CCMA ACMC Canadian Capital Markets Association
Association canadienne des marchés des capitaux

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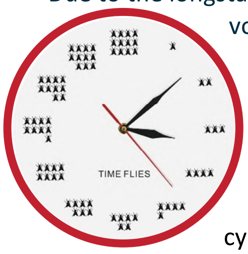
LET'S TALK T+1

Montreal's financial centre (credit: Vent du sud 1129717294)

We can do this the hard way, or the better way…



Due to the longstanding interconnectivity of North-American markets (as evidenced by the many interlisted securities, and high volumes and values of cross-border trades), the standard securities settlement cycle in Canada must be the same as that in the United States to avoid detrimental effects on Canadian investors and capital markets. With the U.S. announcing a move to a standard one-day settlement period (T+1, down from the current T+2) in 2024, Canadian capital market stakeholders also need to make systems and procedural changes to reduce by a day the time between trade date and settlement date.

But the goal isn't just being able to settle by 4 p.m. ET on T+1. Rather, to get the full benefit of a shorter settlement cycle – that is, to reduce and free up the capital otherwise needed on T+1 to collateralize the risk that transactions will not settle – firms also must enter transactions, allocate block trades, make corrections, and confirm all trade details on trade date.

In the news…

Canada's regulators on T+1:
Staff of the Canadian Securities Administrators published Staff Notice 24-318 *Preparing for the Implementation of T+1 Settlement* on February 3, 2022 to raise awareness of the Canadian securities industry's intention to shorten the standard settlement cycle for most trades in securities from two days after the date of a trade (T+2) to one day after trade date (T+1). The Notice states: "We encourage industry participants, including registrants, marketplaces, and other capital market stakeholders, to prepare for the transition to T+1 and to raise any specific concerns related to the transition."

The U.S. Securities and Exchange Commission (SEC) proposed T+1 rule amendments:
The SEC issued a 247-page proposal, Shortening the Securities Transaction Settlement Cycle *(SEC File No. S7-05-22, Request for Comments on T+1)*, on February 9, 2022. It includes 153 questions, many regarding T+0. The proposed rule changes, if enacted as drafted, would take effect **no later than March 31, 2024**, and would, among other things:

- Shorten the standard settlement cycle for most securities transactions from T+2 to T+1 *(amendments to 17 CFR 240.15c6-1)*
- Prohibit broker-dealers from entering into contracts with institutional customers unless the contracts require these parties to complete allocations, confirmations, and affirmations by the end of trade date, arguably making broker-dealers liable for customers failing to complete these processes by the end of trade date *(new 17 CFR 240.15c6-2)*
- Require investment advisers that are parties to contracts under new Rule 15c6-2 to keep records of their allocations, confirmations, and affirmations *(amendments to 17 CFR 275.204-2)*
- Require clearing agency central-matching-service providers (CMSPs) to establish policies and procedures to facilitate straight-through processing *(new Exchange Act Rule 17Ad-27)*.

The CCMA, like the U.S. Securities Industry and Financial Markets Association (SIFMA), The Depository Trust and Clearing Corporation (DTCC), Investment Company Institute (ICI), and others, will respond to the SEC's proposal. Canadian firms also may send their own responses, **due no later than April 11, 2022,** to comments@sec.gov.

Committee Updates

T+1 Steering Committee (T1SC): At February and March 2022 meetings, T1SC members discussed a number of issues, including these:

- ***OWG-007 – Corporate Actions:*** **Issue closed;** no industrywide changes required although the calculation of the ex-dividend date (to receive an upcoming dividend associated with a security, investors must have bought the stock before this date) must be accurate.

Also, in the T+1 environment, the ex-date and due-bill redemption date will be the same. Finally, the Canadian market will follow DTCC's proposal to eliminate protect/letter-of-guarantee periods related to voluntary event expiries: tendered shares will have to be delivered to the depositary agent by the expiry date/time of the offer.

- ***LRWG-005 – National Instrument (NI) 81-104 Alternative Mutual Funds:*** **Closed;** no action required. Most of NI 81-104 already has been repealed, including the part that had referred to the settlement period in NI 81-102 *Investment Funds*.
- ***LRWG-010 – Labour-Sponsored Investment Funds (LSIFs):*** **Closed;** no action required. As LSIFs are governed by contract, firms will have to verify the status of each LSIF because it is expected that some LSIFs will move to T+1 and others may not. In the T+3 to T+2 move, 55 of 101 LSIFs moved to T+2.

T1SC members also formally approved the CCMA's Communications Plan and a draft response to the SEC's proposed T+1 rules. The CCMA response, which focuses only on particularly pressing issues in the SEC's request for comments, will be sent in April 2022.

Operations Working Group (OWG): The CCMA has engaged an industry expert to update the CDS Job Scheduler (Issue OWG-013) – the lynchpin for almost everything that needs to be done to ensure trades settle on time on T+1. This work includes:

- Documenting the current end-of-day batch-processing schedule, setting out the current start and end time for each job stream
- Identifying inputs to and outputs from each processing function (trade entry and correction, block trade allocation, trade reconciliation, and confirmation of domestic, cross-border, and international trades)
- Investigating and documenting relevant aspects of service bureau, vendor and participant business processes for each CDS job stream
- Highlighting roadblocks to T+1 securities settlement
- Proposing revisions to current timelines to enable T+1 transition.

Findings and recommended changes will be presented to OWG members for review at the end of April 2022, with final recommendations to be taken to the T1SC for approval in late spring.

As well, OWG members are reviewing securities listed in the T+1 Asset List to begin the process of confirming what securities will, or are expected to, move to a standard settlement cycle of T+1. Comments received by the end of April will be discussed and amended/approved by the OWG before the updated list is sent to the T1SC for approval by the end of May. The approved list version will be released in June for broad public comment.

Work also is proceeding on two additional issues: Securities Lending (OWG-009) and ETF Creation/Redemption (OWG-003).

Phil Zywot, Board Director of the Canadian Securities Lending Association (CASLA), explained that agent lenders will need to receive timely notification on trade date – that is, no more one-day cushion – of what securities they will need to settle on behalf of the beneficial owners. Agent lenders will have to become more efficient in determining which securities are available, out on loan, and available for substitution, and which positions must be recalled. Borrowers will have to react to recalls with greater urgency given there is one fewer day to identify an alternative source of supply. Work to identify solutions is underway by the securities lending sector.

Pat Dunwoody, Executive Director of the Canadian ETF Association, said CETFA has a working group that is documenting all of the relevant creation and redemption processes, reports, and related timelines within the ETF industry (creation is the process of buying underlying securities to 'wrap' into the ETF structure, while redemption is the reverse: 'unwrapping' the instrument back into individual securities). Once this analysis is complete, CETFA will identify what may have to change to meet the needs of T+1 settlement.

Legal & Regulatory Working Group (LRWG): LRWG members continue to work their way through the committee's issue log. In upcoming meetings, members will begin to focus on whether, and if so what, changes are needed to rules of the Investment Industry Regulatory Organization of Canada (IIROC) and other entities.

Communications & Education Working Group (CEWG): In addition to an intended podcast and more FAQs, the committee is working on the first of three surveys – assessing how many firms are aware of and preparing for T+1.

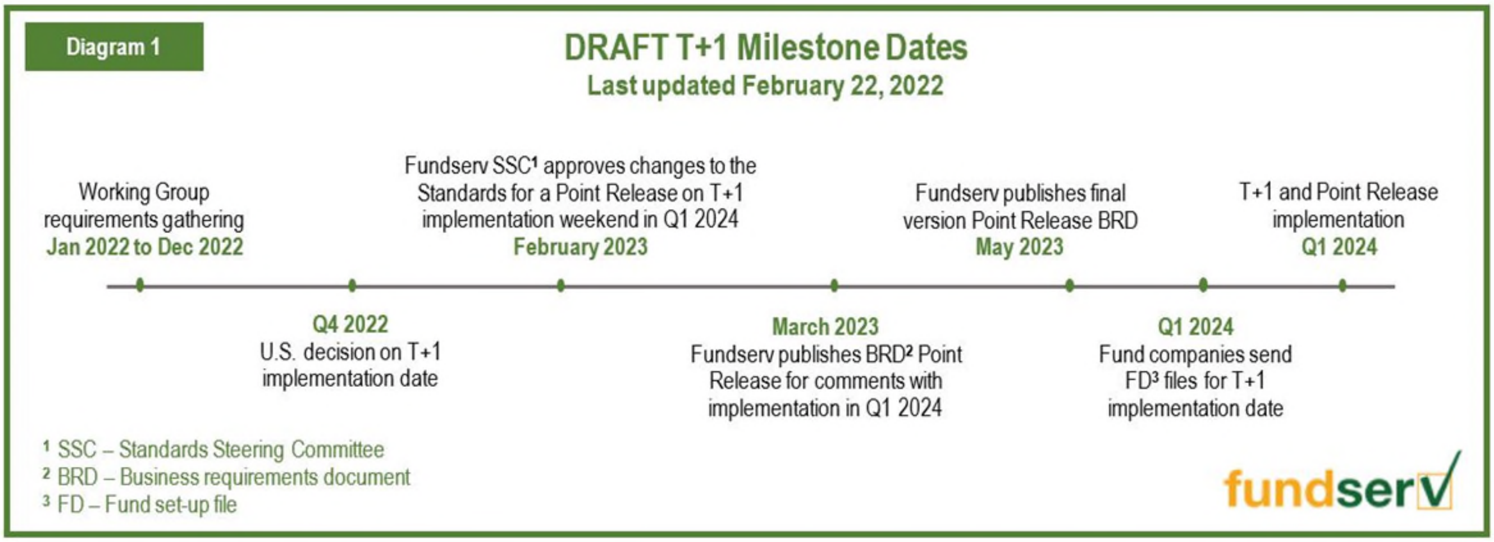
Mutual Funds Working Group (MFWG): Fundserv is confident that mutual funds will be ready to transition to T+1 when a transition date is set and that the majority of manufacturers will move their funds to settle on T+1 at that time to remain on the same cycle as the securities that make up their funds. Liquidity will be a challenge for some: any fund whose net redemptions exceed cash and near-cash (e.g., money-market) holdings will have to find a way to fund redemptions in less than a day's time. As happened when the standard settlement cycle was shortened to T+2, some mutual funds – for example, those with longer settlement cycles – may not move to T+1 *(see **Table 1**)*.

Table 1

Current settlement cycle	# of Funds, Etc.	Percentage
Settle on T+1	8,242	8%
Settle on T+2	**83,660**	84%
Subtotal T+1 or T+2	***91,902***	*92%*
Settle T+3 or more	8,070	8%
Total	**99,972**	100%

Source: Fundserv Fund Profiles (as at March 17, 2022)

Fundserv also has published a proposed schedule that aligns with the U.S. and Canadian debt and equity T+1 migration timelines *(see **Diagram 1**)*. This is a draft and will change once feedback has been received from Fundserv members.



Tips & To-do's

- ***Keep your eye on the matching and confirmation goal:*** While global events, month-/quarter-ends, and holidays all affect trade entry and confirmation rates, you want to see in your firm's data an overall rising trend in percentages of trades entered and confirmed by number and value. Check your firm's institutional trade-matching record against the industry average *(see **Table 2**)*.

Table 2

	Debt/Equity Trades Entered		Debt/Equity Trades Confirmed	
By end of T	% Industry by #	% Industry by $	% Industry by #	% Industry by $
Feb-22	84.6%	80.8%	39.1%	53.0%
Jan-22	83.1%	80.2%	36.4%	53.8%
Dec-21	83.0%	79.8%	35.6%	50.2%
Nov-21	84.9%	80.9%	34.3%	52.3%

Source: CDS Institutional Trade Processing Statistics

- ***Follow*** the CCMA on LinkedIn and please encourage colleagues and counterparts to do likewise. Why? Between issues of the CCMA's bimonthly newsletter and committee meetings, updates will be on LinkedIn.

Tools

- Want to know the current settlement status of funds by product type and settlement date? Visit Fundserv's easy-to-use Fund Profiles page.
- Not sure if your company is involved in T+1 yet or want to know who is participating? Here's a link to check on membership by committee and firm.

To come

- ***End-May 2022:*** The T+1 Asset List, recording what securities and fund categories are moving (or are expected to move) to a standard settlement cycle of T+1, will be released for industrywide comment after initial OWG input.
- ***End-May 2022:*** Get ready to answer the CCMA's T+1 Awareness Survey.
- ***June 7, 2022:*** The Investment Funds Institute of Canada (IFIC) welcomes a return to a live 2022 Operations Day, with livestream options for participants not able to join in person; a T+1 segment is featured, and the event is open to all *(registration on IFIC's website will open in April)*.

From Keith Evans, CCMA Executive Director:

"While we can't solve individual firm problems, we're going to do everything possible to present opportunities to find solutions."