



BRASIL
BOLSA
BALCÃO

BRAZILIAN EXCHANGE AND OTC.

SETTLEMENT CYCLE – CASH EQUITIES
TRANSITION TO T+2

BUSINESS MODEL



AGENDA

1. INTRODUCTION

2. SCOPE BY PROCESS

3. TEMPORARY PROCEDURES FOR IMPLEMENTATION

4. BASIS FOR IMPLEMENTATION

5. NEXT STEPS

CHAPTER 1

PROJECT T+2 INTRODUCTION, BENEFITS AND GOVERNANCE



INTRODUCTION



CONTEXT

- A. The 2008 financial crisis led to studies on how to shorten the settlement cycle to T+2 in the world's largest economies.
- B. Studies conducted by consultants in Europe and the US explored opportunities to increase efficiency in the post-trading process, such as trade confirmation and pre-matching, which might reduce the settlement cycle from T+3 to T+2.
- C. In the Brazilian model, the trades are already locked in for settlement and there is no confirmation stage. However, the process of customer identification (allocation), custodian transfer authorization and pre-matching occurs on T+1 and T+2, leading to T+3 settlement.

INTRODUCTION

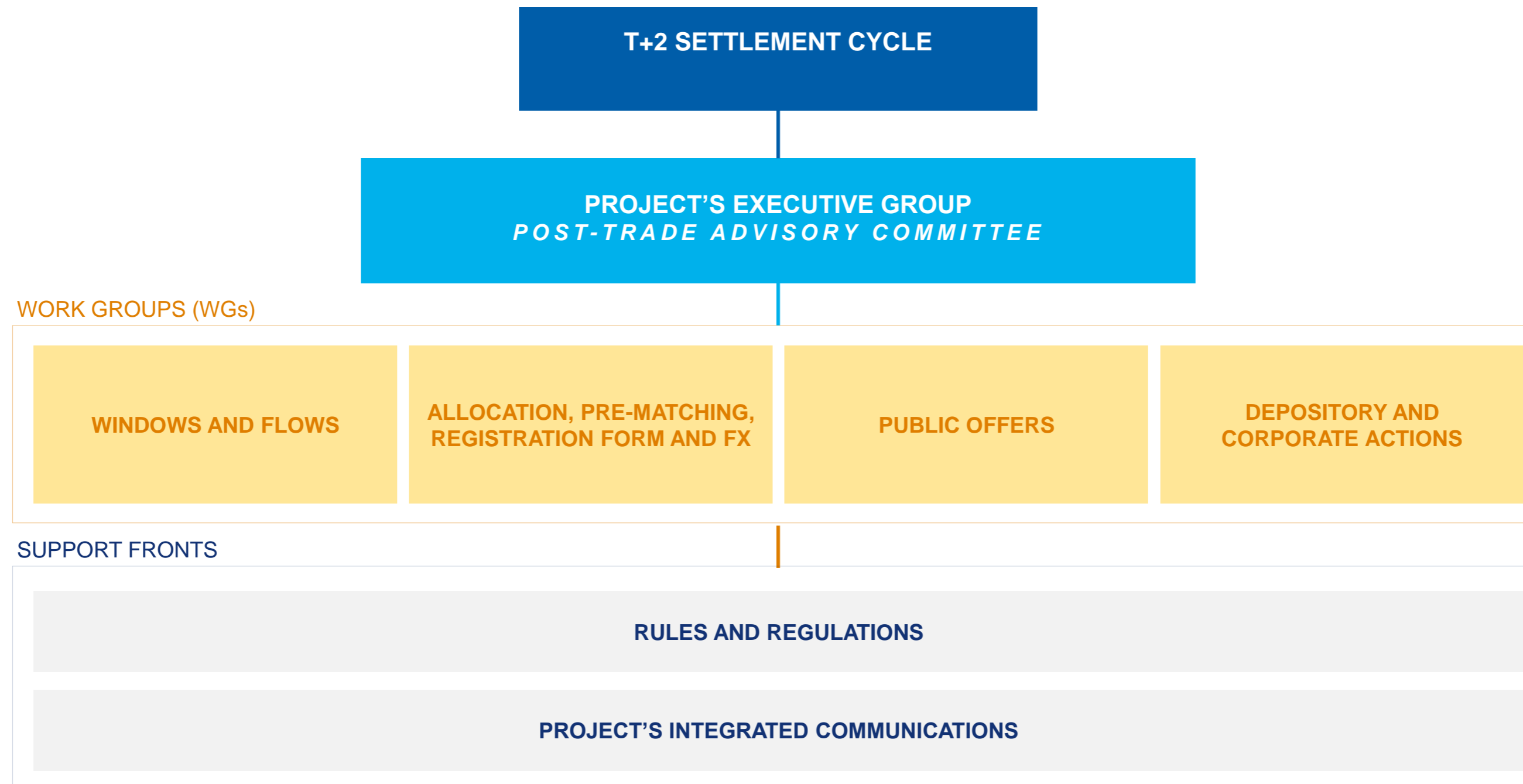


BENEFITS

- A. Reduction of counterparty risk for individual investors, participants and CCP.
- B. Greater efficiency in post-trading processes, thus reducing costs.
- C. Operational risk reduction.
- D. Increased availability of capital.

PROJECT T+2 – PROJECT GOVERNANCE

PROJECT GOVERNANCE – SCOPE PHASE

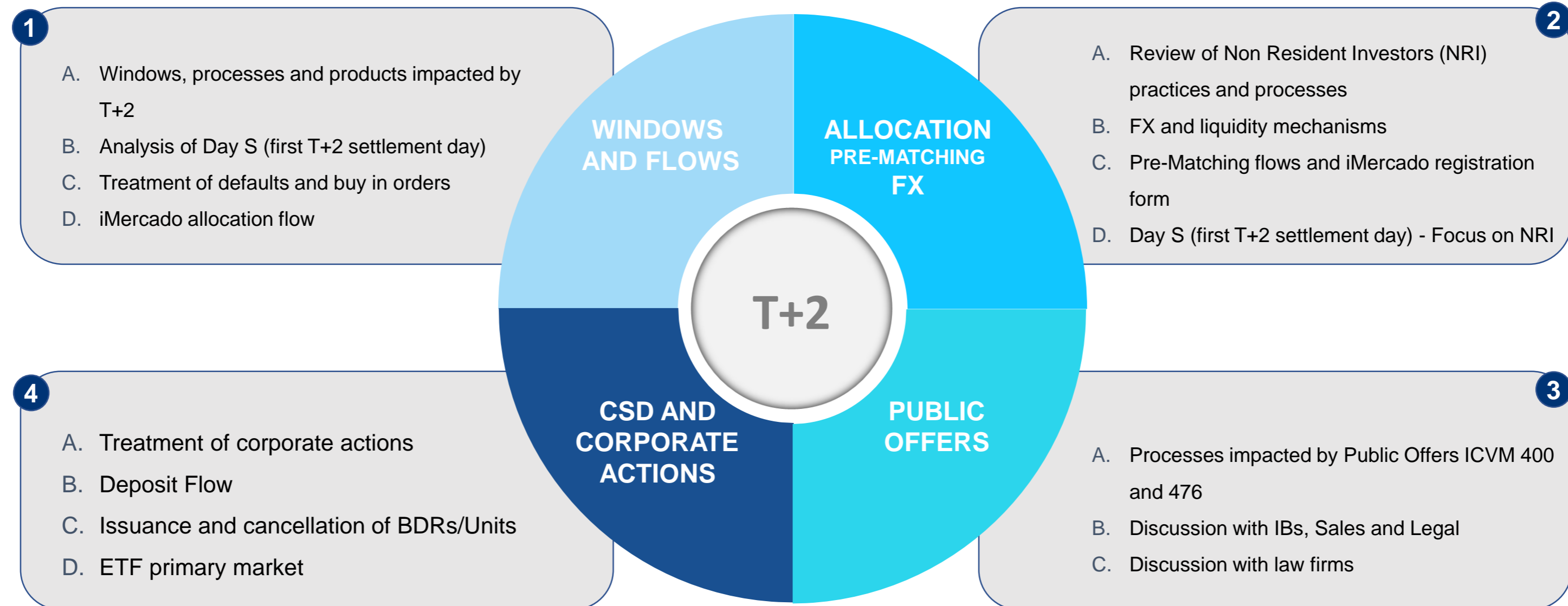


TIMELINE OF SCOPE PHASE

FEBRUARY 2018	MARCH 2018	APRIL 2018
<p>BUSINESS MODEL (BUILDING THE SCOPE)</p> <ul style="list-style-type: none"> • Process analysis • Engagement of various participants as per their activity categories • Discussion of alternatives seeking greater effectiveness and less impact • Design of the business model proposal 	<p>March 21</p> <ul style="list-style-type: none"> • Validation of proposal with Executive Group Post-Trade Advisory Committee 	
<p>BUSINESS MODEL (BUILDING THE SCOPE)</p> <ul style="list-style-type: none"> • Windows and Flows: 5 WGs and 1 meeting with Assets • Allocation, pre-matching, FX: 5 WGs and 1 conference call with foreign customer, intermediary and 3 custodians • Public Offers: 5 WGs, 6 bilateral, 1 law firm • Deposits and Corporate Actions: 5 WGs 		<p>Workshops and dissemination</p> <p>Implementation Plan <i>(B3 and Participants)</i></p> <p>Presentation to Regulators</p> <p>April 30</p> <ul style="list-style-type: none"> • Announcement of implementation schedule

PROJECT T+2 – WORK GROUPS (WGs)

MAIN TOPICS DISCUSSED WITH WGs



CHAPTER 2

SCOPE BY PROCESS



PROJECT T+2 – GENERAL DIAGRAM – T+2

T+2 SETTLEMENT WINDOW

T+1 PROCESSES



BVBG.013
BVBG019
IMBARQ



T+2 PROCESSES



SPB = Brazilian Payment System



CHAPTER 2.1

ALLOCATION, PRE-MATCHING AND CUSTODY AUTHORIZATION



CUSTODY TRANSFER ALLOCATION, PRE-MATCHING AND AUTHORIZATION



1. The deadlines and current schedules for **customer allocation will be maintained: 8:30 p.m. of T+0** for local investors and **3:00 p.m. of T+1** for nonresident investors.
2. It should be noted the importance of **parallelizing** the **Allocation and Pre-Matching** processes by participants in order to correct errors during the allocation period. The use of **iMercado** flows, both for allocation, matching, pre-matching, and registration form and as support for this parallelization and optimization of processes.
3. **Real errors in the current allocation process** were analyzed, being the main causes identified to date:
 - a. **Registration inconsistencies** at the local broker and/or international broker; and
 - b. **Difference in financial matching** based on **average price or commission** calculation

CUSTODY TRANSFER ALLOCATION, PRE-MATCHING AND AUTHORIZATION



4. Following the allocation in T+1, there will be an **intraday processing** between **3 pm and 4 pm** to generate the following files - BVBG019, BVBG013 and IMBARQ.
5. The **custody transfer authorization** shall occur from **3:00 p.m. on T+1 to 8:30 p.m.**
In addition, there will be a window **for treatment of exceptions** from **7:00 a.m. to 9:30 a.m. of T+2.**
6. The following **assessments** were requested from B3:
 - a. Treatment of **allocation by average price**, both in **iMercado** and in the **Clearinghouse**, replacing the current model – trade by trade. The average price for each block trade would be calculated by B3 and used in a standardized way by all participants across all stages of the process.
 - b. **Earlier initiation** of the custody transfer **authorization** process for **customers already matched.**

CHAPTER 2.2

SETTLEMENT



SETTLEMENT



- 1. The settlement process will occur on the second business day after trading (T+2).**
- 2. The main time windows will be:**
 - a. Deadline for portfolio change in the instructions by **10:50 a.m. of T+2**
 - b. Asset delivery window starting at **11 a.m. of T+2**
 - c. Closing of margin call closure at **1:30 p.m.**
 - d. Deadline for payment of debtors at **2:50 p.m.** (unchanged)
 - e. Asset and cash receipt window at **3:50 p.m. T+2** (unchanged)
- 3. Repurchase deadlines have been adjusted:**
 - a. Buy-In orders cancellation: **by T+5**
 - b. Confirmation of Buy-In orders: **by T+6**
 - c. Buy-In order reversal: **in T+7**

SETTLEMENT



4. No further improvements to the flow of **closing exchange rate** in the context of the Project T+2 were suggested.
5. Market participants requested B3 to **assess** two new flows to improve current operational processes:
 - a. Treatment of **allocation errors** in the clearinghouse systems **after** the allocation period (automation of the letter of transfer between different account holders).
 - Full trading participant (PNP)/Settlement participant (PL) requests the exchange of accounts between T+1 and T+2 in the morning, provided that the settlement instruction is not accepted by the Custodian.
 - The exchange of accounts is subject to validation by the Clearinghouse.
 - b. Creation of a **liquidity mechanism by custodians** with the settlement underlying shares as guarantee.
 - The Clearinghouse should consider **custodians** in the **asset restriction** chain, allowing them to restrict delivery to investors who have not performed their payment, while respecting the hierarchy in the restriction of rights:
Clearinghouse > CM => PNP / PL => CST

CHAPTER 2.3

**SECURITIES LENDING
AND FORWARD
CONTRACTS**



SECURITIES LENDING AND FORWARD CONTRACTS



FORWARD CONTRACTS

1. The early settlement of the forward contract requested by the buyer in the current model can be for T+3, T+2 or T+1.
2. After cycle reduction, it will only be possible to request for T+2 or T+1.

SECURITIES LENDING

1. The settlement window for **contracting securities lending** will not **change** with the entry of T+2.
 - a. *We suggest the early start of the securities lending process to 1 hour (from 8 a.m. to 7 a.m.) during the stabilization period.*
2. Lending offers eligible for treatment of defaults (automatic sec lending contracts) must have a maturity greater than or equal to T+7. Currently the rule only allows offers with maturity starting from T+9.

SECURITIES LENDING



CONTRACT CANCELLATION, AMENDMENT AND RENEWAL

PROCESS	CURRENT (T+3)	NEW (T+2)
Contract amendment	From T+1 of contracting to M-2 at 7:00 p.m.	No change
Contract cancellation	In T+0	No change
Contract renewal	May be requested until M-4	May be requested until M-3

T = TRADING DATE
M = MATURITY DATE

SECURITIES LENDING



EARLY SETTLEMENT OF CONTRACTS

PROCESS	CURRENT (T+3)	NEW (T+2)
Early settlement requested by lender	Until 9:30 a.m.: settles in R+3	Until 9:30 a.m.: settles in R+2
	After 9:30 a.m.: settles in R+4	After 9:30 a.m.: settles in R+3
	May be requested until M-4	May be requested until M-3
Early settlement requested by borrower	Settlement in R+1	No change

R = REQUEST DATE
M = MATURITY DATE

Note: The deadlines for cancellation of the request for early settlement will not change

SECURITIES LENDING



TREATMENT OF CORPORATE ACTIONS

PROCESS	CURRENT (D+3)	NEW (D+2)
Date of action application	In T+3 from the last date with rights.	In T+2 from the last date with rights.

TREATMENT OF CORPORATE ACTIONS – PRIORITY PLACEMENT OF SHARES

PROCESS	CURRENT (D+3)	NEW (D+2)
Maturity date of sub-agreement created by priority placement of shares	In T+4 from the placement settlement date	In T+3 from the placement settlement date

SECURITIES LENDING



TREATMENT OF CORPORATE ACTIONS - SUBSCRIPTION

PROCESS	CURRENT (T+3)	NEW (T+2)
Return of lender's rights	In T+9*	In T+8*
Lender with no rights chooses cash settlement or sub-agreement	In T+10*	In T+9*
Cash settlement of the right	In T+11*	In T+10*
Maturity date of sub-agreement after subscription approval	T+4 from date of approval	T+3 from date of approval

*from update of corporate action

CHAPTER 3

TEMPORARY PROCEDURES FOR IMPLEMENTATION



PROCEDURES FOR THE FIRST DAY OF THE NEW SETTLEMENT CYCLE (DAY S)

SETTLEMENT PROCESS ON DAY S:



- A. Settlement of the **two trading sessions** (S-3 and S-2) in a **single window**.
- B. The **allocation and custodian indication authorization** processes for the S-3 and S-2 trading sessions will be kept **segregated**.
- C. The securities settlement **instructions** of the two trading sessions comprise the instructions to settle on Day S in an **non-cleared** manner, but with an **optimization algorithm**.
- D. **Cleared cash** settlement.
- E. S-3 **defaults** will automatically **generate buy-in orders**.
- F. **Open repurchases** with a trading date prior to S-2 (1st trading day in T+2) **remain** with the **current repurchase terms**. **Repurchases** with trading date from S-2 (including), will follow the **new deadlines**.
- G. A reduction or even temporary exemption of the fine delivery failures during the stabilization period has been requested - subject to regulatory approval.

CHAPTER 4

BASIS FOR IMPLEMENTATION



BASIS FOR IMPLEMENTATION



1. VALIDATION

- a. Validation of changes will be done through internal tests of each institution and certification tests with B3.
- b. B3 will establish a certification test environment and will provide a set of data compatible with each participant's production operations.
- c. Day “S” mock tests are planned.
- d. A complete parallel production test will not be carried out. However, we will have production replication days in the certification environment with a focus on a few processes.

2. THE IMPLEMENTATION DATE WILL OBSERVE THE FOLLOWING:

- a. It will occur in different months (April and May), due to the large volume of corporate actions, and, as far as possible, on dates when the volume traded is historically below average.
- b. It will not occur on the week-end prior to the options exercise.
- c. It will seek dates in which Day S is immediately prior to a week-end.

IMPLEMENTATION PLAN

TIMELINE – IMPLEMENTATION PHASES

APRIL 2018

*Implementation Plan
(B3 and Participants)*

IMPLEMENTATION PHASES:

DESIGN

DEVELOPMENT

TESTS

IMPLEMENTATION

PHASES

CHAPTER 5

NEXT STEPS



PROJECT T+2: NEXT STEPS

1. MARKET HEARING: PLEASE SEND FEEDBACKS TO B3.
2. FORMAL ANNOUNCEMENT OF THE **FINAL SCHEDULE BY END OF APRIL 2018.**



BRAZILIAN EXCHANGE AND OTC.