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SEC shortens settlement date for broker assisted sales of stock to T+1. Are you ready?

Seven key steps to ensure that your organization is prepared

There are new rules being introduced that will dramatically impact U.S. publicly traded companies that grant broker assisted sales of stock to executives and other employees. Starting May 28, 2024, U.S markets are going to require a "T+1 settlement" date for broker assisted sales of stock. According to the U.S Securities and Exchanges Commission (SEC), this change primarily is designed to protect shareholders and investors by reducing market risk and exposure, particularly during market volatility and increase operational and capital efficiency.[1]

Bottom line: If your organization makes stock option grants, these new rules could result in significant changes to the way in which you handle tax withholding and deposit requitements for taxes due on stock options and certain other equity awards. What's more, it will require tighter coordination between stakeholders in your organization as well as third-party vendors your company is collaborating with for the administration and reporting of compensation, benefits, tax, and other regulatory requirements.

Settlement period gradually compressed

From the mid-1990's through 2017, companies essentially had **three days** to settle the exercise of broker assisted sales of stock. In other words, the company had three days—T+3—from the day an employee exercised the stock option to settle the transaction. Prior to that, companies had five days to settle the transaction (i.e., T+5). The three-day settlement period requirement remained for 22 years—until 2017—when the settlement period was shortened to two days (i.e., T+ 2).

Now the SEC will further reduce the settlement period for stock options to one day – T+1. The SEC pointed out that a shorter settlement period helps reduce the risk of default, and also minimizes the impact of any errors because they can be detected and alleviated quickly before there are any significant changes in shortened turn stock prices. The SEC added that its ultimate goal would be to have a same day (T+0) or even instantaneous settlement date; this is something organizations will only be able to manage if they implement an automated process in the future.

Let's take a closer look at the new rules, how they might impact you, and what you need to do to comply.

[1] See Federal Register: Shortening the Securities Transaction Settlement Cycle

New rules make multi-party coordination a must

The steps that come into play when broker assisted sales of stock are granted and then exercised typically involve multiple stakeholders, both internal and external, including the:

- **Share plan administrator (SPA)**
- **Tax provider**
- **HR/Mobility**
- **Equity administrator**
- **Payroll**
- **Edgar or corporate issuer preparer**
- **Legal (in and/or outside counsel)**
- **Treasury/ transfer agent**
- **Finance**

It's going to take tighter and more efficient coordination among these parties—as well as upgraded technology and processes—to ensure that your organization achieves T+1 settlement.

It's critical that the eight parties noted above (or possibly more) need to work together in order to meet the new T+1 settlement requirements, which cover timely processing, settlement, SEC filings and payroll deposits.

Exercise (T) → Settlement (T + 1) → Next day (T + 2)

Some exceptions to T+1: The SEC's new rules don't prevent the parties to vary (e.g., extend) the settlement dates by express agreement at the time of the transaction. In addition, the new rules don't apply to exempted securities, government securities, municipal securities, commercial paper, banker's acceptances or commercial bills, or to security-based swaps. See KPMG Regulatory Alert: "SEC Final Rule for T+1 Settlement Cycle," February 2023.

Seven steps to prepare for T+1

Considering that the May 2024 deadline will be here before we know it, there are a number of steps you should consider taking now, including:

1. **Form a working group:** Bring together all of your key stakeholders involved in the process—internal and external alike—so they understand the new T+1 requirement and what's needed. Also, conduct several working sessions to make sure ALL departments and third parties are aligned to meet the shorter, T+1 turnaround well before the May 2024 deadline.

2. **Review roles and responsibilities:** Review and understand the big picture, the role of each party (internal and external), and the timing for each task. Try to find ways to consolidate tasks and ensure tighter coordination. Evaluate the process from end-to-end, from option grant to exercise to payroll reporting to withholding to see where it can be improved. You may find that you need to hire additional back-office resources, upgrade your software and systems, and/or contract with technology service providers in order to comply with the new rules.

3. **Get HR data in shape:** Start getting your "HR data house" in order; with this shortened turnaround time, your HR data needs to be pristine. Work with your HR business partners, coordinate your HR policies regarding work locations/living locations and be ready for this quick one-day turnaround; once the T+1 rule takes effect, there's not going to be time to check where someone has worked over the life of a 10-year option to make sure you're in compliance.

4. **Revisit contract terms and service level agreements with third parties:** Its worth taking a look at these agreements and making sure third parties are willing and able to meet the turnaround time. Evaluate if certain steps or processes can be consolidated or handled by upgraded technology or AI.

5. **Communicate with employee and departments:** As with any change, it's good practice to communicate—and even overcommunicate. Make sure that employees who were granted stock options are aware of the change and that each of the departments involved in the process are ready to go on day one of the T+1 change.

6. **Test out systems in advance:** A lot of preparation will need to occur over the next few months to ensure that all parties, internal as well as external third parties (e.g., investment funds, their fund administrators, and prime brokers) are ready for the adoption. To ensure success, the new systems should be rigorously tested, and the transition should happen gradually.

7. **Make sure you're in tax compliance:** Don't forget that the U.S. next day deposit rule may not synch with other countries' requirements for reporting and withholding if you **have employees exercising options outside the U.S**. This part of the puzzle will not go away, so careful coordination with your payroll and other department will be needed for as long as the tax settlement rules remain different.

T+1 deadline on the horizon. Be ready

May 2024 is not that far off, and it's certainly not too early to start preparing for the SEC's new T+1 requirements. Corporations have experienced the shortening of broker assisted sales of stock settlement periods several times over the past two decades. While these shorter turnaround deadlines are usually doable, they do require tight coordination among multiple stakeholders to meet the settlement and tax compliance time frames.

Don't forget Payroll: Earlier this year, KPMG Washington National and Global Reward Services provided updated commentary on the U.S. payroll deposit rules for equity awards. See KPMG Tax Alert: "Timing of Employment Taxes for RSUs under current SEC Settlement Timelines," February 2023.

There's one other thing to keep in mind: if the SEC's ultimate goal is to go to a same day (T+0) or even instantaneous settlement date, the steps you take today for T+1 could be leveraged for a future compression of this timeline.

Don't forget other markets: Canada is also going to T+1 and others appear to be soon to follow.

How KPMG can help you

The KPMG Global Reward Services team can help design and implement total rewards programs and processes to align your talent agenda and business needs, and continuously support you through the evolution of your programs in response to changing business requirements and regulatory activities.

Our team has extensive functional and industry experience that can address your global talent and reward needs from strategy through execution. From compensation and benefits to performance management and career training, we use technology and data analytics to help companies make better decisions and attract, develop and retain talent.

Finally, you can benefit from our global strength and capabilities established through our global network of member firms located in all of the world's commercial hubs. This capability enables us to serve you, wherever you do business—now or in the future.

Connect with us

For more information on the SEC's new T+1 settlement rules for stock-based compensation, how this development may impact you and your company, and how to comply with the new rules, please click here or contact one of our professionals listed below:

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