notice shall state:

(a) the [that unless the transaction is completed by a specified] date and time[,] by which the transaction must be completed which shall not be earlier than 5:15 p.m. EST of the close of the business day following the date the [telephonic] notice is given, the transaction may be closed out in accordance with this section[.]; and [The seller shall immediately thereafter send, return receipt requested, a written notice of close-out to the purchaser.]

(b) [Such notice shall] contain the information specified in subparagraph (B) below, and shall be accompanied by a copy of the purchaser's confirmation of the transaction to be closed out or other [written] evidence of the contract between the parties.

(B) *Content of Notice.* The written notice sent in accordance with the requirements of subparagraph (A) above shall set forth:

- (1) the [name and address] identity of the broker, dealer or municipal securities dealer originating the notice;
- (2) the [name and address] identity of the broker, dealer or municipal securities dealer to whom the notice is being sent;
- (3) the [name of the person] contact to whom the originator provided the required telephonic notice;
- (4) the date of such [telephonic] notice;
- (5) the par value and description of the securities involved in the transaction with respect to which the close-out notice is given;
- (6) the trade date and settlement date of the transaction;
- (7) the price and total dollar amount of the transaction;
- (8) the date of improper rejection of the delivery;
- (9) the date by which the delivery of the securities must be accepted, which shall be completed within 10 calendar days; and
- (10) the name and telephone number of the person at the broker, dealer, or municipal securities dealer originating the notice to contact regarding the close-out.

(C) *Execution of Close-Out.* Not earlier than the close of the business day following the date [telephonic] notice of close-out is given to the purchaser, the seller may sell out the transaction at the current market for the account and liability of the purchaser. A seller executing a close-out shall, upon execution,

notify the purchaser for whose account and liability the transaction was closed out by telephone. The seller shall immediately thereafter confirm such notice [in writing, sent return receipt requested,] and forward a copy of the confirmation of the executed transaction. Any moneys with any additional expenses or any additional cost due on the close-out of the transaction shall be forwarded to the appropriate party within [ten] five business days of the date of execution of the close-out notice.

(D) *Acceptance of Delivery*. In the event the transaction is completed by the date and time specified in the notice of close-out, the seller shall be entitled, upon [written] demand made to the purchaser, to recover from the purchaser all actual and necessary expenses incurred by the seller by reason of the purchaser's rejection of delivery.

(iii) *Close-Out Under Special Rulings*. Nothing herein contained shall be construed to prevent brokers, dealers or municipal securities dealers from closing out transactions as directed by a ruling of a national securities exchange, a registered securities association or an appropriate regulatory agency issued in connection with the liquidation of a broker, dealer or municipal securities dealer.

(iv) *Recordkeeping*. All records regarding the close-out transaction shall be maintained as part of the firm's books and records.

[(iv) *Procedures Optional*. Nothing herein contained shall be construed to require the parties to follow the close-out procedures herein specified if they otherwise agree.]

(i) – (j) No change.