

# **NYCHA- BCHA- BDUG Dealer-Time Taskforce**

April 12, 2001

Mr. Warren J. Spector, Chairman  
The Bond Market Association  
40 Broad Street  
New York, New York 10004-2373

Dear Mr. Spector:

In the past eighteen months, The New York Clearing House Association L.L.C.(NYCHA), the Boston Clearing House Association (BCHA), and the Bank Depository Users Group (BDUG) have separately written to the Bond Market Association (BMA) requesting that the BMA guideline known as Dealer-time be eliminated (see attachments A, B, and C respectively). Unfortunately, the BMA Government Operations Committee has rebuffed the efforts of these Industry groups to engage in a dialogue on this issue, so we are writing to you directly to pursue these efforts before proceeding with alternative approaches available to us, one of which is outlined below.

Dealer-time is a fifteen-minute window at the end of the Fed's book-entry security processing day, during which dealers may make deliveries to customers, but customers cannot make deliveries to dealers. As a result of your guideline, our clients are left unable to deliver many transactions and incur significant overnight financing costs. An analysis by four NYCHA banks in June 1999 revealed that Dealer-time was costing their clients \$17,150,000 on an annual basis.

The Industry organizations opposed to Dealer-time represent eighty-five banks and their thousands of institutional and retail clients. Many of these domestic and global clients have complained to us about the Dealer-time practice and its resulting costs. They have not encountered such a practice in any of the emerging or developed markets in which they invest and it is difficult to explain to them how the world's most sophisticated securities market allows for an unlevel playing field on securities settlement.

The appearance of a favored class of participant undermines the market's integrity and investor confidence in it, and is surely not in the best interests of the BMA and the overall treasury/agency market. Additionally, your guidelines promote settlement inefficiencies and increase costs to the underlying investors in the treasury/agency market. While this practice may have been born of necessity in the physical processing environment of yesteryear, it no longer has any justification or place in today's highly automated book-entry environment.

There are additional reasons why Dealer-time should be eliminated:

- Dealer-time once existed for other major products such as Ginnie Maes and Commercial Paper. When these securities were made book-entry eligible, Dealer-time was appropriately eliminated. Accordingly, our members have expressed concerns regarding current Industry plans to move Ginnie Maes from the non-dealer time DTC environment to the Fed environment in which Dealer-time persists (attachment D).
- We understand your guideline was originally designed to assist dealers in an era when treasuries were issued in physical form and had to be hand-delivered by messenger often late in the processing day. In today's automated electronic environment, treasuries are issued in book-entry form and new issuance is completed by 10:00 A.M. EST—consequently, this is no longer an issue. This guideline also has gone well beyond its original scope of treasuries, to affect many more security types such as Fannie's, Freddie's, Salle Mae's, IBRD's, etc.
- In the past, there was concern that eliminating Dealer-time would create processing logjams at the end of the day. According to FED statistics, however, 92% of all FBE activity is processed by 2:00 PM EST each day, hence this scenario is extremely unlikely. Moreover, the previously mentioned elimination of Dealer-time for Ginnie Maes and Commercial Paper occurred with no adverse impact to the industry.
- The Dealer-time guideline in the BMA Government Securities Manual is inaccurate. It lists the customer-to-dealer cut-off time at 2:45 P.M. when in practice today it is 3:00 P.M. EST. We should also point out that since the Fed no longer publishes a list of primary dealers, there is no bonafide source to say who is and who isn't a dealer.
- The entire Securities Industry is striving to achieve Straight-Through Processing (STP). Dealer-time is an STP inhibitor as trades only settle in one direction during that timeframe. The industry can never fully achieve STP as long as Dealer-time exists.

On August 10, 1995 the Federal Reserve Board announced it was revising delivery hours on book-entry securities to 3:15 P.M. EST for deliveries, 3:15-3:30 P.M. EST for reversals. The Board also gave an opinion on the new closing times and the Dealer-time guideline:

*The Board believes that these closing times will satisfy adequately the known processing needs of market participants with respect to interbank transfers. The Board believes that the new closing time provides sufficient opportunity for market participants to complete daily deliveries, absent unusual operating or computer problems. In addition, the Board's action does not preclude the continuation of an industry standard for a dealer-turnaround time if the industry believes it is needed. The Federal Reserve Bank's Book-Entry securities operating circulars will be modified to eliminate reference to a separate deadline for dealer-to-customer deliveries...*<sup>1</sup>

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<sup>1</sup> Federal Reserve Board Press Release, August 10, 1995, Section III. Selection of Appropriate Closing Time, Page 9, Paragraph 2.

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Our members, along with our clients, agree with the Fed's assertion that the new deadlines would (and have) met the needs of market participants. We also view the Board's action to eliminate all reference to Dealer-time from Fed literature as unwillingness on the Board's part to endorse your guideline.

The Board did note that Dealer-time could continue if "the industry" felt it was needed. The NYCHA, BCHA, and BDUG membership respectfully disagree that the BMA represented the entire Industry on this issue five years ago—nor do they represent the entire industry on this issue today. The Industry includes not only BMA members such as Broker Dealers but also Custodial Banks, Investment Managers, and other financial institutions which have not been consulted in the decision making process. It is also important to note that the BMA Dealer-time guideline is voluntary as it states: "*As with all BMA guidelines, the good delivery guidelines are recommendations only and each firm must decide for itself whether to follow them*".

Since your guideline promotes unequal opportunity and abrogates our clients' rights to have an equal opportunity to settle their trades, our members cannot support this voluntary guideline. One alternative available to our members would be to only recognize the Federal Reserve Bank deadlines, and to pursue compensation claims on valid deliveries made between 3:00-3:15 P.M. that are subsequently rejected by dealers as being "too late" because of Dealer-time. These deadlines were approved by the Board of Governors in August 1995 and are detailed in the Federal Reserve Bank's Operating Circular 7, "Book-Entry Securities Account Monitoring and Transfer Services", appendix B, page 12, and reprinted below. These are also the only deadlines that the Fed's National Book-Entry System recognizes from a systemic messaging perspective.

Opening of Fedwire	8:30 A.M. EST
Closing Time – Transfer Origination	3:15 P.M. EST
Closing Time – Transfer Reversals	3:30 P.M. EST

Even though our past attempts to work with the BMA on this issue have failed, our membership believes it is in the industry's best interests to make one last effort to resolve this issue directly with your organization. Towards that end, we will make the necessary staff and resources available to work on this issue immediately with the appropriate BMA counterparts. We believe that if the BMA works with our taskforce in the next three months, to establish a process that will result in the elimination of Dealer-time this year, our members would be willing to forgo alternate approaches and remedies which are more immediately available to us.

Our members strongly believe that one fair and consistent guideline is in the best interest of our industry. We would urge the BMA to review your guideline not only for fairness but to measure whether it is consistent and in the spirit of the stated BMA's goals: "*to promote efficiency and reduce market costs*" and ensure "*open and free access to the public securities market*". We would respectfully submit that not only does Dealer-time no longer meets these BMA goals, it actually promotes market inefficiency, increases market costs, and limits equal market access.

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Our members are committed to seeing Dealer-time eliminated and welcome the opportunity to work with the BMA to that end. We believe that the facts and arguments for the elimination of this antiquated guideline are extremely compelling and, as such, must be changed in the best interests of our industry.

Sincerely,

\*The New York Clearing House Association:

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Jeffrey P. Neubert

The Boston Clearing House Association:

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Robert McGovern

The Bank Depository User Group:

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Carol P. Bright

cc: Dennis Dirks, Depository Trust and Clearing Corporation  
Robert Fry, Government National Mortgage Association  
Dara Hunt, Federal Reserve Bank  
Paul Saltzman, The Bond Market Association  
Michael Wyne, Asset Managers Forum

Attachments

\*The New York Clearing House Association's Securities Operations Committee helped prepare this letter. The Committee consists of the following banks, two of which abstained from voting to send this letter: The Chase Manhattan Bank, Citibank, N.A., Bankers Trust Company, The Bank of New York, HSBC Bank, U.S.A., Fleet Bank, National Association, and State Street Bank.