TMPG | Treasury Market Practices Group

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Treasury Market Practices Group Proposes Fails Charge Recommendations for Agency Debt and Agency MBS Markets and Seeks Public Comments

The Treasury Market Practices Group (TMPG) today proposed fails charge recommendations for the agency debt and agency mortgage-backed securities (MBS) markets and requested public comments on those proposed recommendations.

The historically elevated levels of fails in these markets create inefficiencies, increase credit risk for market participants and heighten overall systemic risk. By replicating the incentives that exist in a higher rate environment to deliver securities in a timely manner, the proposed fails charges are expected to reduce fails. The introduction of these charges is designed to support the efficiency and liquidity of the agency debt and agency MBS markets, such that trading better reflects the underlying availability of securities for delivery and market participants are afforded greater certainty regarding settlement of their transactions.

“The TMPG is proposing fails charges in the agency debt and agency MBS markets in order to reduce the incidence of delivery failures in these markets,” said Tom Wipf, TMPG chair. “We strongly believe that, like the fails charge recommended by the TMPG in the Treasury market, these recommendations will lead to more robust markets for agency debt and agency MBS and will serve to broadly reduce the risks associated with high levels of fails .”

These fails charge recommendations, which serve as a complement to the TMPG’s “Best Practices for Treasury, Agency Debt, and Agency Mortgage-Backed Securities Markets,” are modeled after the recommended Treasury fails charge but are structured to reflect the characteristics of the agency debt and agency MBS markets.

For the agency debt market, the proposed fails charge would accrue each calendar day a fail is outstanding and would include a $500 minimum claim threshold, similar to the recommended Treasury market fails charge trading practice. Debentures issued by Fannie Mae, Freddie Mac and the Federal Home Loan Banks would be subject to this charge.

For the agency MBS market, the proposed fails charge would accrue each calendar day a fail is outstanding, but the fail would not be subject to a charge if delivery occurs on either of the two business days following contractual settlement date (referred to as the resolution period). Charges for fails settled in a given calendar month would be aggregated between legal counterparties, and a claim would be made if aggregate charges for the month exceed $500. Agency MBS issued or guaranteed by Fannie Mae, Freddie Mac and Ginnie Mae would be subject to this charge.

The TMPG is recommending the two-day resolution period to allow market participants to resolve operational fails, in recognition of the nature of clearing and settlement in the agency MBS market. The TMPG may consider a shorter resolution period, or elimination of the resolution period altogether, if circumstances warrant.

The TMPG today also released a white paper describing the risks associated with large and persistent fails in the agency MBS market.

Members of the public may submit comments by Friday, June 10, 2011, to tmpg@ny.frb.org. The TMPG expects to release final recommendations soon after its evaluation of public comments. At this time, the TMPG expects that the final recommendations will include a recommended implementation date of early 2012, in order to allow market participants to develop the necessary infrastructure and operational support to process fails charge claims.

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About the Treasury Market Practices Group (TMPG)

The TMPG is a group of market professionals committed to supporting best practices in the Treasury, agency debt and agency mortgage-backed securities (MBS) markets. It is composed of senior business managers and legal and compliance professionals from a variety of institutions, including securities dealers, banks, buy-side firms, market utilities and others, and is sponsored by the Federal Reserve Bank of New York.

For more information on:
Treasury Market Practices Group, visit www.newyorkfed.org/tmpg

"Recommended Agency Debt Securities Fails Charge Trading Practice," see
www.newyorkfed.org/tmpg/debtfails_04292011.pdf

"Recommended Agency Mortgage-Backed Securities Fails Charge Trading Practice," see
www.newyorkfed.org/tmpg/agencymbs_04292011.pdf

"Understanding Settlement Fails in Agency Mortgage-Backed Securities" (TMPG White Paper), see
www.newyorkfed.org/tmpg/tmpg_04292011.pdf

"Best Practices for Treasury, Agency Debt, and Agency Mortgage-Backed Securities Markets," see
www.newyorkfed.org/tmpg/bestpractice_09142010.pdf

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