

EXECUTIVE SUMMARY

THIS REPORT PRESENTS THE ASSESSMENT BY THE Group of Thirty (G30) Global Monitoring Committee (GMC) of developments in the clearing and settlement arena since the publication of the G30 report, *Global Clearing and Settlement: A Plan of Action*, in January 2003. It identifies places where progress is being made as well as areas where little or no progress is apparent. A great deal has already been achieved, but many recommendations require further work. The Global Monitoring Committee notes that the clearing and settlement objectives and goals set out only three years ago remain achievable and, in many cases, are already being progressively implemented. The Committee underscores that the improved infrastructure that would result from full implementation of the G30 recommendations would help enhance confidence in the markets themselves and ensure that the vision of a safer, more efficient global clearing and settlement system can be brought to fruition.

INTEROPERABILITY

Progress is being made in achieving the interoperability agenda, which seeks to facilitate clearing and settlement across different national and international systems. This is most evident in Europe, but advances are under way between the United States and Canada. In other regions, the G30's recommendations are being acted upon, but mainly at the level of domestic markets. The longer-run aim remains the achievement of interoperability on a global basis. Concerning specific recommendations of the original G30 report:

- Coordinated timing between systems is well advanced in domestic markets and in certain regions. The United States and Canada are largely synchronized. In Europe, the introduction of the Target 2 integrated infrastructure will allow better coordination of securities settlement and payments systems. In the Asia-Pacific markets, some barriers remain and further synchronization is needed. By far the most significant long-term

challenge will be synchronizing payment and securities settlement systems on a global scale. Progress to date on that front has been limited.

- The goal to have central counterparties in place and functioning in all major securities markets is almost fully implemented.
- The availability of securities lending is implemented at a basic level in all major markets. However, the supportive framework of law and regulation necessary to make the process an attractive economic proposition is not uniformly available in all markets. This is an area requiring further improvement.
- Significant progress on immobilization and the elimination of paper from clearing and settlement has been made, but paper and manual processes are still being used in some areas. Fully achieving this goal requires changes in law, business processes, and culture. Dematerialization remains the ultimate goal.
- The adoption of uniform messaging standards and communication protocols is under way, but not on a wide enough basis. While all large financial intermediaries have moved to adopt common international standards, most infrastructure providers still operate proprietary standards.
- The implementation of reference data standards has proven difficult. With no global owner of reference data and friction between the needs of the domestic and cross-border market users, progress has been slow. Future progress will require greater efforts by market infrastructure operators and international institutions with global reach.
- Automated institutional trade matching schemes exist in all major European markets, the United

States, and Canada, but not yet in Asia-Pacific markets, with the exception of Japan.

- Efforts to automate and standardize asset servicing processes, including corporate actions, tax relief arrangements, and restrictions on foreign ownership, are long-term goals that have yet to be achieved.

MITIGATING RISK

The G30's risk management agenda and recommendations center on financial, operational, and legal risks. Overall, there has been considerable progress in implementing the G30's recommendations in many areas, but in some cases the record is more mixed.

- On business continuity and disaster recovery planning, the news is positive. The implications of a large-scale market disruption have been carefully considered and improvements have been made in all major markets. The September 11, 2001 terrorist attacks, more recent acts of terrorism, epidemics of disease, and natural catastrophes have highlighted the stark consequences of inadequate and insufficiently tested disaster response plans. Business and government actors have undertaken planning exercises aimed at preparing for such circumstances.
- Risk management awareness among clearing and settlement services has clearly increased, but monitoring the extent of implementation among users of these services is beyond the scope of the G30 monitoring exercise. At present, the business models of individual service providers are not open enough. The G30 called for each provider to publish an outline of the risk framework, including underlying risk management processes and standards. In many markets this is a vital step where further action is required.
- Scenarios for dealing with a key market player that is disabled have yet to be addressed in

most markets. An appropriate response to such a scenario remains to be formulated. Greater international cooperation will be needed to coordinate the response to failure of international intermediaries.

- Limited progress has been made in some markets on ensuring the final simultaneous transfer and availability of assets. Although all major markets generally offer some variant of delivery versus payment (DvP), in many markets users are still exposed to ambiguity.
- All of the target 15 securities markets looked at by the GMC have generally adequate conditions of legal enforceability with respect to contracts.
- The G30's call to advance legal certainty over rights to securities, cash, or collateral raised complex legal issues regarding "conflict of law" and "substantive law" matters. Both of these are being addressed by work on The 2002 Hague Securities Convention and the future UNIDROIT Convention on Intermediated Securities.
- On the issue of better valuation and support for closeout netting arrangements, there have been a number of significant improvements. These include more flexible close-out netting methodologies and the passage of EU statutes that provide momentum for convergence of close-out netting laws in the European Union. On a global scale, the ISDA Model Netting Act provides a good template against which to measure national legislative fixes.

IMPROVING GOVERNANCE

On governance, the GMC reports progress in a number of areas and notes that boards and senior management are increasingly recognizing the critical importance of governance. Nonetheless, challenges remain; continued focus and effort are required on governance matters.

- Boards and management have an increasingly clear understanding of the need for experienced board membership and certain infrastructure providers are adopting appropriate guidelines.
- There is a clear regulatory framework in place within each of the 15 target markets to provide oversight of clearing and settlement activities.
- There is a continued lack of clarity around fair access to services for users in some markets, particularly in the case of cross-border users.
- Further effort will be required to ensure that user and other stakeholder interests are given equitable attention. As with a number of the

risk recommendations, these are matters for implementation by the industries concerned and by individual firms.

CONCLUSION

The members of the Global Monitoring Committee are heartened by the significant progress that has been achieved on many of the G30's recommendations during the last three years. But the Committee notes that a great deal remains to be done if the full efficiency gains of a truly global clearing and settlement system are to be achieved, while mitigating risk and ensuring sound governance. The GMC urges those involved to maintain their commitment to the goals laid out in 2003 and to the national, regional, and global efforts designed to achieve those goals.