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T+1 Settlement Efforts:
Canadian Outlook and Considerations

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BY LOU LESNIKA
Director, Product Management

As Director of Product Management, Lou is part of a team responsible for developing products and services that meet the sophisticated and evolving needs of CIBC Mellon's clients.

"Shortening the settlement cycle produces a number of benefits, including mitigating operational and systemic risk by reducing exposure between the parties to a trade, between the counterparties and central clearinghouses, and in terms of harmonization between various markets.

The Canadian Capital Markets Association (CCMA) announced Monday, May 27, 2024 as the Canadian T+1 start date.

The last date securities will be traded on the current two-day standard in Canada and the U.S. will be Friday, May 24, 2024.

The CCMA highlighted that capital markets participants in the U.S. and Canada will make the required systems changes to support a shortened standard securities settlement cycle on the weekend of May 25/26, 2024.

According to the CCMA, the first day of T+1 trading will be the next business day in both countries. Monday, May 27, 2024 in Canada and Tuesday, May 28, 2024 in the U.S.

Canadian and U.S. market stakeholders including U.S. and Canadian central depositories, the Canadian Capital Markets Association (CCMA), and industry participants including CIBC Mellon are preparing to shorten the settlement cycle in Canada to T+1, the day after trade date.

Given the substantial volume of cross-border trading activity between Canada and the United States, the CCMA will align the Canadian market timelines to those of the U.S. - a project supported by Canadian securities regulators.

The Canadian Securities Administrators (CSA) published for comment proposed rule amendments to National Instrument 24-101 Institutional Trade Matching and Settlement (NI 24-101). According to the CSA, the proposed amendments focus on facilitating the shortening of the standard settlement cycle for institutional equity and long-term debt market trades in Canada to T+1 from T+2 in alignment with upcoming changes to the U.S. settlement cycle.

The Depository Trust & Clearing Corporation's (DTCC) latest document "T+1 Securities Settlement Industry Implementation Playbook" helps clients prepare for the transition to an accelerated settlement cycle in 2024.

Shortening the settlement cycle produces a number of benefits, including mitigating operational and systemic risk by reducing exposure between the parties to a trade, between the counterparties and central clearinghouses, and in terms of harmonization between various markets. In addition, sell-side firms are expected to see an overall reduction in collateral that they need to post to the depository on a daily basis. However, buy-side firms will have to allocate purchases on trade date and are expected to be able to complete transactions sooner, meaning that funds on sale will be available to them one day earlier.

THE CANADIAN CAPITAL MARKETS ASSOCIATION

“The CCMA and its industry partners are working together on the T+1 project. Aligning with the U.S is critical for Canada, but this also means that the industry will have new challenges around this initiative to deal with. For instance, there will be a misalignment with settlement dates in Europe that will need to be managed. The current NI 24-101 Institutional Trade Matching and Settlement has a matching deadline of T+1 at noon that will need to be adjusted. The transition to T+2 in 2017 had market participants essentially doing post-trade activities faster than when the settlement standard was T+2, with effectively two overnight batch processing cycles to ensure that trades were ready to settle. That included reporting the trades, reconciling the trades, allocating block trades, and confirming the trade details. Now, to achieve a T+1 settlement cycle, all of these activities should be done on trade date, or in the overnight batch, between T and T+1.

-Keith Evans, Executive Director,
Canadian Capital Markets Association

The CCMA will continue engaging with stakeholders in Canada, the U.S., and other affected countries on multiple challenges.

According to the CCMA's news release, capital markets participants in Canada are involved in a series of major regulatory and market structure initiatives (e.g. enhanced cost disclosure and the TMX/CDS Post-Trade Modernization project). Furthermore, markets in Europe, the U.K., and Asia will continue to operate on a T+2 settlement cycle for the immediate future. As a result of the time zone differences, the CCMA outlines a few challenges that remain including how to affirm a trade on T when it is already T+1 in a counterparty's country, and how to settle a trade requiring foreign currency conversion on T+1 when transactions in major currencies settle on a T+2 basis.

The CCMA led national industry-wide efforts to reduce the settlement cycle to T+3 from T+5 in 1995, and to T+2 from T+3 in 2017, on the same day as the U.S. given Canada's and the U.S.'s highly inter-related capital markets. After the latest transition, CCMA members completed a T+2 Project – Post-Mortem Report (2018), which provides guidance for CCMA members working on the T+1 project.

For more information, and to keep up to date on the CCMA's newsletters and FAQs, visit http://www.ccma-acmc.ca/

SECURITIES LENDING IMPLICATIONS

As the industry continuously looks to improve the efficiency and resiliency of securities lending markets, standardization, digitization and governance will remain key focus areas.

Given T+1's direct effect on securities finance, it will likely be at the forefront of many standardization initiatives. There is anticipation of more pressure in the warm and hard-to-borrow space. Often, the agent lender will receive the sale notification either late in the day or even on the following day, resulting in the recall being processed a day later than needed to achieve T+1 settlement. Under T+1, the recall would have to be sent out on T – trade date – or the borrower will not have time to source alternative or additional supply elsewhere or to buy back the position. Agent lenders may have to hold back larger buffers to accommodate late sales in less liquid names, thereby reducing maximum revenue generation on the total position.

With less time to instruct foreign exchange movements, compounded by diverging standard securities (T+1) and foreign currency (T+2) settlement cycles, there will be extra pressure to confirm / match transaction details on the trade date.

The industry as a whole may need to look to modify deadlines for accepting and processing recalls, which may need to be extended on the evening of T. Beneficial owners will likely be required to explore ways to provide notifications more efficiently to their agent lender, whether that is through automation or some sort of improved or more frequent batch facility.

BENEFITS TO CLIENTS AND SECURITIES FIRMS

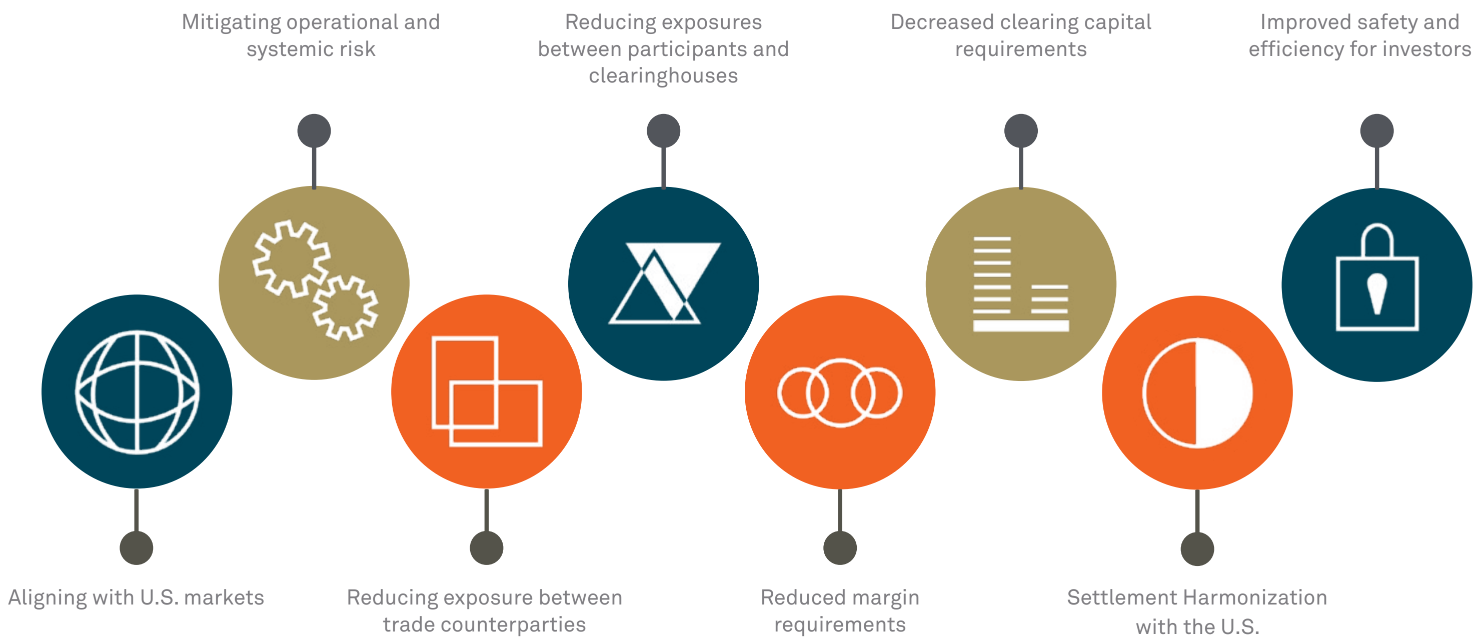
Of the range of benefits of the shortened cycle, arguably the most important are the certainty, safety and increased soundness of Canadian capital markets for participants. T+1 will promote reduced counterparty risk, reduced margin requirements, and decreased clearing capital requirements. The Canadian and U.S. market structure will also work to improve safety and efficiency for investors.

IMPACTED SECURITIES THAT WILL SETTLE ON T+1

Some examples of securities impacted by the settlement switch to T+1 include:

- Stocks/equities
- Corporate bonds/debentures
- Federal, provincial and municipal government bonds
- Convertible bonds

For a finalized list as at January 2023, please see the CCMA's website.



BENEFITS OF SHORTENING THE SETTLEMENT CYCLE:

CIBC MELLON AND T+1

CIBC Mellon is playing an active role in the readiness and consultations taking place across the industry leading up to the T+1 implementation. On top of creating a project team to assess the operational impacts of T+1, CIBC Mellon employees actively participate in various T+1 working groups with key industry stakeholders in order to stay at the forefront of regulatory and industry changes. In establishing a comprehensive team of knowledgeable professionals, we cannot only ensure our readiness but ensure we are supporting clients through this transition by means of providing localized insights.

CIBC Mellon participated actively on the T+2 project in 2016-2017. CIBC Mellon's custody system is currently settling trading activities across a wide range of settlement cycles. We are ready and able to handle T+1 settlement following implementation with the United States. We bring considerable settlement experience – in addition to our daily settlement activities, a number of CIBC Mellon employees were active participants during Canada's previous, successful shortening of the settlement cycle to T+2 from T+3 in 2017.

We are also taking steps with the relevant market utilities and entities to affirm that our technology and operational procedures are appropriately updated.

> “T+1 will promote reduced counterparty risk, reduced margin requirements, decreased clearing capital requirements and continued settlement harmonization with the U.S. The Canadian and U.S. market structure will also work to improve safety and efficiency for investors.

CIBC Mellon Industry Perspectives

In this episode of CIBC Mellon Industry Perspectives, Lou Lesnika, Director of Product at CIBC Mellon, hosts a discussion with Keith Evans, Executive Director of the Canadian Capital Markets Association (CCMA) on T+1 settlement plans in Canada, including operational considerations. For more information, listen to our podcast.

For more information

We will continue to provide clients with updates as they relate to T+1 settlement in Canada and CIBC Mellon's supportive efforts. If you have any questions, please reach out to Lou Lesnika or your Relationship Manager.

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