FDIC Announcement to Highlight Actions that Banks Should Take to Prepare for the Shortening of the Securities Transaction Settlement Cycle

Background

On March 22, 2017, the SEC adopted an amendment to the Securities Transaction Settlement Cycle Rule 15c6-1 shortening the regular settlement cycle from T+3 to T+2 for many U.S. securities including equities, corporate bonds, unit investment trusts—and financial instruments composed of these products—when these securities are traded on the secondary market. See 82 Fed. Reg. 15564 (March 29, 2017). SEC's compliance date for this amendment is September 5, 2017 (T+2 compliance date). In addition, on March 28, 2017, the Municipal Securities Rulemaking Board (MSRB) made similar changes to the settlement cycle for municipal securities. Other securities self-regulatory organizations have finalized, or plan to finalize, rules necessary to implement the new settlement cycle and related processes.

These rule changes, made in conjunction with a multi-year securities industry initiative to shorten the settlement cycle, are intended to reduce counterparty risk, lower margin requirements for clearing agency members, reduce procyclical margin and liquidity demands during periods of market volatility, and better align the U.S. securities transaction settlement requirements with other markets across the globe. Industry participants have been developing and testing the necessary changes to processes and systems to implement this industry-wide change. These changes to the securities trading clearance and settlement process and, indirectly, to income processing, corporate action processing, securities lending, and other related processes significantly affect a broad range of market participants and services including:

- Financial institutions;
- Financial market utilities that provide central counterparty services and central securities depository services;
- Matching and electronic trade confirmation services;
- Broker-dealers;
- Municipal securities dealers;
- Custodians;
- Transfer agents;
- Institutional and retail investors;
- Asset managers;
- Securities lending agents; and
- Systems and service providers that support these activities.

Guidance

The FDIC anticipates that, as of the T+2 compliance date, FDIC-supervised institutions would not effect or enter into a contract for the purchase or sale of an affected security that provides for payment of funds or delivery of securities later than the second business day after the date of the contract, unless otherwise expressly agreed to by the parties at the time of the transaction.

Institution management and the directorate should take appropriate steps to ensure they are prepared for this industry-wide change to T+2 standards on September 5, 2017. Preparation includes identifying all lines of business, products, and activities that involve securities settlement and servicing. Institution management should also monitor regulatory changes that affect securities settlement and servicing, system and process changes at financial market utilities, custodians' system and process changes, and third-party system or service provider changes.

Based on the nature and scope of the institution's securities processing activities, management should determine what system and process changes or outreach may be needed for a smooth transition to T+2. Institution management should establish and follow an appropriate project plan for implementation. Issues management should consider when developing the project plan include:

- Changes to trust accounting or other securities processing systems;
- Changes to operational procedures for securities clearance and settlement, income processing, corporate action processing, and securities lending;
- Changes to client communications, agreements and disclosures that reflect settlement time frames;
- Oversight of third parties' T+2 implementation processes;
- Changes to service level agreements with third parties providing trade clearance and settlement, income processing, or other services affected by T+2 implementation;
- Training for employees that deal with securities clearance and settlement;
- Heightened focus on risk management practices and surveillance systems to effectively identify and address potential increases in failed trades or processing exceptions; and
- Contingency planning and staffing for the days leading up to and immediately following implementation.