

Shortening the Settlement Cycle: Stopping for a Quick Breath



By Kevin Burns, STA Operations Committee Co-Chair and Senior Industry and Business Operations Analyst, Computershare

Shortening the settlement cycle continues to be an important issue across the financial sector. After several years of discussions, some of which stalled over time, there is a growing sense that the time to act is upon us. A number of industry groups, led by the Depository Trust and Clearing Company (and including the STA), are actively working toward shortening the U.S. settlement cycle for equities, municipal and

corporate bonds, and unit investment trusts (UITs) from T+3 (trade date plus three days) to T+2 (trade date plus two days) as a means to reduce credit and liquidity risk.

At this point, there are dozens of industry leaders and a handful of committees all working to develop recommendations for speeding up the settlement process. Given all the moving parts, now seems like a good time to take a step back and look at where we're at, what the goals are and who are the important players.

The goals

While there remains some discussion about how much to shorten the cycle, the ultimate goal remains of making it shorter than T+3. At the moment, T+2 is the target and would put the U.S. in line with other capital markets around the world. However, there are some who advocate for going as far as T+1, though that seems less likely in the near-term.

After seeing other countries implement a shortened settlement cycle, the DTCC last April issued a position paper formally calling for a T+2 settlement cycle. Shortening the cycle would reduce risk, limit exposure, optimize capital and improve efficiency. It would also bring the U.S. into alignment with the European Union, where the majority of countries, including the U.K., migrated to T+2 in October 2014.

By shortening to T+2, everyone involved in the process, from seller to broker and issuer to investor, will enjoy increased efficiency and reduced risk.

The players

With the existing intricacies of the industry, the effort to shorten the cycle requires large-scale collaboration and cooperation. Following the release of its position paper, the DTCC convened a steering committee to approach the issue and develop a plan and timeline for implementation of a shortened cycle.

The **steering committee**, chaired by the Securities Industry and Financial Markets Association (SIFMA) and the Investment Companies Institute (ICI), as well as an industry working group, has set out to define objectives and tasks needed to achieve T+2 settlement in the U.S. The steering committee is made up of senior-level representatives from industry associations and firms that represent various segments of the industry.

Reporting into the steering committee is the **industry working group**. This group supports the steering committee by identifying the business and rule changes needed, and a high-level plan with milestone dates to implement the changes required to shorten the settlement cycle to T+2. The industry working group will make its determinations based on input from the sub-working groups, which are represented by four main segments: buy side, sell side, industry associations and other market segments.

The **sub-working groups** represent more than 400 industry professionals (subject matter experts) with unique perspectives on the challenges and needs for shortening the cycle. The sub-working groups are charged with providing analyses to identify any required technology, behavioral, and regulatory changes required to facilitate a transition to T+2. There are 17 sub-working groups in all addressing a comprehensive approach to shortening the settlement cycle.

The STA is represented at each of these levels. Charlie Rossi is a participant on the steering committee, Katie Sevcik from Wells Fargo and I are participants on the working group, and several transfer agents have individuals participating on the sub-working groups. Our goal is to make sure that we understand the potential changes required and ensure that transfer agents needs are addressed.

It is certainly a large number of individuals, groups and committees involved in this process, but for such a fundamental change to occur, all facets of the industry must be considered. The challenges in technology and regulation require that the effort be exhaustive and the working groups are committed to laying out a roadmap for success.

A public website has been established that is a great resource for additional information on the T+2 initiative. This site contains additional detail on the committees and working

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groups along with updates as we move forward towards implementation.

This site can be found at www.ust2.com.

Next steps

As you can imagine, an undertaking involving so many people and interests is not likely to move at breakneck speeds. However, the steering group is committed to maintaining positive momentum. A number of the sub-working groups have already wrapped up their analyses and the remaining are in the process of wrapping up their work.

These reports will all be compiled for the working group, which from there will create a roadmap document to present to the steering committee. This document will provide

the committee with a proposed target date for technology implementation, as well as any regulatory challenges that may exist. Though the timeline for implementation will ultimately be subject to the final findings of the working group, it's generally accepted that the timeframe for implementation will be at least two years.

As Europe and other markets have moved to T+2, it's critical that the U.S. no longer lag behind the rest of the world. Thanks to the efforts of the DTCC and everyone involved with the working groups and sub-working groups, we now have the pieces in place to get to T+2 in a reasonable period of time. From there, the DTCC has added that this roadmap should be used to determine the viability of T+1 further down the road to truly advance the U.S. markets to the front of the world. ■

Regulations of a Transfer Agent – Adoption of the Rules and Section 240.17Ad-1

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The timing of all of the necessary actions to effect a transfer is considered the “turnaround” time, which begins once an item is received by the transfer agent. There is one catch to the “turnaround time”, a “window” or “drop”. The location of the “window” or “drop” will determine if the item is considered received. If there is significant distance from where the transfer agent performs the transfer functions, the item would not be considered received. The item is only considered received when it is delivered to the location where the transfer agent actually performs the transfer function. The definition of a “business day” is any day the transfer agent is normally open for business. This excludes holidays, Saturdays, and Sundays. A non-business day can also be considered in the event local government offices close due to inclement weather and ordinary commerce is suspended.

In summary, here's my interpretation. Sally Jo Shareholder sends in her certificate to transfer the registration to transfer agent ABC. Transfer agent ABC then receives the mail, opens the items, and determines whether or not the item is a routine transfer and sends it to the department to change the registration. The department that changes registrations then receives the items and processes the transfer within the required turnaround time and sends Sally Jo Shareholder a statement reflecting the transaction. This is high level but most transfer agents call this “ownership change.” ■

This is only the presenter's interpretation of the regulations and does not constitute legal advice.

From the Editor:

I want to thank all our contributors who have written such excellent articles for this month's Newsletter and issue an invitation to other members to join the group! In particular, I am thinking that it would be interesting, in future issues, to build more of a sense of community among STA members. Perhaps you or a colleague volunteer for a worthy Not For Profit organization and want to get the word out about it. Perhaps you took a particularly memorable vacation and would like to share some of your experiences or insights about it. Perhaps you achieved some milestone with a hobby or personal project. Let's start thinking now about how to add some of these more people oriented articles to our Newsletter going forward.



Cynthia