



# US T+2 Settlement - Buy Side Impacts

Post Trade Processing Update | August 2015

White  
Paper



The proposed US migration to two day settlement (T+2) by Q3 2017 will require significant preparatory work. However, the anticipated benefits are clear: reduced counterparty risk, lower margin cover and less stringent liquidity demands.

a product from  
**corfinancial.**

london | boston | new york

# The proposed US migration to two day settlement (T+2) by Q3 2017 will require significant amounts of preparatory work. However, the anticipated benefits are clear: reduced counterparty risk, lower margin cover and less stringent liquidity demands. Is it time to start considering post trade automation?

In their recently published paper the T + 2 Industry Steering Committee highlighted the significant amounts of preparatory work organizations would need to complete if they were to migrate successfully to a T + 2 operating environment.

They equally state some key benefits such as lower counterparty risk, a decrease in margin and a reduction in liquidity demands. They report that the “industry stakeholders reached consensus and support the migration to T+2” and suggest that the average clearing fund requirements for clearing members is expected to decrease by 15-24%.

Of course, the move from T+3 to T+2 will have an impact and Europe’s recent experience of migrating to T+2 exposed just how much effort really is required by both individual firms and the industry as a whole.

Small firms, especially those with limited IT resources, have to consider carefully how they would change their systems to accommodate the new settlement cycle. Even in fairly substantial

asset managers, there remain many manual post trade processes – meaning settlement affirmation often takes longer than T+2. Post-trade has historically been considered an unwelcome cost of trading and therefore has not received the investment comparable with that of the front office. However, the move to T+2 could be the catalyst firms need to fix manual processes that not only waste time and money but add risk into the system.

Our opinion is to support the work of the T+2 Industry Steering Committee and in fact using post trade automation organizations should start preparing for T+2 now. The BCG report highlights that the US market could achieve approx. \$195M in immediate savings – some of this (\$25M) is related to a reduction in clearing fund contributions but the majority (\$170M) is associated with operational cost savings. If the wider opportunity costs are considered, then we think a multiple of these savings can be achieved through improved liquidity and lower risk.



A shortened settlement cycle could profoundly enhance the health, robustness, and resiliency of our capital markets. In particular, lower margin requirements will allow more trading to occur, and thus deepen market liquidity. A shortened settlement cycle could also mitigate systemic risk by reducing exposure between the parties to a trade, between the counterparties to the clearinghouse, and for the clearinghouse itself. In sum, the effort and expense required to reach T+2 should pay considerable dividends.

*Commissioner Luis A. Aguilar, US Securities and Exchange Commission, 16th July 2015*

In an era of thin margins, tight liquidity and continuing risk, investing in efficient post trade processing can deliver an advantage.

## Only electronic trade matching achieves post trade efficiency.

In making any business assessment the primary aim is to reduce the risk of operational failure, delay or processing errors. These errors not only damage the reputation of the business but ultimately carry cost. At the same time, razor thin margins and increased regulatory compliance require savings to be achieved across the entire value chain.

Manual post-trade processing introduces the risk of human error, and not just for an asset manager - brokers and administrators have to translate data into a format suitable to go through their systems. Let alone the simple fact that manual processing takes significantly more time, even when trades match exactly.

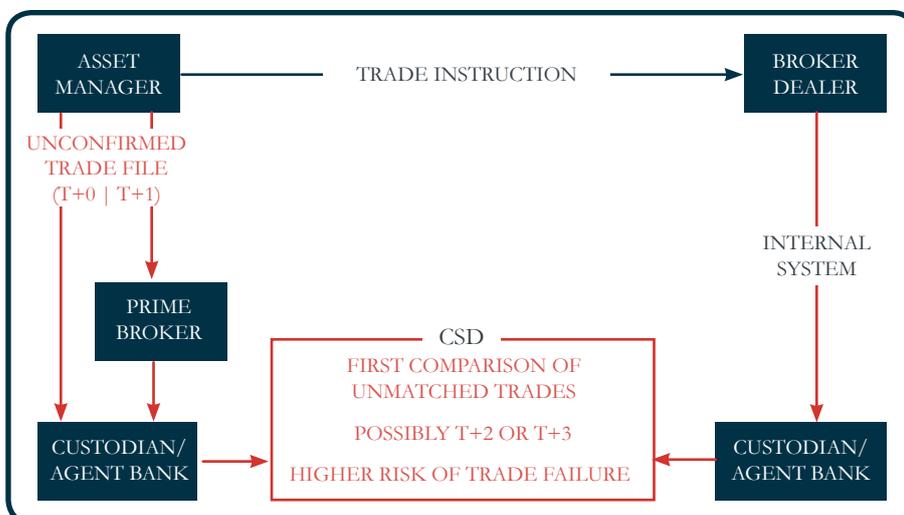
Institutional investors do consider an asset manager's operational infrastructure, as well as the performance return of investment teams, in their judgement of capability and control. When an entity is entrusted with handling client money poor processing efficiency can mean additional operational cost and ultimately higher overall fees, as well as greater risk. Fund growth from new investments is increasingly dependent on scoring highly in both.

Automated systems like salerio should be able to highlight trade confirmation issues quickly and efficiently to the Investment Manager, greatly reducing the risk from trade booking errors and avoiding any potential financial impact. Similarly, a sufficiently robust electronic confirmation process allows Investment Managers to transmit their settlement messages to their custodians rapidly ensuring settlement instructions are in the market before settlement date, avoiding unnecessary failed trade issues and charges.

This drive for efficiency is evidenced further by some brokers in the marketplace who are actually collecting metrics about their clients' trading activities to quantify how these errors add further cost. Their purpose is initially to educate their clients about the costs of doing business together, but is really to encourage greater efficiency from those asset managers currently causing brokers to spend money on normalising trade data from the client. The pressure on broker margins has increased along with the higher regulation and compliance costs in recent years. Everyone gains by lower costs if these inefficiencies can be eliminated.

If that trend continues asset managers who do not change the way they do business now may well see the traditional administrative support they have enjoyed from their brokers at best become more costly or, at worst, removed.

FIG. 1: THE SETTLEMENT CYCLE **WITHOUT** ELECTRONIC TRADE CONFIRMATION (ETC)



## Process problems

We illustrate in figure 1 how unconfirmed trade files despatched to the next step in the settlement cycle (custodian, prime broker or 3rd party administrator) run a higher risk of failing to settle on the agreed date. It is largely irrelevant what route to the CSD the asset manager takes, as all parties in the process may be dealing with flawed information. The first time any differences in the asset

manager's and the executing broker's files are likely to be discovered is at the CSD, probably on T+2 or T+3 – but in all likelihood too late for the trade to be repaired in time.

The knock-on effect of not being able to rely 100% on trade information is that trading positions may be misreported, if the assumptions is that all trades will settle when due.

## Proposed solution

The Industry Steering Committee and its various working groups have been remarkably speedy, particularly by the past performance standards of the Financial Services industry, to identify the technology, behavioural, regulatory and other changes required to facilitate an industry move to T+2 in the US.

The key focus of their work is the confirmation and settlement of trades, which remain just as valid to asset managers anywhere in the world

In figure 2 it is illustrated how the inclusion of electronic trade confirmation can improve the flow. Placing a control mechanism between the asset manager's trading desk and the broker is vital in identifying issues promptly. Issues will become apparent on T rather than T+2 or later. Therefore, incorporating an automated, exceptions based process at this stage in the trade lifecycle eradicates unnecessary post trade processing risk. The aim here is to identify

potential causes of settlement failure as early and clearly as possible not hand holding every transaction through the workflow.

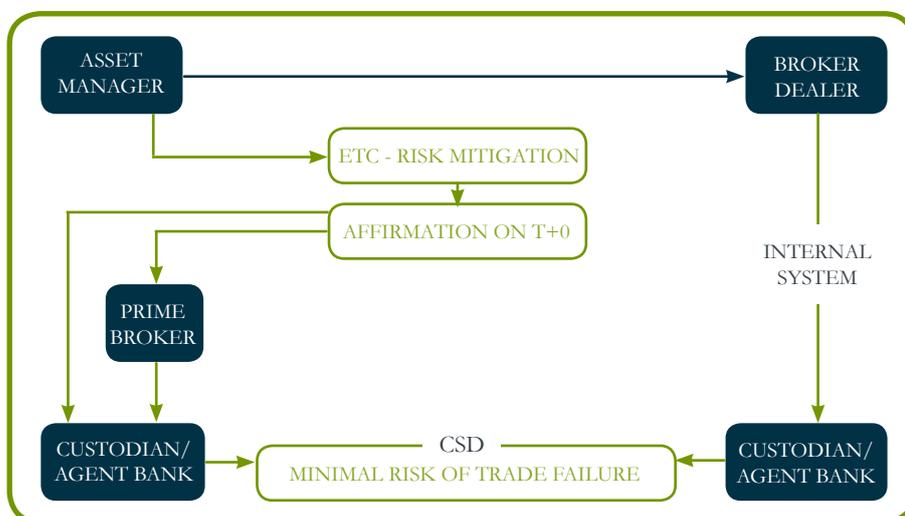
Although a simple idea, electronic trade confirmation across multi assets classes, which also covers the requirements of differing regions is no mean feat.

There are several electronic trade confirmation options available, which each provide differing degrees of asset coverage, connectivity to numerous industry utilities and flexibility to work within your own business rules. You need to assess the goodness of fit and the real core competencies built into each system as well as their ability to integrate to your own infrastructure and any other third parties, whether real-time or aggregated end of day feeds.

Whatever automated solution you chose, it should reduce the risk for all parties, as the accuracy of information means assumed post trade positions can be relied upon from outset and thereby reduce the potential for settlement cycle problems to impact on trading capability.

## So why should buy side firms consider salerio's electronic confirmation capabilities to automate their post trade processing?

FIG. 2 : THE SETTLEMENT CYCLE WITH ELECTRONIC TRADE CONFIRMATION (ETC)



**FLEXIBILITY:** salerio offers an electronic trade confirmation for International and US Domestic equity and fixed income instruments as well as coverage for FX and other treasury instruments. The different workflows are all built into one implementation with a single point of exception management for all, removing the need for the business user to interact with multiple systems and interfaces. To enable this salerio connects to

various industry utilities such as Omgeo Central Trade Manager (CTM), Oasys, TradeSuite and SWIFT (GETC). This provides the required coverage but also the choice of which method to use, based on your specific requirements.

**SPECIALISM:** salerio specialises in automating post trade confirmation and settlement. It is the only thing we do, so we are exceptionally good at integrating with your internal systems, matching electronically with your broker dealers, and issuing appropriate settlement instructions to custodians in the knowledge that the information is accurate, meaning trades will not fail for that reason.

salerio comes out of the box with standardized routes to cater for the subtleties of your infrastructure. We have seen almost every variation possible, all of which have been built into our standard product.

**SUPERIOR EXCEPTIONS MANAGEMENT:** salerio not only identify exceptions, it isolates them, prioritizes their urgency and delivers only the exceptions directly to processing teams for manual intervention. We call that Straight-To-Processing – there is no hunting through queues or endless searching of spreadsheets.

**FUTURE PROOF:** Investing in salerio now is future-proofing your business, as every implementation contains all options, allowing customers to turn on exactly what they require, today and tomorrow. Moreover, functionality not required today but may be needed in the future is available immediately.

**VALUE:** Because salerio is a standard product, implementation is fast, much less complex than many other products and therefore significantly less expensive. You start enjoying the commercial benefits in weeks (not many months or years), while system upgrades are much simpler to carry out ensuring our client base benefits from the continued additions and improvements being made.

**TRUSTED:** We are extremely proud of the trust our clients put in salerio. We work very much as partners with them, understanding what they are trying to achieve and helping to realise their

goals in the most cost-effective manner we can. We build our product roadmap together.

To read the US T+2 Industry Steering Committee White Paper, go to <http://www.ust2.com/pdfs/ssc.pdf> ■



Salerio is used by asset management, hedge fund and third party outsourcing businesses operating across the globe. We already work with some of the largest US asset managers. We believe in talking to us we'd be able to demonstrate how Salerio could deliver efficiency and reduce cost of your current post trade operations. We can help you through the preparation necessary for T+2. Salerio can deliver tangible added value to your business.

Find out more about why our customers are enjoying the benefits of salerio. How can we help?

call 0207 877 4045  
email [info@corfinancialgroup.com](mailto:info@corfinancialgroup.com)  
visit [corfinancialgroup.com](http://corfinancialgroup.com)

solutions from

**corfinancial.**

london | boston | new york.

 **salerio.**

Automates the flow of securities and treasury trades from matching through to settlement.

 **bitarisk.**

Suite of applications addressing needs of private wealth managers, investment advisors, asset managers, quant teams.

 **paragon.**

Fixed-income accounting hub delivers front-to-back office portfolio accounting and processing solutions.

 **sanctionsmonitor.**

A sophisticated, easy-to-implement and easy-to-use sanctions monitoring, auditing and reporting tool.

 **abraxsys.**

Comprehensive integrated banking platform delivering an industry-leading banking service.

 **costars.**

Retail fund/transfer agency solution providing end-to-end administration for collective investments.

 **almeter.**

Control financial and business risk by assessing the impact of varying interest rate scenarios and hedging activities.

 **kycmonitor.**

Case management solution to provide clear evidence to the relevant authorities that effective and sufficiently robust AML controls are in place.