MEMO# 35665

April 2, 2024

SEC Divisions Issue FAQ and Risk Alert Regarding T+1 Standard Settlement Cycle

[35665]

April 02, 2024

TO: ICI Members
Equity Markets Advisory Committee
Global Operations Advisory Committee
Operations Committee
Securities Operations Advisory Committee
Small Funds Committee SUBJECTS: Operations
Settlement
Trading and Markets RE: SEC Divisions Issue FAQ and Risk Alert Regarding T+1 Standard Settlement Cycle

On March 27, three SEC divisions issued notices relating to the upcoming May 28, 2024 implementation of the T+1 standard settlement cycle under Rule 15c6-1. First, the Divisions of Trading and Markets and Investment Management issued a FAQ that responds to questions about the standard settlement cycle and investment adviser recordkeeping requirements.[1] Further, the Division of Examinations published a Risk Alert that provides additional information about its assessment of registered entities' preparedness for the shortened settlement cycle.[2] This memo describes the FAQ and the Risk Alert, respectively, further below.

Divisions of Trading and Markets and Investment Management FAQ

The FAQ responds to seven questions regarding the transition to a T+1 standard settlement cycle. Notable responses address the following:

- 1995 Limited Exemption: The FAQ highlights the SEC's 1995 limited exemption from Rule 15c6-1 for certain securities transactions for which the facilities for transfer or delivery of the securities exist primarily outside of the United States.[3]
- Exemption from Same-Day Affirmation: The FAQ notes that transactions that are exempt from Rule 15c6-1, e.g., transactions subject to the SEC's 1995 limited exemption order, are also exempt from the requirements for same-day affirmation under Rule 15c6-2.[4]

- Extension Beyond Standard Settlement: The FAQ notes that, as has already been the case prior to T+1 transition, the parties to a transaction may extend settlement for a given transaction by expressly agreeing at the time of the transaction to the terms of settlement.[5] However, as the Commission had stated in the past, this "override" is intended for use only in "unusual" or "limited" circumstances.[6] Further, the FAQ states that the same-day affirmation requirements would continue to apply to these transactions.
- Same-Day Affirmation: In response to a question as to whether a market participant has satisfied same-day affirmation requirements if they achieve a rate of 90%, the FAQ notes that Rule 15c6-2 does not establish a "threshold" or "safe harbor" linked to the percentage of transactions that achieve same-day affirmation.
- Adviser Recordkeeping Requirements: The FAQ clarifies that a registered investment adviser must make and keep records of each confirmation it receives, any allocation, and affirmation that it sends or receives, no matter the source or form of the allocation, confirmation or affirmation. Further, the recordkeeping requirements apply regardless of when each confirmation is received or when any allocation or affirmation is sent or received.[7]

Division of Examinations Risk Alert

The Division of Examinations' Risk Alert describes the scope and content of examinations and outreach related to the transition to T+1 standard settlement. In addition to reviewing and assessing the preparedness to comply with shortened settlement, the Division will examine whether changes have been made to comply with other related requirements, including same-day affirmation[8] and new recordkeeping and reporting requirements. Accordingly, the Division may review preparations relating to activities in clearance and settlement,[9] operational readiness,[10] and disclosures, representations, and/or communications to customers, clients, and/or vendors.[11] The Risk Alert includes an appendix specifying the types of information and documents that it may review.[12]

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Notes

[1] SEC Divisions of Trading and Markets and Investment Management, Frequently Asked Questions Regarding the Transition to a T+1 Standard Settlement Cycle (modified Mar. 27, 2024) ("T+1 FAQ"), https://www.sec.gov/exams/educationhelpguidesfaqs/t1-faq. The FAQ represents the views of division staff and, like all staff guidance, have no legal force or effect.

[2] SEC Division of Examinations, Risk Alert: Shortening the Securities Transaction Settlement Cycle (Mar. 27, 2024) ("T+1 Risk Alert"), available at https://www.sec.gov/files/risk-alert-tplus1-032724.pdf. The Risk Alert represents the views of division staff, and like all staff statements, have no legal force or effect.

[3] See FAQ #2. The SEC's 1995 order exempts (1) transactions in securities for which there is no transfer agent in the United States and which is not eligible for deposit at a registered

clearing agency (together, "transfer or delivery facilities"); (2) transactions in securities for which there are transfer or delivery facilities in the United States and outside the United States if annual trading in such securities in the United States constitutes less than 10% of the aggregate worldwide trading volume; and (3) transactions in securities executed by a US broker-dealer outside of the United States, the terms of which provide for delivery or payment outside of the United States. The order, however, also specifies that an exemption does not apply to (1) transactions intended to be executed by a US broker-dealer on a registered securities exchange or through the facilities of a registered securities association subject to the rules of a national securities exchange or registered securities association and settled through the facilities of a registered clearing agency; or (2) transactions executed by a US broker-dealer on a foreign exchange to satisfy its obligations to a US customer.

[4] See FAQ #3 for a description of the types of transactions exempt from Rule 15c6-1, and therefore, also from Rule 15c6-2.

[5] SEC Rule 15c6-1(a), (d).

[6] See FAQ #4 (citing 2017 T+2 settlement cycle adopting release).

[7] See FAQ #7.

[8] The Division points out recent public data suggesting that custodians and investment managers that manually affirm their transactions are providing affirmations at a significantly lower rate on trade date than prime brokers or investment managers that use central matching tools. Risk Alert at 3.

[9] This includes clearing services provided to institutional clients, retail customers, or other broker-dealers; custodial or prime brokerage services; securities lending recall activities and payment activities that support clearance and settlement; trade allocation and fail management processes; and custodian communication.

[10] This includes implementation of, or enhancements or modifications to, systems, controls, policies or processes associated with the shortened settlement cycle, along with information related to any testing events, such as testing events with DTCC, broker-dealers, vendors, or other parties.

[11] See T+1 Risk Alert at 3-4.

[12] See id., Appendix A.
