

MEMO# 2679

April 9, 1991

GROUP OF THIRTY RECOMMENDATIONS

April 9, 1991 TO: INTERNATIONAL COMMITTEE NO. 4-91 RE: GROUP OF THIRTY RECOMMENDATIONS _____ The Group of Thirty ("G30") is an independent, non-partisan, non-profit organization comprised of international financial leaders. The organization was established in 1978 to "deepen understanding of international economic and financial issues, to explore the international repercussions of decisions taken in public and private sectors, and to examine the choices available to policy makers." In 1988 the G30 initiated a project to improve the state of risk, efficiency and cost in the world's clearance and settlement systems. The Group published the following nine recommendations and began the process of setting up committees in each country to oversee their adoption. The recommendations are: 1. All trade comparisons should be accomplished by T+1 no later than 1990. 2. Indirect market participants (institutions, eg. pension plans, mutual funds) should be members of a confirmation/comparison system by 1992. 3. A central securities depository should be achieved in each country by 1992. 4. A review of a trade netting system to determine its appropriateness should be undertaken; and if appropriate, netting should be implemented by 1992. 5. A delivery-versus-payment (DVP) practice should be in place by 1992. 6. A same-day funds (SDF) settlement convention should be adopted. 7. A rolling settlement system should be adopted with final settlement on T+3 by 1992. -2- 8. Securities lending and borrowing should be encouraged. 9. Each country should adopt an international standard for securities numbering and messages by 1992. The United States presently meets six of the nine recommendations, not meeting the recommended procedures of T+3 settlement, same-day funds, and international securities ID numbers. The attached chart sets forth the status of each country's settlement practices as of early 1990 compared with the nine G30 recommendations. Each year the Group of Thirty issues an updated status report which provides current information on each country's progress toward adherence to the G30 recommendations. The 1991 status report is expected to be available for distribution this June. The U.S. chapter of the report is available now and is enclosed for your information. In the United States, a Working Committee was established to study the existing settlement systems in the United States. This committee consists of representatives from brokers, banks, financial intermediaries and other major industry organizations including the Investment Company Institute. The U.S. Working Committee ("USWC") representatives met with SEC Chairman Breeden at a "Roundtable" on November 27, 1990. The USWC presented the following proposals for change to the U.S. securities markets based on two of the nine G30 recommendations - moving to a T+3 settlement period and adopting a same-day funds payment convention: o By 1992, settlements and other movements of corporate and municipal securities must be effected only by book-entry movements within a depository for transactions among financial intermediaries (brokers, dealers, and banks) and between financial intermediaries and their institutional clients. o By 1992, all new corporate or municipal securities issued must be eligible for

depository processing, and procedures have to be developed to monitor inappropriate sale transactions during new issue stabilization periods. o In 1992, all payments for settlements among financial intermediaries and their institutional customers should be made using same-day funds. This would also apply to payments associated with dividends, interest, redemptions, and reorganizations. The 1992 time frame is subject to validation as implementation plans are developed. -3- o By 1993, settlements of corporate and municipal securities must be effected on T+3 only by book-entry for all market participants. Alternatives to the immobilization of assets of retail customers at financial intermediaries will need to be in place prior to the implementation of book-entry settlement. The USWC proposed a direct registration system for assets of retail customers. Notwithstanding the USWC presentations to the SEC at the "Roundtable", objections were raised by some of the participants in the industry groups. In particular, representatives of the Depository Trust Company ("DTC") and a major regional retail stockbroker objected to the implementation schedule as well as several general provisions. While DTC acknowledged that T+3 settlement and same-day funds are worthwhile goals, it stated that, at this time, the costs of implementation outweigh the benefits to be gained. DTC suggested that the costs of developing and operating a same-day funds system be measured carefully against the risks and associated costs of the current next-day funds environment. DTC also stated that other projects to expand and improve U.S. settlement systems must be considered before giving priority to implementation of the G30 recommendations. DTC questioned the time frames set for implementation by the G30 as it will need to make substantial system changes to support the G30 recommendations. These system changes will take significantly longer than the G30 schedule. The regional retail broker/dealers are concerned that the costs associated with making cash available for security settlements on T+3 could drive smaller firms out of business, or if passed on to investors, could discourage individual participation in the financial markets. Some firms may require money on deposit before executing a trade, branches may have to "chase down" customer payments in order to meet shorter time frames, and customers could lose the right to inspect and verify a physical confirmation prior to payment. Retail investors may find that dealing as individuals within this new environment is too cumbersome. This may drive many individuals from the marketplace altogether and may force smaller broker/dealers out of business. Chairman Breeden, while supporting the efforts of the USWC and most of the G30 recommendations, departed from a major G30 proposal and took an unusual position stating that individual shareholders should continue to be able to request physical stock -4- certificates. The regional retail broker/dealers in particular were counting on the reduced costs resulting from the immobilization of certificates to partially offset the potentially significant ongoing costs associated with the need for settlement funds on T+3. Chairman Breeden responded to the questions raised by the regional retail broker/dealer community by asking Howard Shallcross of Merrill Lynch to form a Retail Committee. The Chairman asked that the Committee study the retail issues brought forth by the recommendations and report its findings to the Commission within six months. The Shallcross Retail Committee has been meeting regularly and should be reporting back to the SEC in May or June. At the "Roundtable", the SEC also asked the USWC to continue its efforts by documenting the steps necessary to implement changes to the U.S. settlement system. In January 1991, the USWC submitted a report called "Issues Affecting Implementation of The Group of Thirty Recommendation In the United States" to the Commission. The report outlines the issues critical to the implementation of the G30 recommendations and proposes an approach and a timetable for resolving these issues. The USWC is awaiting SEC comment. The USWC has subsequently issued a proposal for changes to the DTC Institutional Delivery ("ID") System to support T+3 settlement. It chartered the ID Focus Group which is made up of DTC and industry representatives to finalize the proposal. Presently, Donald O'Connor (VP -

Operations) and Diane Butler (Director, Operations/Fund Custody) are representing the Institute on the U.S. Working Committee and the ID Focus Group respectively. Diane M. Butler Donald E. O'Connor Director of Operations & Vice President - Operations Fund Custody Attachment Enclosure

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