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Ms. Vanessa Countryman
Secretary
U.S. Securities and Exchange Commission
100 F Street NE
Washington, DC 20549-1090

Submitted via email to rule-comments@sec.gov

April 11, 2022

Dear Ms. Countryman,

Shortening the Securities Transaction Settlement Cycle [File No. S7-05-22]

The Alternative Investment Management Association Limited (AIMA)[1] appreciates the opportunity to respond to the U.S. Securities and Exchange Commission's (Commission or SEC) proposal to adopt rules and rule amendments to shorten the standard settlement cycle for most broker-dealer transactions from two business days after the trade date ("T+2") to one business day after the trade date ("T+1") (the "Proposing Release").[2]

AIMA met with SEC staff in July 2021 at its request to discuss industry requirements for shortening the settlement cycle in the United States, as well as the potential impact on market participants. Following discussions with members, AIMA submitted a letter to the SEC to outline our considerations and concerns for a move to T+1.

AIMA also joined the T+1 industry working group and steering committees formed by the Investment Company Institute (ICI), Securities Industry and Financial Markets Association (SIFMA) and the

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[1] AIMA, the Alternative Investment Management Association, is the global representative of the alternative investment industry, with more than 2,100 corporate members in over 60 countries. AIMA's fund manager members collectively manage more than $2 trillion in assets. AIMA draws upon the expertise and diversity of its membership to provide leadership in industry initiatives such as advocacy, policy and regulatory engagement, educational programs and sound practice guides. AIMA works to raise media and public awareness of the value of the industry. It is committed to developing skills and education standards and is a co-founder of the Chartered Alternative Investment Analyst designation (CAIA) – the first and only specialized educational standard for alternative investment specialists. AIMA is governed by its Council (Board of Directors). For further information, please visit AIMA's website, www.aima.org.

[2] SEC, Proposing Release, Shortening the Securities Transaction Settlement Cycle, 87 FR 10436 (Feb. 24, 2022) (the "Proposing Release").

Depository Trust & Clearing Corporation (DTCC) providing input to the *T+1 Report* cited in the Proposing Release.[3] Although AIMA remains an active member of this valuable consortium, this letter should be considered in its own right from what may be submitted by the larger group.

With respect to the Proposing Release, we commend the Commission's intended efforts to reduce risk in the U.S. settlement cycle and improve efficiency in post-trade processing. Many of our U.S.-based asset manager members already have capabilities to process trades in a manner close to, or consistent with, the Proposing Release's T+1 expectations. These members await the successful implementation of required changes by their counterparties and vendors to ensure that T+1 settlement can come to fruition on a timely basis.

Our concern is most acutely focused on a number of international issues raised by a U.S. move to T+1, which were summarized in our previous letter to the Commission on October 27, 2021. The Proposing Release raises considerable risks for asset managers with primary or significant exposure to markets that will remain at T+2. In absence of further global coordination, the resulting market misalignment from the move to T+1 poses a number of harmful unintended consequences to these asset managers, their counterparties and overall market health and stability.

The Proposing Release also raises concerns for trades undertaken at or near the U.S. market close, particularly for members in time zones several hours ahead of the United States. The requirement to "complete allocations, confirmations, and affirmations as soon as technologically practicable and no later than by the end of the trade date"[4] may be difficult for those in the same/similar time zone for trades occurring at or near the close, but it may not be feasible for those located in regions that are several hours (or more) ahead, where new cut-off times would occur late into their overnight. Currently, those members rely on the ability to complete any final operational obligations in their morning, an option that would no longer be available to them.

Finally, the cost analysis presented in the Proposing Release significantly underestimates the system and process changes that will be required by even the most sophisticated fund managers, as well as potential need for all fund managers to redraft and renegotiate myriad agreements with investors, counterparties and vendors that are affected by settlement timing. Additional requirements for registered investment advisers to timestamp certain trading records adds further complexity and cost to those managers' efforts. We respectfully question how the Commission determined the cost impact of the Proposing Release on asset managers and would welcome further information in this regard.

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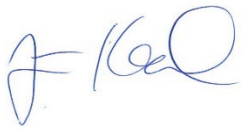
[3] Proposing Release, at 10438, fn. 18.

[4] Proposing Release, at 10446.

Our members' concerns are outlined in greater detail in the accompanying Annex. We would be happy to elaborate further on any of the points raised in this letter. For further information please contact Suzan Rose at srose@aima.org.

Yours sincerely,



Jiří Król
Deputy CEO, Global Head of Government Affairs
AIMA

Cc: The Honorable Gary Gensler, Chair
The Honorable Hester M. Peirce, Commissioner
The Honorable Allison Herren Lee, Commissioner
The Honorable Caroline A. Crenshaw, Commissioner
Mr. Haoxiang Zhu, Director, Division of Trading and Markets

AIMA

ANNEX

Counterparty Dependencies in Settlement, Making Changes to Ensure T+1 Readiness

Asset managers are capable of making the necessary changes to their policies, procedures, operations and legal obligations to comply with an accelerated settlement cycle. However, it should be noted that they are almost entirely dependent on their broker-dealer trading counterparties, stock loan providers, prime brokers, custodians and administrators to ensure they can meet the functional requirements of settlement on the proposed timetable. The Proposing Release does not acknowledge the heightened vulnerability of all asset managers in their dependency on their many industry counterparties and vendors to ensure that accelerated settlement can successfully come to fruition.

Much of the work asset managers will need to undertake in moving to T+1 cannot occur until related counterparty changes are well underway. Adjustments will need to be made to systems that control trading, portfolio management, operations, treasury, risk management and accounting. Policies and procedures governing those areas will require corresponding adjustments. Given that the Proposing Release advises that all such changes also be made with a view toward a further acceleration to T+0 settlement, it is critical that asset managers await at least partial completion of counterparty changes before making revisions to their own.

Myriad counterparty agreements also will require amendments, as will many fund constitutional documents. Certain of these changes can be made sufficiently ahead of a completed T+1 infrastructure, though it is unlikely they can be finalized without their counterparties' revised service level agreements. Similarly, operational and contractual changes may need to occur where settlement-related tasks are shared with, or delegated on a limited basis by, other entities that are required to make changes.

Asset managers can and will analyze their internal functions in advance of counterparty changes, but their own work to comply with T+1 trade settlement will rely on clear and coordinated planning with all counterparties, well in advance of a go-live date.

Critical Issues Arising from Misalignment with International Markets

The move to T+1 trade settlement in the U.S. will result in a misalignment with international markets that will remain on a T+2 settlement cycle. The proposal makes mention of "Potential Mismatches of Settlement Cycles"[5] when discussing a potential future move to T+0 but contains no meaningful discussion of these concerns for the move to T+1.

The Proposing Release raises considerable issues for asset managers with primary or significant exposure to markets that will remain at T+2. In the absence of significant global coordination, the

[5] Proposing Release, at 10473.

resulting market misalignment from the move to T+1 poses a number of harmful unintended consequences to these fund managers, their counterparties and overall market health and stability. To date, we are unaware of any substantial efforts to coordinate the U.S. move to T+1 settlement with non-U.S. markets.

Specific misalignment concerns include:

- ***F/X Settlement Risk*** – Accelerating U.S. settlement to T+1 raises the risk that transaction funding dependent on F/X settlement may not occur in time. Settlement of spot Forex transactions generally occurs at two days post execution, although the period of irrevocability - between the unilateral cancellation deadline for the sold currency and actual receipt of the bought currency - can extend well beyond T+1. This known timing mismatch is not anticipated to qualify related trades for the "override" provision in Rule 15c6-1(a) under the U.S. Securities Exchange Act of 1934, as amended ("Exchange Act"), discussed in the Proposing Release.

  Alternative sources of funds to settle U.S. trades on T+1 may therefore need to be in place, whether liquidating other more readily available assets, pre-funding trades in USD or borrowing USD to meet an accelerated U.S. settlement deadline. All of these alternatives increase the cost to fund transactions, create allocation inefficiencies and are likely to dissuade participation in U.S. markets.

  Unilateral cancelation deadlines by currency need to be considered. Service agreements between corresponding banks will need to agree and identify the cancellation cut-off time to manage risks effectively, within a window that affords T+1 settlement. We expect this will occur within the U.S. in order to comply with T+1 settlement, but we do not have any indication that this will occur in other regions, beyond shortening or curtailing activity in order to meet U.S. settlement obligations.

- ***International Banking and Market Coordination Issues*** – Many core international markets will remain at T+2 with no announced plans to accelerate settlement further. The rigid deadlines of banking systems pose a significant risk, as do simple time zone or calendar differences that otherwise can be accommodated by a T+2 settlement cycle.

  Foreign banking deadlines and cutoff times for transaction processing in related markets must be carefully re-examined to ensure activity can be harmonized in an accelerated U.S. settlement framework.

- ***Collateral/Liquidity Risk*** – The above F/X and coordination issues threaten asset managers' ability to ensure funding is available in time to settle their U.S. trades at T+1. Uncertainty about collateral for settlement may mean foreign asset managers could need to redeem money market funds to meet their financing needs – or forego transacting in U.S. markets in order to comply with the accelerated settlement requirements. Similarly, U.S. fund managers may be forced to reduce or curtail their foreign market participation due to the inability to align foreign trade settlement with

their U.S. market funding needs. Ultimately, trade financing issues will lead to both significantly lower trading volume and lower overall liquidity, which poses a very real risk to overall market health and stability.

In the Proposing Release, the Commission acknowledges "mismatched settlement timeframes"[6] as a result of the move to T+1 and recognizes that a "disorderly transition to a shorter settlement cycle could lead to an increase in settlement fails."[7] It downplays these misalignment concerns by pointing out that the prior move from T+3 to T+2 did not result in a marked change to fail volumes.[8] However, this rationale fails to consider that, in its prior move to T+2, the U.S. was aligning itself with the majority of foreign markets, and therefore would not have seen the mismatch issues it now will as a result of the proposed unilateral move to T+1. When the U.S. was at T+3 settlement, and foreign markets settled more quickly, the risk was to participation in those foreign markets – these same collateral and liquidity issues we are citing, in reverse. As well, F/X settlement generally was not of concern when the U.S. was at T+3; it was in line with T+2 markets and in advance of U.S. settlement obligations. One cannot assume the two single-day settlement accelerations will mirror each other in market impact; the move from T+3 to T+2 was wholly different in this regard.

We strongly disagree with the Commission's preliminary belief that the anticipated benefits of a shortened settlement cycle "will justify the anticipated costs"[9] of market misalignment, nor do we believe this will be adequately addressed by broker-dealers as a competitive advantage. Rather, we believe the costs will be significant enough to drive volume down and away from U.S. markets, a serious unintended consequence that has not been accurately assessed in the Proposing Release.

Other Trade Settlement Timing Issues

As noted in our letter, the Proposing Release raises concerns for trades undertaken at or near to U.S. market close, particularly for members in forward time zones. Although the Proposing Release's intention is T+1 settlement, the actuality is closer to same-day settlement when factoring in the time available to meet all related obligations.

End of day trading, which can be sizeable around such events as a portfolio rebalance, will be subject to the same-day allocation, confirmation and affirmation requirements of the Proposing Release, despite a very short processing window. For asset managers located in regions that are several hours (or more) ahead, where new cut-off times would occur late into their overnight, same-day requirements may make end-of-day trading operationally impossible. Those members in particular

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6 Proposing Release, at 10448, fn. 119.
7 Proposing Release, at 10448.
8 *Ibid.*
9 *Ibid.*

rely on the ability to complete any operational obligations in their subsequent morning, an option that no longer would be available to them.

Shifting end-of-day trading to market open to avoid this truncated processing window would amplify existing open volatility and distort the day's valuable price and volume indicators, traditionally used by market participants to plan and prepare themselves for the rest of the trading day.