How Does the T+2 Settlement Cycle Affect Dividend Investors?

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On September 5, 2017, the Securities and Exchange Commission (SEC), the Depository Trust & Clearing Corporation (DTCC) and the major stock exchanges in the securities industry shortened the settlement cycle for transactions.

Prior to this date, U.S. equities, corporate bonds, municipal bonds, unit investment trusts and other related instruments had a settlement date of the trade date plus three business days, or T+3. For example, if an investor were to sell a stock on a Friday, the funds would not actually be settled until Wednesday of the following week. For a variety of reasons, the DTCC has shortened this settlement from the three business days to two business days (T+2).

Let us see the implications of this change.

Check out all the corporate announcements regarding dividend payouts in our Dividend Payout Changes and Announcements tool here.

Why the SEC Is Changing from T+3 to T+2

The SEC proposed a new amendment to the settlement cycle rule (Rule 15c6-1(a)) to shorten the settlement cycle for most broker-dealers to be compliant on September 5, 2017. The reasoning behind this is that it will reduce the liquidity risk for broker-dealers, free up more financial resources and reduce margin and other fees that retail and institutional clients pay. The DTCC, which settles the actual trades in the U.S., estimates the shorter settlement cycle will reduce its average daily capital requirements by 25%, or $1.36 billion. In the new amendment, the SEC stated that the shortening is also supported by changes in technology, operations and infrastructure since the original rule was written.

How the Change Affects Investors

The United States is one of the last areas of the world when it comes to changing to T+2 settlement, as Europe, Australia, New Zealand and Hong Kong have already shifted. Now with the new change, investors can buy and sell at a faster pace than before. For example, when an investor buys a stock, the money is due in the account within two business days. Same goes for when an investor sells a stock – then the broker-dealer needs to deliver the funds within two business days. However, a potential issue is when an investor does not deliver the money in a timely matter. If a client buys a stock and then sells the same stock before any funds were received, it will cause a Regulation T freeze. When this happens, an investor is restricted from

trading without cash in hand for 90 days. This protects the broker-dealer from investors that are looking to day trade without ever having to deposit funds.

Another major difference is how this new change affects dividends. According to NYSE Rule 235 and Nasdaq Rule 11140(b)(1), the ex-dividend date cycle has been shortened from two days to one day before the record date. Issuers with a record date on or after Thursday, September 7, 2017, will abide by the new one-day ex-dividend cycle. This is important for dividend investors because it shortens the timing of when a stock needs to be purchased for the holder to be eligible for the upcoming dividend. For example, **Wal-Mart Stores** (WMT) has its next ex-dividend date on December 7, 2017. Prior to this change, the record date was supposed to be two business days after, or December 11, 2017. However, since the cycle has shortened to only one day, the new record date is December 8, 2017. So an investor for the dividend would only be eligible if they purchased WMT prior to December 7. This would also be applicable to investors that sold their WMT shares prior to the ex-dividend date, as they sold their right to the upcoming dividend away.