



## **Recommended Closing Time Practices for Delivering Fedwire-Eligible Securities**

*Revised May 28, 2009*

In lieu of the existing Securities Industry and Financial Markets Association (SIFMA) guidelines and current industry practice (see Appendices B and C, respectively); the Treasury Market Practices Group (TMPG) and SIFMA recommend that, in general, market participants observe 3:00 p.m. EST<sup>1</sup> as the deadline for origination of deliveries of Fedwire-eligible securities, effective July 1, 2009.<sup>2</sup> In addition, TMPG and SIFMA recognize that some market participants may find it beneficial to negotiate, bilaterally with some of their counterparties, alternative closing time arrangements to cover settlements between themselves and those counterparties.<sup>3</sup> For example, market participants with sophisticated inventory control systems may prefer to originate and receive deliveries *with each other* up until the 3:15 p.m. cutoff time for originating deliveries of Fedwire-eligible securities prescribed by the Federal Reserve System. Such mutually-agreed arrangements would not violate the general closing time recommendation of the TMPG and SIFMA.

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<sup>1</sup> All times referred to in this recommendation are premised on a 3:30 p.m. Fedwire Securities Service close. In the event of an extension, all referenced times within this recommendation would adjust accordingly, relative to the actual Fedwire Securities Service close on a given day.

<sup>2</sup> In making this recommendation, the TMPG and SIFMA are modifying their prior proposed recommendation on closing time practices published on April 28, 2009. Readers are reminded that the earlier recommendation had an effective date of June 1, 2009, while the revised recommendation has an effective date of July 1, 2009. The one-month postponement is intended to give custodians time to effect necessary system modifications.

<sup>3</sup> Any alternative closing time arrangement would remain subject to prevailing Fedwire closing times (see Appendix A for current Fedwire closing times).

Adherence to the recommended closing time practice would not require any change in either (1) current Fedwire closing times (see Appendix A), or (2) the current Fixed Income Clearing Corporation (FICC) practice of closing its delivery system for Fedwire-eligible securities at 3:00 p.m. The interval between 3:15 p.m. and 3:30 p.m. would continue to be reserved for reversals only.<sup>4</sup>

## **Background**

The revised closing time practice recommendation resulted from discussions among TMPG members and other market participants during the course of finalizing implementation details associated with the TMPG recommendation regarding charges for settlement fails in the market for U.S. Treasury securities.<sup>5</sup> Some buy-side market participants expressed dissatisfaction with the existing market convention under which dealers can deliver securities to customers until 3:15 p.m., but customers can usually only deliver securities to dealers until 3:00 p.m.<sup>6</sup> This convention can sometimes leave a customer who had, at 3:00 p.m., an uncompleted obligation to receive securities and a matching uncompleted obligation to deliver the same securities in the position of taking in the securities after 3:00 p.m. without being able to turn the securities around and redeliver them on the same day. Instead of a pair of matched fails, the customer is left with an unmatched fail to deliver, resulting in higher interest expenses and/or an overdraft charge. Some buy-side market participants expressed the view that closing times should treat all market participants the same, regardless of whether they are real-money investors, leveraged investors, or dealers.

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<sup>4</sup> A reversal is a return of securities previously delivered in cases where the original delivery was, or is believed to have been, in error. The restriction of the 3:15 p.m. to 3:30 p.m. period to reversals arises from Federal Reserve System policies (see Appendix A).

<sup>5</sup> Although this guidance grew out of work related to the Treasury market, it applies to all Fedwire-eligible securities, because restricting it to Treasury securities would be operationally burdensome. The TMPG recommendation and related material appears at [www.newyorkfed.org/tmpg/](http://www.newyorkfed.org/tmpg/).

<sup>6</sup> Some dealers make exceptions in some cases and allow some customers on some occasions to deliver securities between 3:00 and 3:15 p.m.

## **Discussion**

The recommended general deadline of 3:00 p.m. for the origination of deliveries of Fedwire-eligible securities removes the asymmetry between dealers and customers embedded in the current industry practice. However, the TMPG and SIFMA recognize that some market participants may find it beneficial to negotiate, bilaterally with some of their counterparties, alternative closing time arrangements to cover settlements between themselves and those counterparties. Some participants may have sophisticated inventory control systems and those participants (as well as the market as a whole) can benefit from a brief, end-of-day interval during which those participants can attempt to fulfill outstanding delivery obligations while retaining control of what comes into their clearing and custodial accounts. Such market participants may prefer to agree to originate and receive deliveries *with each other* on a mutually-agreed basis up until the 3:15 p.m. Federal Reserve System cutoff time for originating deliveries of Fedwire-eligible securities.

The recommendation that, in general, market participants originate deliveries of Fedwire-eligible securities not later than 3:00 p.m. leaves room for such beneficial agreements while eliminating the non-consensual asymmetry in current closing time practices.

Although mutually beneficial agreements as to alternative closing time arrangements would not violate the general closing time recommendation of the TMPG and SIFMA, alternative closing time arrangements may entail significant additional costs and operational burdens. The TMPG and SIFMA suggest that market participants consider carefully the relative costs and benefits with respect to their individual businesses of entering into such arrangements. In particular, each market participant should consult with its custodian or custodians about the cost and complexity of entering into an alternative closing time arrangement.

## **What is the Recommended Treatment for Fails Charges on U.S. Treasury Securities Under this New Practice Guidance?**

It is important to recall that the fails charge recommendation applies only to delivery fails with respect to transactions in U.S. Treasury securities, whereas the revised closing time recommendation applies to all Fedwire-eligible securities. In the event that a seller fails to deliver Treasury securities to a buyer on a given day, the TMPG recommends that the buyer charge the seller for the settlement fail pursuant to the TMPG practice recommendation published on March 31, 2009,<sup>7</sup> regardless of whether the parties are observing the general 3:00 p.m. closing time or have agreed to some alternative closing time arrangement.

#### **Appendix A. Current Fedwire Closing Times**<sup>8</sup>

- Any market participant can originate a delivery prior to 3:15 p.m.
- The interval between 3:15 p.m. and 3:30 p.m. is reserved for reversals only.

#### **Appendix B. Current SIFMA Delivery Guidelines**<sup>9</sup>

- Any market participant can originate a delivery prior to 2:45 p.m.
- Between 2:45 p.m. and 3:00 p.m., a customer can not originate a delivery to a dealer, but dealers can originate deliveries to other dealers and to customers.
- Between 3:00 p.m. and 3:15 p.m., neither customers nor dealers can originate deliveries to dealers, but a dealer can originate a delivery to a customer.
- The interval between 3:15 p.m. and 3:30 p.m. is reserved for reversals only.

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<sup>7</sup> The “U.S. Treasury Securities Fails Charge Trading Practice”, published by the TMPG and SIFMA, is available at [http://www.sifma.org/capital\\_markets/docs/fails-charge-trading-practice.pdf](http://www.sifma.org/capital_markets/docs/fails-charge-trading-practice.pdf).

<sup>8</sup> Federal Reserve Operating Circular No. 7 (August 19, 2005), Appendix B.

<sup>9</sup> Public Securities Association, *Government Securities Newsletter*, “PSA Amends Good Delivery Deadlines for Extended Fedwire Book-Entry System,” November 27, 1995, p. 2.

Comment: This scheme was put in place to allow dealers 15 minutes (between 2:45 and 3:00) to clean up fails to each other, and 15 minutes (between 3:00 and 3:15) to make deliveries to customers. It was thought that delivering a security to a customer removes the security from circulation, so deliveries to customers should be postponed until the last 15 minutes of the delivery day.

### **Appendix C. Current Industry Practice**<sup>10</sup>

- Any market participant can originate a delivery prior to 3:00 p.m.
- Between 3:00 p.m. and 3:15 p.m.,
  - a customer can not originate a delivery to a dealer,<sup>11</sup>
  - a dealer can originate a delivery to another dealer with the permission of the dealer, but
  - a dealer can originate a delivery to a customer *without* the permission of the customer.
- The interval between 3:15 p.m. and 3:30 p.m. is reserved for reversals only.

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<sup>10</sup> Some dealers may observe slightly different conventions.

<sup>11</sup> Some dealers do allow a customer to originate a delivery during this 15 minute window with the permission of the dealer.