T+1 Policies and Procedures

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Securities Exchange Commission (SEC) Rule and what does it mean to firms?

The decision from the SEC to shorten the standard settlement cycle would require market participants to revamp their policy and procedures for improved efficiency and meet the compliance date of May 28th, 2024.[1]

OVERVIEW

- Identify changes and establish protocol for trade processing, asset servicing, documentation, and exception handling
- Create or modify policies and procedures that clearly identify and describe the technology systems, operations, and processes
- Develop communication plan for stakeholders
- Address the timing of allocations, confirmations, and affirmations in the polices and procedures
- Conduct training and testing to determine seamless migration

THE FINALIZED RULES WILL HAVE IMPACT ON:

Market participants should minimize manual isolated process and transition to a centralized automated workflow potentially helping to reduce the chances of default

Trading
- The settlement cycle timelines have been shortened to **T+1 from the current settlement cycle of T+2**

Broker Dealer
- Policies and procedures are to **determine Same Day Affirmation and Allocation** targets are being followed

Investment Advisors
- Additional responsibility to **maintain records** of Allocation and Affirmation sent/received with date & time stamp

Central Matching Service Provider
- Additional requirement to have **written policies & procedures** to facilitate STP and file report for the same

Forex trade participants
- Firms involved in **Foreign Exchange Settlement** should revisit process flows and modify as there will be markets still operating in T+2

Operations
- All broker-dealers and firms should assess their **business operations as well as technological** impacts to comply with regulatory requirements

[1]*SEC.gov | SEC Finalizes Rules to Reduce Risks in Clearance and Settlement.*

Where should firms focus?

An overview of the potential impact on policies and procedures around some of the key functions is provided below.

Allocation & Affirmation

- The final rule states that firms must allocate trades as soon as technologically practical but no later than end of day on trade date (T). Industry recommends to allocate the trades latest by 7:00 PM ET on trade date.
- The affirmation deadline for institutional trade affirmation at DTCC is changing from 11:30AM ET on T+1 to 9:00PM ET on T.
- The timing of the CNS Projection Report has changed. The new timing is 2:00AM ET on T+1, and the midday projection file is moving to 5:00PM ET on T+1.

Security Lending

- The stock loan legally binding recall time will continue to be determined per the securities lending agreement in effect between the lender and the borrower. The industry recommends 11:59PM ET on T recall cutoff as "leading practice".
- Margin Calculations Processes will require a revisit.
- Organizations should also review existing Master Securities Loan Agreements and adjust as required for a T+1 settlement.

Prime Brokers

- The Executing and Prime brokers will need to submit their trades to NSCC for CNS clearing prior to the proposed 9:00PM ET on T as agreed by DTCC and the T+1 IWG.
- Disaffirmation of trades between 9:00PM ET on T to 1:30PM ET on T+1 will result in reversal transactions being generated by NSCC for same day settlement.
- Disaffirmation of trades between 1:31PM ET on T+1 to 5:00PM ET on T+ 1 will result in reversal transactions being generated by NSCC for the next business day after settlement (S+1).

Written Agreements vs Policy & Procedures

The Commission is modifying Rule 15c6-2 to provide two options for market participants to comply with the rule: written agreements or written policies and procedures.

Written Agreements

- Written agreement require market participants to establish individualized agreements that outline the operational arrangements for each relevant relationship.
- The written agreements option is useful for broker-dealers who already have existing agreements in place with their customers' advisers, custodians, or other agents.
- The written agreements requirement may be burdensome and impractical in cases where agreements do not already exist or where third parties are involved in the process.

Written Policies & Procedures

- Written policies and procedures should address the timing of allocations, confirmations, and affirmations, include a communication plan with market participants, describe the broker-dealer's ability to monitor compliance, develop controls and supervisory procedures, and establish metrics to measure compliance.
- This option is beneficial for market participants who do not have existing agreements or prefer a more flexible approach.
- They should be written, established, implemented, maintained, and enforced by the compliance date, with ongoing updates or revisions as required.

The Commission believes that both options can achieve the same goals and market participants can choose the approach that best suits their business models, customer base, securities offered, and commercial relationships.[2]

Market participants should determine that their policies and procedures are reasonably designed to achieve timely settlement and address potential systemic failures within their own processes.

[2] SEC.gov | SEC Finalizes Rules to Reduce Risks in Clearance and Settlement.

Elements of Policy and Procedures

Policies and procedures should be reasonably designed to include the five specific elements as described below.
We have used the example of a broker-dealer to explain the concept.

Technology and Operation

Identify and describe any technology systems, operations, and processes that the broker-dealer uses to coordinate with other relevant parties, including investment advisers and custodians, to determine completion of the allocation, confirmation, or affirmation process for the transaction.

Time Frame

Set target time frames on trade date for completing the allocation, confirmation, and affirmation for the transaction.

Communication

Describe the procedures that the broker-dealer will follow to determine the prompt communication of trade information, investigate any discrepancies in trade information, and adjust trade information to help confirm that the allocation, confirmation, and affirmation can be completed by the target time frames on trade date.

Addressing Delays

Describe how the broker-dealer plans to identify and address delays if another party, including an investment adviser or a custodian, is not promptly completing the allocation or affirmation for the transaction, or if the broker-dealer experiences delays in promptly completing the confirmation.

Monitoring

Measure, monitor, and document the rates of allocations, confirmations, and affirmations completed within the target time frames, as well as the rates of allocations, confirmations, and affirmations completed as soon as technologically practicable and no later than the end of trade date.

Other Focus Areas

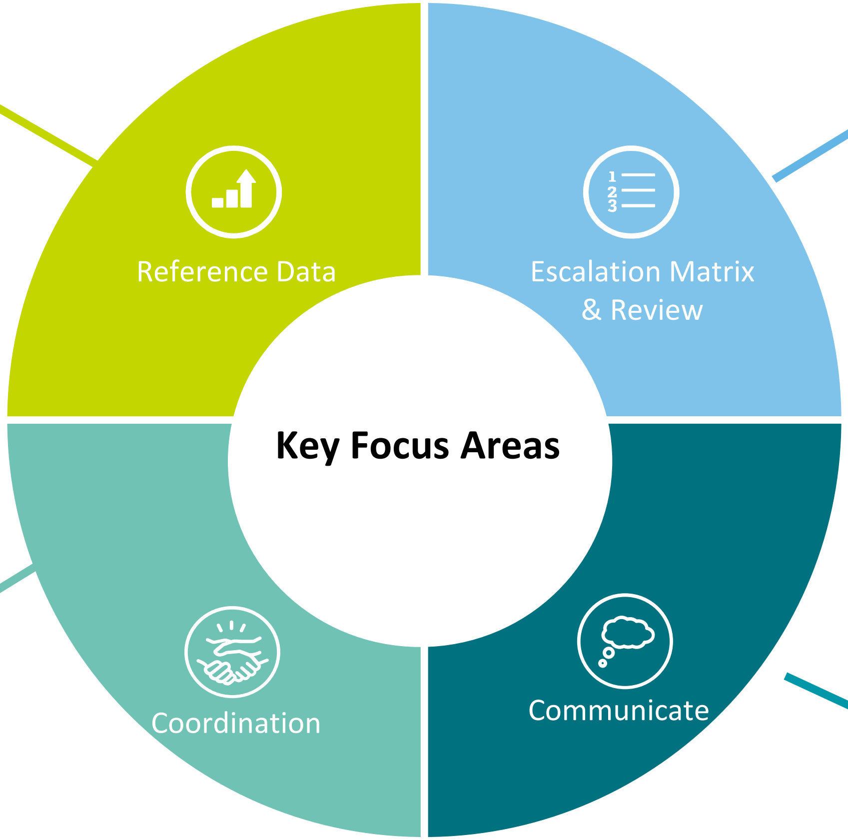
Below are additional key areas that firms should consider.

Reference Data

- Organizations should consider update their reference data (e.g., the asset type, counterparty information), security, pricing data, and standardized settlement instructions (SSIs).
- Policies and Procedures need to be updated for a Security type based on specific existing applicable rules (E.g., MSRB rules for Municipal Securities).

Coordination With IT Vendors and Stakeholders

- Coordinate with IT vendors to understand their transition plans and establish an escalation matrix for IT vendors and timelines (in compliance with firm policies).
- Coordinate with stakeholders to understand their timelines for upgrading systems/policies and procedures for testing and establish an escalation matrix for stakeholders for any issues on the other end.



Escalation Matrix, BCP & Review

- The escalation matrix should be updated with the timelines for escalation, as well as the contact information for key stakeholders. It should be reviewed and updated regularly.
- Guidelines should be clear and concise for policy owners to review their existing policies and procedures determining that they are aligned with the new settlement cycle and address any potential risks or gaps.
- The Business Continuity plan should include identifying potential risks, developing mitigation strategies, and testing the plan regularly. It should be communicated to all stakeholders.

Communication with Stakeholders

- Modernizing Communication Channels for Trade Away Processes.
- Enhancing Communication Efficiency Among Affirming Parties.

Illustrative approach for revisiting policies

A framework for updating policies can be found below, which provides a step-by-step approach

Identify scope of work, stakeholders, documents, and technology involved

- Identify all stakeholders
- Identify the IT systems and infrastructure & manual processes
- Identify the specific requirements and considerations for each type of financial instrument
- Identify the challenges and implications of coordinating settlement activities across different time zones

Develop & design policies and procedures

- Develop broad policies and procedures with requirements, roles and responsibilities of each stakeholder
- Establish protocols for trade processing, asset servicing, documentation, and exception handling
- Determine compliance with regulatory requirements and industry leading practices

Exceptions handling & documentations

- Draft protocols for handling exceptions and discrepancies
- Establish clear documentation procedures to record and resolve any issues or disputes
- Implement broad monitoring and reporting mechanisms to track and address exceptions in a timely manner

Implement, review & update

- Regularly review and update the policies and procedures to adapt to changing market conditions and regulatory requirements
- Conduct periodic audits and assessments by Policy Owners to determine compliance
- Identify areas for improvement by staying informed about industry developments and leading practices.

Educate & train

- Provide broad training and education programs
- FAQ on Policies & Procedures
- Foster a culture of compliance and continuous learning to facilitate a smooth transition to the T+1 settlement cycle

How can Deloitte help?

Deloitte is well positioned to help accelerate the development and delivery of policies and procedures that are practical, effective and will achieve the required level of adoption. We leverage our deep understanding of the capital market with a well-balanced team of individuals who have regulatory and business experience.

Supervisory, Regulatory and Compliance Experience

We aid companies in addressing legal and regulatory compliance while establishing effective oversight processes:

- We bring strong supervisory, regulatory and compliance credentials and demonstrated ability to leverage insights into leading practices.
- We provide advisory services to numerous industry and regulatory groups in defining compliance standards and measures and drafting policies and procedures.

Broker-Dealer and Investment Advisory Experience

- Our team has strong history of effective project delivery across broker-dealers and investment advisors.
- Our collective experience with broker-dealers and investment advisors as well as our regulatory and risk management background – enables us to understand the breadth and importance of effective policy and procedure.

Banking and Capital Markets

Deloitte offers tailored insights across banking and capital markets through diverse experience:

- Serving our clients locally with access to our organization's global resources and industry experience.
- Leveraging extensive industry knowledge, advanced research, reports, and surveys to lead strategic initiatives and shape the future of your business.

Accelerated Settlement Experience

- We helped to facilitate the industry transition to T+2 settlement and assisted firms' implementation
- Published T+2 Industry Implementation Playbook to support industry's migration to T+2 in 2017
- Supported industry-wide analysis, planning, and testing protocols through T+2 transition in coordination with industry leadership
- Supported leading firms' T+2 technical and operational implementation and go-live readiness activities

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