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**Affected Rules**  
[Rule G-12](#); [Rule G-15](#)

## Request for Comment on Changes to MSRB Rules to Facilitate Shortening the Securities Settlement Cycle

### Overview

The Municipal Securities Rulemaking Board (MSRB) is seeking comment on draft amendments to 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. The purpose of these draft amendments is to facilitate shortening the settlement cycle for transactions in municipal securities. The draft amendments are being proposed in response to a securities industry-led initiative to shift from the current T+3 (trade date plus three days) regular-way settlement cycle to a T+2 (trade date plus two days) regular-way settlement cycle. This initiative is being led by the Industry Steering Committee (ISC) jointly chaired by the Investment Company Institute (ICI) and the Securities Industry and Financial Markets Association (SIFMA).

Comments to this request for comment should be submitted to the MSRB no later than December 10, 2015, and may be submitted in electronic or paper form. [Comments may be submitted electronically by clicking here.](#) Comments submitted in paper form should be sent to Ronald W. Smith, Corporate Secretary, Municipal Securities Rulemaking Board, 1900 Duke Street, Suite 600, Alexandria, Virginia 22314. All comments will be available for public inspection on MSRB's website.<sup>1</sup>

Questions about this notice should be directed to Barbara Vouté, Municipal Operations Advisor, Justin Pica, Director of Product Management, or Michael B. Cowart, Assistant General Counsel, at 703-797-6600.

<sup>1</sup> Comments generally are posted on the MSRB's website without change. For example, personal identifying information such as name, address, telephone number, or email address will not be redacted from submissions. Therefore, commenters should only submit information that they wish to make available publicly.



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## Background

The “regular-way” settlement cycle for U.S. equities, corporate bonds and municipal bonds currently is defined in the Securities and Exchange Commission (SEC) and MSRB rules as T+3 and has been unchanged since the shortening of the T+5 (trade date plus five days) settlement cycle in 1995.

In 2012, the Depository Trust and Clearing Corporation (DTCC) initiated an effort to shorten the U.S. settlement cycle and sponsored a cost-benefit analysis of shortening the settlement cycle to T+2 or T+1.<sup>2</sup> Following the results of this analysis, DTCC determined to pursue a change to a T+2 settlement cycle as an interim step before pursuing a change to T+1. In early 2014, DTCC received endorsements from the ICI and SIFMA for shortening the settlement cycle from T+3 to T+2. In April 2014, DTCC published a white paper stating its rationale for shortening the settlement cycle to T+2.<sup>3</sup>

In October 2014, DTCC formed the ISC to oversee the T+2 settlement cycle initiative. Supporting the efforts of the steering committee is a working group and sub-working group structure comprised of industry subject matter experts charged with identifying the technological, behavioral and regulatory changes that would be required to facilitate a transition to T+2.

In a letter to the SEC, the ISC identified both SEC and self-regulatory organization (SRO) rule changes that it believes would be necessary to support a T+2 settlement cycle.<sup>4</sup> The ISC recommended that the relevant regulatory organizations be able to confirm support of the transition to T+2 by the third quarter of 2015 and adopt applicable rule changes by the second quarter of 2016. The ISC expects this timeline to permit a securities industry-wide transition to T+2 by the third quarter of 2017. The MSRB announced its support of this initiative and its willingness to consider necessary rule changes, consistent with the decisions of other regulators.<sup>5</sup>

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<sup>2</sup> Cost Benefit Analysis of Shortening the Settlement Cycle (October 2012), <http://www.dtcc.com/news/2012/october/01/cost-benefit-analysis-of-shortening-the-settlement-cycle>.

<sup>3</sup> DTCC Recommends Shortening the U.S. Trade Settlement Cycle (April 2014), <http://www.dtcc.com/~media/Files/Downloads/WhitePapers/T2-Shortened-Cycle-WP.pdf>.

<sup>4</sup> Letter from Paul Schott Stevens, President and CEO, Investment Company Institute, and Kenneth E. Bentsen, Jr., President and CEO, Securities Industry and Financial Markets Association, to Mary Jo White, Chair, Securities and Exchange Commission (June 18, 2015).

<sup>5</sup> See e.g., MSRB Press Release: MSRB Holds Quarterly Meeting (August 3, 2015).

In June 2015, ISC sent a letter to the SEC, and copied the MSRB and other SROs, describing the ISC's recommendation and requesting that the SEC support the T+2 initiative.<sup>6</sup> In response to this letter, SEC Commissioners Michael S. Piwowar and Kara M. Stein released a statement in support of the T+2 initiative noting that "the Commission's Investor Advisory Committee encouraged the Commission and market participants to move forward on reducing the settlement cycle, which would improve investor protections and reduce systemic risks" and citing an interest in having the settlement cycle shortened "as soon as possible."<sup>7</sup>

On September 16, 2015, SEC Chair Mary Jo White sent a letter in response to the ISC letter noting she "strongly support[s] [the ISC's] efforts to shorten the settlement cycle from the third business day after the trade date to no later than the second business day ("T+2")."<sup>8</sup> Chair White stated that she supports the ISC's recommended implementation timeline and noted that she is "committed to considering regulatory changes necessary for this migration to proceed on a timetable that will permit the industry to complete its essential work by no later than the proposed goal of the third quarter of 2017." Further, Chair White stated that she has "requested that the SROs finalize [schedules of rule changes necessary to support a T+2 settlement cycle] by October 31, 2015." The MSRB developed such a schedule and believes requesting comment at this time will enable it to consider necessary rule changes within the timetable proposed by the ISC.

## MSRB Rule Changes

SEC Rule 15c6-1 currently defines regular-way settlement as occurring on T+3 for equities and corporate bonds. Although SEC Rule 15c6-1 does not apply to municipal securities, the MSRB has previously stated that the regular-way settlement cycle of municipal securities should be consistent with that of the

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<sup>6</sup> *Id.*

<sup>7</sup> Commissioners Michael S. Piwowar and Kara M. Stein, Public Statement Regarding Proposals to Shorten the Trade Settlement Cycle (June 29, 2015), <http://www.sec.gov/news/statement/statement-on-proposals-to-shorten-the-trade-settlement-cycle.html>.

<sup>8</sup> Letter from Mary Jo White, Chair, Securities and Exchange Commission, to Kenneth E. Bentsen, Jr., President and CEO, Securities Industry and Financial Markets Association, and Paul Schott Stevens, President and CEO, Investment Company Institute (September 16, 2015).

equity and corporate bond markets.<sup>9</sup> Among other reasons, this ensures that investors will not be faced with different settlement cycles when replacing equity or corporate debt with municipal securities.

This regulatory consistency is currently reflected in MSRB Rules G-12(b)(ii) and G-15(b)(ii), which define T+3 as the regular-way settlement cycle for municipal securities transactions. These rules were last changed in 1995 in coordination with changes made to SEC Rule 15c6-1 to facilitate the industry's initiative to shorten the settlement cycle from T+5 to T+3. The MSRB now proposes to amend MSRB Rules G-12(b)(ii)(B), G-12(b)(ii)(C), G-12(b)(ii)(D) and G-15(b)(ii)(B), G-15(b)(ii)(C) to define regular-way settlement as occurring on T+2. The draft amendments to MSRB Rules G-12 and G-15 are based on the ISC's recommendation and the SEC's support of a shift to a T+2 settlement cycle. The MSRB notes that the MSRB draft amendments to facilitate the transition to a T+2 settlement cycle will be dependent on SEC amendments to SEC Rule 15c6-1(a), which would establish T+2 as the standard for regular-way settlement cycle for equities and corporate bonds.

## Economic Analysis

### 1. The need for the draft amendments to Rules G-12 and G-15.

The need for the draft amendments arises from the industry-led initiative to shift from the current T+3 regular-way settlement cycle to a T+2 settlement cycle. The MSRB understands that the SEC intends to make regulatory changes necessary to support this shift by the third quarter of 2017<sup>10</sup> and that Financial Industry Regulatory Authority (FINRA) also intends to make conforming changes. Absent changes to MSRB Rules G-12(b)(ii) and G-15(b)(ii) to make these rules consistent with the changes the MSRB anticipates the SEC and FINRA will make, municipal security market participants would have to utilize a different settlement cycle than what will be used for equity securities and corporate bonds. The MSRB believes that all market participants benefit from a consistent settlement cycle across equity securities, corporate bonds and municipal securities—an outcome that the MSRB draft amendments would support.

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<sup>9</sup> 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).

<sup>10</sup> *Supra* note 7.

**2. Relevant baselines against which the likely economic impact of elements of the draft amendments to Rules G-12 and G-15 can be considered.**

The relevant baseline against which the likely economic impact of the draft amendments to Rules G-12 and G-15 should be considered is the settlement cycle used for equity securities and corporate bonds. This cycle is regulated by SEC Rule 15c6-1 and other FINRA rules. MSRB Rules G-12(b)(ii) and G-15(b)(ii) have historically been amended to remain consistent with SEC Rule 15c6-1.

Because the draft amendments are contingent on anticipated changes to SEC Rule 15c6-1, which would shorten the settlement cycle for equity securities and corporate bonds to T+2, the relevant baseline is a regulatory environment in which those financial products are subject to the industry-recommended shortened settlement time.

**3. Identifying and evaluating reasonable alternative regulatory approaches.**

Rather than conforming to the anticipated future settlement cycle for equity securities and corporate bonds, the MSRB could either continue to define regular-way settlement as T+3 or propose to shorten the settlement cycle even further. The MSRB believes that all market participants benefit from a consistent settlement cycle across equity securities, corporate bonds, and municipal securities and identifies this consistency as the primary need for the draft amendments. Given the likely benefits of consistency and likely costs of inconsistency, it is unclear whether having a longer or shorter settlement cycle than equity securities and corporate bonds would qualify as a reasonable alternative.

In addition, when comparing a T+2 settlement cycle to a T+1 settlement cycle, the MSRB relied on the detailed cost-benefit analysis conducted by DTCC ("DTCC cost-benefit analysis")<sup>11</sup> which concluded that the "payback period"—the time period after which the benefits would outweigh the costs—was considerably shorter for the T+2 settlement cycle due to significantly higher upfront costs associated with the T+1 settlement cycle.

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<sup>11</sup> *Supra* note 2.

#### 4. Assessing the benefits and costs of the draft amendments to Rules G-12 and G-15.

The MSRB policy on economic analysis in rulemaking addresses consideration of the likely costs and benefits of the rule with the draft amendments fully implemented against the context of the economic baseline discussed above. To address this consideration, the MSRB relied significantly on the DTCC cost-benefit analysis.<sup>12</sup> The MSRB is seeking, as part of this request for comment, additional data or studies relevant to a shortened settlement cycle, particularly in the municipal securities market, the costs of implementing the systems and processes necessary to comply with the draft amendments, and the potential unintended or indirect economic consequences of the draft amendments.

##### **Benefits**

Consistent with the DTCC cost-benefit analysis<sup>13</sup> and the Recommendation of the SEC Investor Advisory Committee,<sup>14</sup> the MSRB believes that a shift to a T+2 settlement cycle may yield important benefits for market participants, including operational costs savings, reduced counterparty risk, decreased clearing capital requirements, reduced pro-cyclical margin and liquidity demands and increased global securities settlement harmonization. The MSRB believes that the draft amendments would allow for these outcomes in the municipal securities market and ensure that municipal securities market participants are not at a disadvantage related to settlement cycle compared to equity security and corporate bond market participants.

##### **Costs**

The DTCC cost-benefit analysis identified operational changes to certain industry practices, technological and infrastructure investments, and changes to the securities market infrastructure that would be required to achieve a shorter settlement cycle. DTCC estimated these costs for several types of market participants involved in equity, corporate bond, and municipal bond markets.<sup>15</sup> While the DTCC cost-benefit analysis did estimate the levels of investment that would be potentially required based on the function

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<sup>12</sup> *Supra* note 2.

<sup>13</sup> *Supra* note 2, pp. 32-35.

<sup>14</sup> Recommendation of the Investor Advisory Committee: Shortening the Trade Settlement Cycle in U.S. Financial Markets (February 12, 2015), <https://www.sec.gov/spotlight/investor-advisory-committee-2012/settlement-cycle-recommendation-final.pdf>.

<sup>15</sup> *Supra* note 2, p. 40.

performed by market participants (*e.g.*, broker-dealers vs. buy side firms), it did not attempt to allocate the investment costs by market.

These operational, technological, and infrastructure changes would be necessitated by the anticipated amendments to SEC Rule 15c6-1, the baseline against which the MSRB draft amendments are measured. The MSRB assumes the changes necessary to comply with SEC Rule 15c6-1 and achieve a shorter settlement cycle for equities and corporate bonds are identical to those necessary to support a shorter settlement cycle for municipal securities. Therefore, for those firms that participate in both the municipal securities market and the corporate bond or equity market—the majority of affected market participants—the MSRB estimates that the additional cost of the draft amendments relative to the baseline would be relatively small. The MSRB recognizes, however, that certain market participants only participate in the municipal securities market and will be required to make investments to achieve a T+2 settlement cycle. For those firms, the costs of transitioning to a T+2 settlement cycle will be associated with the draft amendments to Rules G-12 and G-15 and may, based on the DTCC cost-benefit analysis, amount to as much as \$4 million per firm.

The MSRB is unaware of any data that would support a quantitative estimate of the overall impact of a shortened settlement cycle specifically on municipal securities market participants or, if appropriate, an allocation of the costs estimated in the DTCC cost-benefit analysis across the affected markets. Thus, at this juncture, the MSRB can only make a qualitative assessment based on the assumptions stated above. The MSRB specifically seeks comments that would inform a quantitative estimate of the costs associated with the draft amendments that can be specifically attributed to the municipal securities market.

#### **Effect on Competition, Efficiency, and Capital Formation**

The MSRB believes that draft amendments to MSRB Rules G-12 and G-15, in their support of the industry-led transition to a T+2 settlement cycle, will improve efficiency and capital formation, consistent with the findings included in the DTCC cost-benefit analysis. The MSRB recognizes that both the benefits and the costs associated with the draft amendments may vary by participant and that, in general, regulatory changes that require infrastructure investments may have disparate impacts that could affect the competitive landscape.

## Request for Comment

The MSRB seeks public comment on the following questions, as well as on any other topic raised in this request. The MSRB particularly welcomes statistical, empirical and other data from commenters that may support their views and/or support or refute the views, assumptions or issues raised in this request.

1. Would the draft amendments have an effect on conduct that is required for compliance with any other MSRB rule?
2. Are there any other MSRB rules that should be amended to support a shift to a T+2 settlement cycle?
3. Would a move to a T+2 settlement cycle have any impacts that are unique to transactions in municipal securities?
4. Would the draft amendments impose any cost or burdens, direct, indirect, or inadvertent, on investors or regulated entities? Are there data or other evidence including studies or research, that support commenters' cost or burden estimates?
5. What, if any, costs associated with a T+2 settlement cycle, are associated specifically with the draft amendments and are additional to those costs that make up the baseline?

November 10, 2015

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## Text of Draft Amendments<sup>16</sup>

### Rule G-12: Uniform Practice

(a) *Scope and Notice.*

(i) – (iii) No change.

(b) *Settlement Dates.*

(i) No change.

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<sup>16</sup> Underlining indicates new language; strikethrough denotes deletions.



(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 ~~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) *Customer Confirmations*.

(i) - (viii) No change.

(b) *Settlement Dates*.

(i) No change.

(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) – (g) No change.