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SEC adopts T+1 settlement effective May 2024

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The final rule shortens the settlement cycle to one business day for most securities transactions, effective May 28, 2024.

The SEC adopted a final rule to shorten the standard settlement cycle for most securities transactions from two business days (T+2) to one business day following the trade date (T+1). Many market participants had favored a September 3, 2024 compliance date (falling on the Tuesday after Labor Day) to provide more time to prepare for the transition to the shortened cycle, but the SEC adopted a May 28, 2024 compliance date (the Tuesday after the Memorial Day weekend), an extension of two months from the proposed rule.

The final rule is intended to benefit investors by reducing the credit, market, and liquidity risks arising from unsettled securities transactions. In connection with the shortened settlement timeline, the final rule also adds procedural requirements on broker-dealers relating to allocations, confirmations and affirmations, as well as record-keeping requirements for registered investment advisers.

Shortened settlement cycle

Rule 15c6-1 currently requires that most broker-dealer transactions settle by T+2, and this requirement has been gradually shortened from T+5 over the last several decades. Transactions involving certain securities—such as government bonds, commercial paper, and some limited partnership interests—are exempt from the rule. For firm commitment offerings that are priced after 4:30 p.m. Eastern Time, the current rules default settlement to a T+4 cycle, although in practice most equity and equity-linked offerings settle on T+3.

- **Default rule for most securities transactions is T+1.** Amended Rule 15c6-1(a) requires most broker-dealer transactions to settle by T+1, subject to exceptions provided under Rule 15c6-1(b). These exceptions now include security-based swaps, and unlike other aspects of the rule, the exception for security-based swaps is effective upon the effective date of the final rule, much earlier than the May 2024 compliance date.
- **Firm commitment underwriting priced after 4:30 p.m. EST – settlement changed from T+4 to T+2.** The rule proposal would have eliminated the expressly longer settlement time under Rule 15c6-1(c) for firm commitment offerings priced after 4:30 p.m. Eastern Time, subject to the continuing availability of the override provision discussed below. As a result, by default, firm commitment offerings priced after market close would have been required to close the next day—shortening the normal settlement cycle for equity and equity-linked offerings (which typically price after market close) from three days to one day. The final rule retains Rule 15c6-1(c), but shortens the default settlement cycle to T+2 for these transactions.
- **Override provision.** The final rule retains the so-called "override provision," which provides some flexibility by permitting parties to a trade to agree that the settlement date may be later than T+1, provided that the agreement is express and reached at the time of the transaction. The provision provides welcome and continued flexibility for

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many debt offerings and other offerings involving complex documentation that would cause T+1 settlement to be impractical.

We expect securities transactions that settle on a longer than T+1 cycle to continue to include disclosure alerting investors to that fact in offering documents as is currently the practice. All parties involved in the closing process for securities offerings that settle on a T+1 standard settlement cycle (or T+2 for firm commitment offerings that are priced after-market) will also face a shorter time period to prepare for closing.

The SEC indicated it would continue to consider the feasibility of a move to T+0 settlement (i.e., settlement by end of trade day) in the future and seek to address the associated challenges with market participants.

Same-day allocations and affirmations

Investment managers that effect block trades for the accounts of several customers simultaneously need to provide post-trade underlying account allocation instructions to the broker or custodian before these transactions can settle. Similarly, certain transactions, primarily involving institutional trades, require post-trade exchange of confirmations and affirmations, in order for the parties to compare trade details and facilitate settlement with third-party custodians. These processes are often, but not always, completed on the trade date.

In order to facilitate T+1 settlement, the final rule requires a broker-dealer to either (i) enter into written agreements, or (ii) establish, maintain, and enforce written policies and procedures reasonably designed, in either case to ensure completion of allocations, confirmations, and affirmations as soon as practicable and no later than the end of trade date.

The final rule also amends Rule 204-2 under the Investment Advisers Act of 1940 to require investment advisers to make and keep records of confirmations and time- and date-stamped allocations and affirmations, with respect to transactions that are subject to the requirements of Rule 15c6-2(a).

Impact on other rules

Reducing the standard settlement cycle to T+1 will have follow-on effects on various other rules or market practices that are themselves tied to the standard settlement cycle, closing or the settlement date, typically reducing those time frames by one day. These include:

- Requirements for closing out fail to deliver transactions within a certain number of days following the settlement date under Regulation SHO and Rule 15c3-3(m);
- Delivery of Rule 10b-10 confirmations, which must occur at or before completion of a transaction;
- A more compressed timeframe for prospectus delivery obligations;
- The time period within which a broker-dealer must obtain cash payment or margin from a customer for a securities transaction under Regulation T; and
- Various self-regulatory organization and other rules that reference the time period under Rule 15c6-1 or “regular way” settlement.

While the SEC considered certain of these follow-on effects, it determined not to adopt any related rule changes, reasoning in part that the period running to the compliance date provides sufficient time for market participants to adapt to the shortened settlement cycle.

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