

## Shorter Settlement Cycles are Vital.

### Timing STP's Entry is the Issue

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The Board of Directors of the Securities Industry Association unanimously approved the postponement of the initiative for settling securities the day following trade date (**T+1**). That announcement, made in June, was sensible. It postponed the decision regarding setting a cut-over date until 2004. The complementary decision, to set specific straight-through processing (STP) goals, was wise.

The industry is choosing to move forward rather than let the uncertainty in the marketplace, the close proximity to the terrorist attacks, and the exploding repercussions of corporate accountability scandals block progress.

No one questions the necessity of shortening the cycle. The continuing increase in trade volumes and extreme market volatility are just the more obvious manifestations of this. The goals of STP are valid: increasing the competitiveness of U.S. markets, cutting settlement costs and reducing systemic risk.

The only question is when the date for the conversion to **T+1** will be set. The original 2004 date was too close, the first postponement to 2005 was overwhelmed by the immediacies of dealing with the infrastructure destruction wrought by the WTC attacks. Until STP goes into effect, accruing the benefits from improving the process will be the target.

In just the past three years we have survived so many traumatic situations. The Internet bubble, affecting both the market and the implementation of systems, was followed by the technology non-event of Year 2000. The U.S. economy slowdown was accelerated by terrorism, both here and around the world. Main Street's faith in the U.S. markets was shaken by the perception that everyone – from the CEO down through the guys in accounting – was conspiring.

The result is a harsh reality that changes the justification for STP implementation. Cost reduction projects dominate, with regulatory response, revenue enhancement, competitive advantage, market pressure, and client demand following. As a result, infrastructure initiatives must deliver immediate benefits.

New regulatory initiatives, such as the know-your-customer rules thanks to the Patriotic Act and anticipated rules on corporate accountability and disclosure laws, will be

integrated into the STP process and technology solutions. All this will move the STP process forward while yielding hard benefits along the way.

At the firm level, early **T+1** action was limited to the creation of program management offices. These were high visibility and low-cost initiatives that identified systemic weaknesses in the system. But going forward, **T+1** requires massive reengineering as sequential processes-where each step enriches the transaction's data-are converted to parallel ones. The core of these changes is the creation of several virtual matching utilities (VMUs). The structure of the industry will be changed by these utilities. There will also be "concentrator" organizations, linking smaller firms to the utilities.

These **T+1** identified components will continue to be developed. In addition, the SIA specifically named four areas to be reengineered as part of the continuing pursuit of the cost, efficiency and risk goals. These are improvements to the processing of institutional trades, corporate actions, securities lending and the establishment of book entry settlement as opposed to physical securities.

So many vendors have announced that their products are **T+1** or STP enablers, and these products now need to be incorporated, integrated and used to deliver benefits. The solutions are so varied, that multiple, creative options will arise and need to be worked through.

Will the SEC issue a rule mandating **T+1**? In the opinion of many, the answer is no. But improving the underlying STP processes makes tons of sense. Allowing time to get the components, their data, and their flows right is needed. Immediate market, client and business pressures need to be dealt with. The industry needs to go through an assessment period to determine how to best move forward and achieve the benefits long pursued. Clients need to see that systems are in place that will ensure the fundamental fairness of the market.

The bottom line is that there are areas in the settlement cycle that not only can be immediately improved upon, but will be.

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