

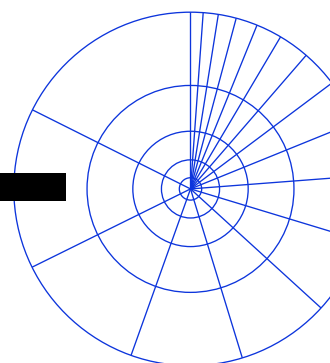
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Defy. Deploy. Run.

T+1 Settlement

December 2023

ESMA Call on evidence on shortening the settlement cycle to T+1



The European Securities and Markets Authority (ESMA) has launched a call for evidence on the shortening of the settlement cycle to T+1 (including T+0). The consultation is aimed at assessing the costs and benefits of a possible reduction of the settlement cycle in the European Union (EU) and identifying whether any regulatory action is needed to smoothen the impact for EU market participants of the planned shortening of the settlement cycle to T+1 in other jurisdictions, such as the US.

The consultation will also help ESMA to evaluate the impact on operations, costs and benefits, preconditions, and the impact on the EU's capital markets.

The background of this consultation is that in 2014, the Central Securities Depositories Regulation (CSDR) introduced the T+2 settlement cycle for a European harmonization and to limit the risk on cross-border settlements. Recently, the United States and Canada have adapted their settlement cycle to T+1, which will come into effect in May 2024. China and India are already operating on shortened cycles. Other jurisdictions such as the UK or Switzerland will evaluate a shortening cycle.

The **main drivers** behind the shortening of the settlement cycles include risk awareness, financial markets, and technological innovation. A strong risk awareness towards settlement and collateral risks has arisen. In addition, the EU need to analyse the current changes in due to other jurisdiction changes and might follow up to stay competitive. Nevertheless, the necessary changes in IT infrastructure and processes are fostering goals towards the Capital Market Union. Innovation such as Straight Through Processing (STP) technology and a high degree of automation potential might increase efficiency. The potential of Distributed Ledger Technology (DLT) and Artificial Intelligence (AI) can as well have a high impact.

— Challenges

However, financial institutions have to cope with intense challenges to implement T+1. Extensive operational changes must be introduced to realise.

A selection of the identified obstacles include:

1. Process compression of post trade activities within a shorter time window
2. Coordination of different entities such as Buy-Side, Sell-Side, Central Counter Parties (CCP), Central Securities Depositories (CSD)
3. Global alignment with different time zones and FX markets
4. Potential asset class or product dependencies
5. Compliance risks (potential introduction of a new settlement regime (harmonized requirements for settlement (as in RTS on settlement discipline 2018); alignment to CSDR Refit
6. The risks might be swapped to CSDR cash penalties for settlement fails

— Benefits

Shortening the settlement cycle to T+1 will bring about extended benefits. Although challenges are high, the credit and counterparty risks are expected to get highly limited. Therefore, less collateral requirements might be needed which leads to potential liquidity improvements for EU market participants. A high degree of automation will further increase efficiency in operational processes. In addition, the implementation might lead to an enhanced global settlement harmonization.

Overall, the shortening is expected to leverage the competitiveness and increase the attractiveness of EU financial markets.

— **LPA Consulting is your Partner for T+1. We support you with:**



1. Operational Post-Trade Process Impact Analysis thanks to our Front-To-Back-Office Expertise



2. Securities and Asset Class Analysis as specialized Capital Market Products Experts



3. Technological Infrastructure and Data Quality Check with our extensive IT- and Analytics Knowledge



4. Regulatory Analysis and Market Practice Check as long-term experienced Compliance and Market Experts

— **Get in Touch!**



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