MEMORANDUM

August 15, 2022

TO: File No. SR-FINRA-2021-10

FROM: Ivan Griswold
Office of Commissioner Mark T. Uyeda

RE: Meeting with Bond Dealers of America

On August 15, 2022 Commissioner Mark T. Uyeda and his counsel, Ivan Griswold, had a meeting with the Bond Dealers of America (BDA). Commissioner Uyeda and the attendees met virtually. The BDA representatives in attendance consisted of:

- Mike Nicholas, Chief Executive Officer, BDA
- Robert Tirschwell, Head of Capital Markets, Brean Capital
- Thomas Fleming, Partner, Olshan Frome Wolosky
- Adrienne Ward, Partner, Olshan Frome Wolosky

The participants discussed BDA's (1) comment letter filed in connection with the Notice of Filing of a Proposed Rule Change to Amend the Requirements for Covered Agency Transactions under FINRA Rule 4210 and, (2) Petition for Review of Order Granting Approval of a Proposed Rule Change, as Modified by Amendment No. 1, to Amend the Requirements for Covered Agency Transactions under FINRA Rule 4210 (Margin Requirements) as Approved Pursuant to SR-FINRA-2015-036, Release No. 34-94013; File No. SR-FINRA-2021-010.

Attachment (slide deck).

Petition to Review Trade Illustrations

Bond Dealers of America

Bean Capital, LLC

Figure A - Prototype Trades in Covered Agency Transactions

Security: FNR 2021-42 NY 3136BGAM3 (CMO)
Trade Date: 06/01/2021
Settlement Date: 06/30/2021
Total Issuance size is 34,022,759
Trade Notional is 30,000,000

Assume the purchase and sale of $30mm FNR 2021-42 NY trades between counterparties at various prices as follows:

Dealer / Seller #1 $\xrightarrow{\text{99-02}}$ Dealer #2 $\xrightarrow{\text{99-06}}$ Dealer #3 $\xrightarrow{\text{99-09}}$ Institution #4 $\xrightarrow{\text{99-15}}$ Dealer #5 $\xrightarrow{\text{99-20}}$ Institution #6

- Trades are often accompanied by a swap, in which the buyer of a Specified Pool or CMO also sells a TBA as a hedge;
- Trades likely all settle on same good settlement date;
- Chain may be quite brief or extensive, and may take days or weeks; to develop;
- Trade in CMO illustrated does not settle via FICC.

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Illustration 1: Financial and regulatory impact of 4210										
	Current					***Proposed 4210***				
	Cash	Margin @ Pershing	WI Req @ Pershing	Reg Capital	TOTAL	Cash	Margin @ Pershing	WI Req @ Pershing	Reg Capital	TOTAL
MTM	-	-	-	(300,000) *	(300,000)	-	-	-	-	-
Margin Call	-	-	-	-	-	(3,000,000) **	-	-	-	(3,000,000)
TOTAL	-	-	-	(300,000)	**(300,000)**	(3,000,000)	-	-	-	**(3,000,000)**

Transaction Description		
T/D	**S/D**	
6/1/2021	6/21/2021	Brean Capital ***BUYS*** $100mm of Ginnie Mae II Pool (G2 MA7359 (36179WE87) - ***NON FICC SETTLING / NON DELIVERABLE*** for their inventory from a primary dealer
6/1/2021	6/21/2021	Brean Capital ***SELLS*** $100mm of TBA back to the primary (G2SF 2 1/2 Jun21 (21H022663) - ***FICC SETTLING / DELIVERABLE*** to hedge their exposure to the pool **** Brean Capital is facing different counterparties on each of these transactions***

Subsequent Event and Impact to Brean Capital		
Event		**- After trade date and before settlement date the value of the pool purchased by Brean decreased by 3 points or $3mm dollars.**
Current Impact		**- From an equity perspective the mark to market loss of $3mm on the long pool purchased would be offset by a $3mm mark to market gain on the hedge position.**
	*	**- Brean would incur a $300k regulatory capital charge due to the decrease in market value of the pool purchased (10% x $3,000,000)**
Proposed Impact	**	**- Brean is issued a margin call for $3mm from the seller of the pool due to the fact that the pool is NON FICC SETTLING / NON DELIVERABLE in essence a bilateral transaction & therefore must wire $3mm to the seller of the pool to satisfy the call. Additionally, due to the fact that Brean is not a member of the MBSCC it is unable to recover from the net any of the margin it was required to post.**
		- By satisfying the margin call to the seller of the pool the regulatory capital charge of $300k would be eliminated.
Summary		**- Even though Brean Capital has effectively hedged its exposure by selling a TBA of the same size, under Rule 4210 it would be required to post margin to the seller of the NON FICC SETTLING / NON DELIVERABLE pool. Currently the impact of this transaction to Brean would be a $300k regulatory charge whereas under the proposed rule 4210 it would be required to post $3mm in margin, or an increase of $2.7mm.**

Illustration 2: Financial and regulatory impact of 4210											
	Current					*Proposed 4210*					
	Cash	Margin @ Pershing	WI Req @ Pershing	Reg Capital	TOTAL	Cash	Margin @ Pershing	WI Req @ Pershing	Reg Capital		TOTAL
MTM	-	-	-	(300,000) *	(300,000)	-	-	-	-		-
Margin Call	-	-	-	-	-	(3,000,000) **	-	-	(3,000,000)	***	(6,000,000)
TOTAL	-	-	-	(300,000)	**(300,000)**	(3,000,000)	-	-	(3,000,000)		**(6,000,000)**

Transaction Description		
T/D	S/D	
6/1/2021	6/21/2021	Brean Capital ***BUYS*** $100mm of Ginnie Mae II Pool (G2 MA7185 (36179V6W5) - ***NON FICC SETTLING / NON DELIVERABLE*** for their inventory from a primary dealer
6/1/2021	6/21/2021	Brean Capital ***SELLS*** $100mm of the same Ginnie Mae II Pool (G2 MA7185 (36179V6W5) - ***NON FICC SETTLING / NON DELIVERABLE*** from their inventory to a customer
		**** In principle this is a riskless trade from the Brean perspective.***

Subsequent Event and Impact to Brean Capital		
Event		- After trade date and before settlement date the value of the pool purchased by Brean decreased by 3 points or $3mm dollars.
Current Impact		- From an equity perspective the mark to market loss of $3mm on the pool purchased would be offset by a $3mm mark to market gain on the sale of the same pool.
	*	- Brean would incur a $300k regulatory capital charge due to the decrease in market value of the pool purchased (10% x $3,000,000)
Proposed Impact	**	- Brean is issued a margin call for $3mm from the seller of the pool due to the fact that the pool is NON FICC SETTLING / NON DELIVERABLE in essence a bilateral transaction & therefore must wire $3mm to the seller of the pool to satisfy the call. However, Brean is unable to issue a call to the buyer of the same pool due to a variety of reasons and therefore must take the full regulatory capital charge of $3mm.
		- By satisfying the margin call to the seller of the pool the regulatory capital charge of $300k would be eliminated.
Summary		- Even though Brean Capital has entered into a riskless principal trade under the proposed rule 4210 they would be required to post margin to the seller & take a regulatory capital charge for the amount that they are unable to call from their customer. The impact to Brean currently is a $300k regulatory charge whereas under rule 4210 total impact would be $6.0mm or an increase of 1900%.

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Illustration 3: Financial and regulatory impact of 4210										
	Current					*Proposed 4210*				
	Cash	Margin @ Pershing	WI Req @ Pershing	Reg Capital	TOTAL	Cash	Margin @ Pershing	WI Req @ Pershing	Reg Capital	TOTAL
MTM	-	-	(1,500,000) ****	(300,000) *	(1,800,000)	-	(1,500,000)	-	-	(1,500,000)
Margin Call	-	-	-	-	-	(3,000,000) **	-	-	(3,000,000) ***	(6,000,000)
TOTAL	-	-	(1,500,000)	(300,000)	**(1,800,000)**	(3,000,000)	(1,500,000)	-	(3,000,000)	**(7,500,000)**

Transaction Description

T/D	S/D	
6/1/2021	6/21/2021	Brean Capital ***SELLS*** $100mm of Ginnie Mae II Pool (G2 MA7311 (36179WDQ8) - ***FICC SETTLING* / DELIVERABLE** to a primary dealer from Inventory
6/1/2021	6/30/2021	Brean Capital ***BUYS*** $100mm of New Issue CMO from the primary dealer which was created from the collateral sold, Ginnie Mae II Pool (G2 MA 7311 (36179WDQ8))
6/1/2021	6/30/2021	Brean Capital ***SELLS*** $100m of the same New Issue CMO (Collateral sold to the primary dealer) to Institutional a/c that cannot or will not post collateral to Brean

** The trades above are in agreement with the SIFMA settlement schedule (good day settlement)*
*** As a result the agency pools sold to the primary dealer netted in FICC, and FICC credits Pershing not Brean Capital, in this example $3mm*

Subsequent Event and Impact to Brean Capital

Event - After trade date and before settlement date the value of the CMO purchased from the primary dealer decreased by 3 points or $3mm dollars.

Current Impact
* - Brean would incur a $300k regulatory capital charge due to the decrease in market value of the CMO purchased (10% x $3,000,000)
**** - Brean is required to post margin to Pershing in the amount of 1.5% of future settling when issued securities (notional) 1.5% x $100mm.

Proposed Impact
** - Brean is issued a margin call for $3mm from the seller of the CMO to cover the decrease in value so Brean has to wire $3mm in cash to satisfy the call as it cannot use the corresponding decrease in the value of the collateral sold to offset the call because Brean does not have access to the net.
*** Given the fact that Brean is unable to collect margin from the buyer of the CMO it is required to take a regulatory capital charge for the full amount of the call, in this case $3mm. Additionally, since Brean does not have access to the net it must use it's own cash to satisfy the call.
**** - Brean is still required to post margin to Pershing in the amount of 1.5% of when issued securities (notional) 1.5% x $100mm.
- By satisfying the margin call to the seller of the CMO the regulatory capital charge of $300k would be eliminated.

Summary - SIFMA requires that all CMO securitizations be created in accordance with their settlement calendar known as "good day settlement." In this example Brean would be required to post margin to the seller & take a regulatory capital charge for the amount that they are unable to call from their customer. Under current rules the impact to Brean would be $1.8mm whereas under 4210 total impact would be $7.5mm.