

Reminder: Securities Transaction Settlement Cycle Shortened to T+1

May 28, 2024

Key change:

Starting May 28, 2024, most stock and security trades in the U.S. will settle in one business day (T+1) instead of two (T+2).

Historical Background:

In the 1920s, the settlement cycle for securities transactions was T+1. Then over the next decades, the length of the settlement cycle increased to T+5 until the SEC adopted Rule 15c6-1 in 1993 to shorten the settlement cycle to T+3. In 2017, the settlement cycle was shortened to T+2, and now we are reverting back to a T+1 settlement cycle. Government bonds settlement is already set at T+1.

What it means:

- Faster transaction completion, reducing risk for both buyers and sellers.
- Investors may need funds available sooner to cover trades.
- Financial institutions need to be prepared for the faster settlement pace.

Why the change?

- Aim is to reduce risk and improve efficiency in the financial system.
- Should improve use of technology and automation.

Risks to Retail Investors:

- Transactions that are being settled on a T+1 basis may settle before investors have cleared a transfer of cash into their accounts. This will also impact Regulation T. Regulation T is a collection of provisions that govern the amount of credit that brokerage firms and dealers may extend to customers for the purchase of securities. According to Regulation T, an investor may borrow up to 50% of the purchase price of securities that can be bought using a loan from a broker or dealer. The remaining 50% of the price must be funded with cash, which needs to be readily available with the new T+1 cycle.
- For tax purposes, investors will have less time to correct any cost-basis decisions made in a trade.

Impact on Foreign Markets:

- The U.S. change is sparking discussions in Europe and elsewhere about adopting T+1.
 - Canada has also adopted T+1. The first day of T+1 settlements in the Canadian securities markets is May 27, 2024 (a holiday in the U.S.)
 - The Tel Aviv Stock Exchange already has a T+1 settlement cycle (for market participants and Israeli investors).
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- European markets may face challenges adapting to a faster settlement cycle.
- Regulators in Europe are considering potential effects on liquidity, failed trades, and operational costs.

Overall, the US shift to T+1 is a significant development for the financial industry. It remains to be seen if Europe will follow suit.

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