

Speech

"Time is Money. Time is Risk" Prepared Remarks before the European Commission



Chair Gary Gensler

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Good afternoon. Thank you, Paulina, for the kind introduction. As is customary, I'd like to note that my views are my own as Chair of the Securities and Exchange Commission, and I am not speaking on behalf of my fellow Commissioners or the staff.

Three years ago this week, just after President Biden took the oath of office while his senior staff were still unpacking boxes, the GameStop events unfolded. Jen Psaki, the new press secretary, had to address these market events from the White House briefing room.^[1]

While you might not be surprised that a market issue reached the West Wing, part of this event related to market plumbing.

Rapidly changing prices led a number of brokers to restrict additional buying activity by their customers due to the clearinghouse making larger than usual margin calls. Many everyday investors lost access to the market at a critical time. Such a market plumbing issue was probably not something with which the new White House anticipated dealing.

This was a real-world example that the market plumbing of clearing and settling matters. As most homeowners know, when the plumbing is backed up ... well, things can get messy. So too in our capital markets.

The longer it takes for a trade to settle—the slower the plumbing—the more risk our markets assume and the more risk fundamentally that we all assume.

As a result of these events, market participants of all stripes called for shortening the settlement cycle.^[2] It also was part of the discussion during my Senate confirmation hearing for this job.^[3]

I'm happy to say, based upon rules adopted by the SEC last year and much work by market participants, just after the U.S. Memorial Day weekend 2024, we'll be cutting in half the timing of an important part of the U.S. market plumbing.

Importance of Clearing and Settling

Clearinghouses, quite central to market plumbing, are vital to our capital markets. They facilitate that which happens after you execute a transaction through the time that it settles. Standing in the middle of the securities markets, clearinghouses are the buyer to every seller and the seller to every buyer.

While central clearing does not eliminate all risk, it does lower it. First, clearinghouses do so by sitting in the middle and reducing the risks among and between counterparties. Second, they provide multi-party netting, which helps lower the overall margin (collateral) needed to be posted in the system. Further, central clearing

reduces risks through the robust rules of the clearinghouses themselves, including for the collection of initial and variation margin.

Importance of Shortening the Cycle

Time is money. Time is risk.

Thus, shortening the market plumbing of clearance and settlement saves money. It lowers risk. It increases efficiency, boosts liquidity, and promotes resiliency of the markets.

For everyday investors who sell their stock on a Monday, they will get their money on Tuesday.

For institutional players, it will free up liquidity that might otherwise be trapped in unsettled trades.

Cutting the settlement cycle in half also reduces the amount of margin, or collateral, that must be placed with the clearinghouse. The way the math works, it means about 29 percent less margin—that comes from the square root of two.

Don't worry, the rest of the math I reference simply is adding plus one or plus two to transaction dates.

Shortening the clearance part of the market plumbing (the time to ensure that all parties agree to the trade details) also lowers risk. The sooner the parties have allocated, confirmed, and affirmed the trade information for their transaction, the lower the likelihood of a settlement failing since the parties will have more time to identify and resolve any potential errors. The Bank of International Settlements first recommended T+0 affirmations 22 years ago.^[4] A decade later, CPMI-IOSCO reaffirmed this in their *Principles for Financial Market Infrastructures*.^[5]

Shortening the cycle also means reducing the credit, market, and liquidity risks of the clearinghouse.

Lowering risks for market participants and clearinghouses, alike, reduces the likelihood that any one entity's failure spreads risk to the financial system, making the system safer for everyone.

The Settlement Cycle Around the World

A settlement cycle of one day after the transaction (T+1) is not new here in the U.S. or around the globe.

In fact, here in the United States, our U.S. government securities market has been T+1 ever since we started central clearing of U.S. treasuries in 1986. We also have T+1 in securities options markets, much of the derivatives markets, and as the normal practice for mutual funds.^[6] U.S. commercial paper, certificates of deposit, and money market funds actually largely settle on the same day as the transaction (T+0).

A bit of history might surprise some in the audience, but the U.S. stock market settled at T+1 well into the 1920s. It was only with increasing volumes that the market plumbing was lengthened to a business week after a transaction (T+5). By the late 1960s and early 1970s, the U.S. market plumbing was breaking down. As a result of this "Paperwork Crisis," Congress for the first time in 1975 gave the SEC authorities to oversee central clearing and write rules to shorten the settlement cycle.^[7]

It took the Stock Market Crash of 1987 as well as a taskforce report before the Commission implemented our first settlement rule in 1995.^[8] That's when we shortened to T+3.^[9]

Similarly, around the globe, time is money and time is risk.

Israel moved to T+1 in 2012 for Tel Aviv Exchange's Clearing House member brokers' equity trades. Broker-to-broker trades in corporate and government bonds also settle T+1.^[10]

By 2014, the European Commission required equity markets in 29 member countries (including the U.K. pre-Brexit) to move to T+2 settlement, joining Germany, Bulgaria, and Slovenia, which were already settling T+2.^[11] We at the SEC followed suit in 2017.^[12]

The U.K. Gilt market has long been T+1.^[13]

Looking at some of the major markets in Asia, India completed moving its equity markets to T+1 in January 2023.^[14] Its sovereign debt has been T+1 since 2017.^[15]

In Japan, equities settle at T+2,^[16] while government bonds settle at T+1.^[17]

China actually has moved to same-day securities delivery (within four hours after market close) for its A-shares securities,^[18] though their related payments move in the banking system the next morning. In Hong Kong, settlement is T+2.^[19]

What's Happening During the U.S. Memorial Day Weekend 2024

While many Americans will be celebrating the unofficial start of summer over Memorial Day weekend, another important thing will be happening. We will transition in the United States to securities settlements of T+1 on May 28, 2024. What we're doing is getting back to the settlement cycle that we had in the United States most of the first 50 years of Memorial Days.^[20]

Investors in the U.S. will benefit. Again, time is money, time is risk.

This step also will help better unify the U.S. market structure, where Treasuries, options, and mutual funds already largely settle in one day.

Further, starting May 28, trades relating to initial public offerings will be shortened from T+4 to T+2.

Another important feature of the SEC's updated rules relates to activities that will be required on the same day that a transaction is executed. Brokers will be required to have policies and procedures reasonably designed to ensure completion of allocations, confirmations, and affirmations as soon as technologically practical.

In addition, registered advisers will be required to keep certain time-stamped records of allocations sent or received, confirmations received, and affirmations sent or received.

Clearing agencies also will be required to have policies and procedures to facilitate the straight-through processing of securities transactions, automating the entire trade process from execution to clearing and settling.

I would note Canada^[21] and Mexico^[22] are joining the U.S. in moving to T+1 on Monday, May 27, the U.S. Memorial Day.

The SEC staff has been working with market participants on implementation. Staff has been having discussions with clearing agencies, banks, broker-dealers, asset managers, service providers, and industry groups. Staff also has been reaching out to colleagues in regulatory agencies around the world.

Last August, Depository Trust & Clearing Corporation (DTCC) opened its testing environment for direct participants of its clearinghouses and their vendors. The Securities Industry and Financial Markets Association, Investment Company Institute, and DTCC have been serving as a forum for market participants to discuss issues, plan, and identify best practices.

While some market participants in Europe and elsewhere may be interested in a delay, I would note market participants in Europe and elsewhere transacting in the United States should ensure they are ready to shorten this market plumbing come the U.S. Memorial Day weekend. Market participants who haven't otherwise done so should be reaching out to U.S. counterparts that execute and clear their trades as well as doing the necessary testing.

Looking Forward

Looking forward, I want to raise four areas for further policy discussions.

First, with much of Asia and North America moving to shorten their settlement cycles, what should other nations do?

I understand that some of the challenges for Europe are different than those we have in the United States. You have dozens of regulated markets and 14 clearinghouses. Your sovereign debt markets are generally at T+2

while our Treasury market is already T+1.

The benefits, though, are just as real. Time is money, time is risk.

For a time going forward, we can expect a mismatch between the settlement cycles in Europe and the major markets in North America as well as Asia. It's not the first time, though, we've had such mismatches—10 years ago, you shortened to T+2 three years prior to us.

I'd also note it's not the first time we'd have mismatches between the settlement cycle for funds and their underlying portfolios. In the United States, we've long had transactions in mutual funds generally settle in one day. Mutual funds and ETFs have used a variety of tools to address settlement time mismatches between fund shares and portfolio investments, including cash reserves, lines of credit, and interfund lending facilities.

What we've learned from such settlement mismatches is, while there are costs, the markets have been able to handle them.

Second, as I look forward, I want to mention the Commission's recently adopted rules to facilitate additional central clearing for the U.S. Treasury market, which will be phased in over two-and-a-half years.^[23] The final rules make changes to enhance customer clearing and broaden the scope of which transactions clearinghouse members must clear. These rules will help to make the Treasury market more efficient, competitive, and resilient.

Third, looking forward, I think it's appropriate for regulators and market participants around the globe to start to consider the possibility of shortening the settlement cycle for currency trading. Currency markets worldwide currently settle T+2. Particularly if Europe and the U.K. were to join the major markets of North America and Asia in moving to T+1, we should start to engage now in conversations, along with central banks, about the possibility of shortening the currency trading settlement cycle.

Fourth, some markets already have moved to settlement cycles on the day of the transaction. This includes parts of U.S. money markets, parts of the Chinese equity markets, and most recently India has proposed doing so in some equity markets.^[24] Thus, looking forward, it raises the question as to whether further shortening beyond T+1 may be appropriate.

Conclusion

Some of you might know that I love romantic comedies. With Valentines Day just around the corner, let me mention the 1987 classic film "Moonstruck," starring Nicolas Cage and Cher. Cher plays Loretta, whose father is a plumber named Cosmo. In one scene, Cosmo shakes his head at a home's pipes, calling them garbage. Better pipes are bronze, he said. The best pipes, though, are copper.

In the U.S. we're upgrading our market plumbing from bronze to copper just after Memorial Day. It will make our market plumbing more resilient, timely, orderly, and efficient, benefitting investors and issuers alike. For those of you debating this in Europe, I think your market plumbing would benefit from copper as well.

Time is money. Time is risk.

[1] See The White House, "Press Briefing by Press Secretary Jen Psaki, Special Presidential Envoy for Climate John Kerry, and National Climate Advisor Gina McCarthy, January 27, 2021" (Jan. 27, 2021), *available at* <https://www.whitehouse.gov/briefing-room/press-briefings/2021/01/27/press-briefing-by-press-secretary-jen-psaki-special-presidential-envoy-for-climate-john-kerry-and-national-climate-advisor-gina-mccarthy-january-27-2021/>; Rev, "Press Secretary Jen Psaki White House Press Conference Transcript January 28" (Jan. 28, 2021), *available at* <https://www.rev.com/blog/transcripts/press-secretary-jen-psaki-white-house-press-conference-transcript-january-28>.

[2] See C-SPAN, "Robinhood CEO, Reddit Co-Founder & Others Testify On GameStop Stock: GameStop Hearing, Part 1" (Feb. 18, 2021), *available at* <https://www.c-span.org/video/?508545-1/gamestop-hearing-part-1>

[1] C-SPAN, Robinhood CEO, Reddit Co-Founder & Others Testify On GameStop Stock: GameStop Hearing, Part 2" (Feb. 18, 2021), *available at* <https://www.c-span.org/video/?508545-2/gamestop-hearing-part-2>; U.S. House of Representatives Committee on Financial Services, "Testimony of Kenneth C. Griffin, Founder and CEO of Citadel and Founder and Principal Shareholder of Citadel Securities" (Feb. 18, 2021), *available at* <https://docs.house.gov/meetings/BA/BA00/20210218/111207/HHRG-117-BA00-Wstate-GriffinK-20210218.pdf>; SIFMA, "Shortening the Settlement Cycle," *available at* <https://www.sifma.org/explore-issues/shortening-settlement-cycle/>.

[3] See U.S. Senate Committee on Banking, Housing, and Urban Affairs, "Nominations of Gary Gensler and Rohit Chopra" (March 2, 2021), *available at* <https://www.congress.gov/event/117th-congress/senate-event/328800/text>.

[4] See The Bank for International Settlements' Committee on Payment and Settlement Systems and Technical Committee of the International Organization of Securities Commissions, "Recommendations for Securities Settlement Systems" (Nov. 12, 2001), Pages 9-10, *available at* <https://www.bis.org/cpmi/publ/d46.pdf>.

[5] See The Bank for International Settlements' Committee on Payment and Settlement Systems and Technical Committee of the International Organization of Securities Commissions, "Principles for Financial Market Infrastructures" (April 2012), Page 141, *available at* <https://www.bis.org/cpmi/publ/d101a.pdf>.

[6] It is T+1 when trading directly with the fund family or the fund's transfer agent. When trading a mutual fund through a broker, it is T+2 settlement.

[7] See The Depository Trust & Clearing Corporation, "Guide to Clearance & Settlement: An Introduction to DTCC" (2022), Page 4, *available at* <https://www.dtcc.com/-/media/Files/Downloads/DTCC-Connection/DTCC-Interactive-Guide-to-Clearance-and-Settlement-2022.pdf>.

[8] The Report of the Bachmann Task Force on Clearance and Settlement Reform in the U.S. Securities Markets, submitted to the SEC in 1992, recommended shortening it from five days to three by 1994. See Report of the Bachmann Task Force on Clearance and Settlement Reform in U.S. Securities Markets, Submitted to The Chairman of the U.S. Securities and Exchange Commission (May 1992), *available at* https://www.sechistorical.org/collection/papers/1990/1992_0526_BachmannReport.pdf. The task force was headed by John W. Bachmann, the Managing Principal of Edward D. Jones & Co. of St. Louis, Missouri. The recommendations in the Bachmann Report were intended to help inform the Commission's approach to considering reforms of the national system for clearance and settlement.

[9] See Securities and Exchange Commission, "Securities Transactions Settlement" [Release No. 33-7022; 34-33023; IC-19768; File No. S7-5-93] (Oct. 13, 1993), Pages 52891-52909, *available at* https://archives.federalregister.gov/issue_slice/1993/10/13/52889-52917.pdf

[10] See Clearstream, "Israel: New T+1 settlement regime for equities" (March 18, 2012), *available at* <https://www.clearstream.com/clearstream-en/securities-services/settlement/israel-new-t-1-settlement-regime-for-equities-1299460>; Clearstream, "Settlement Process—Israel" (December 15, 2023), *available at* <https://www.clearstream.com/clearstream-en/securities-services/market-coverage/middle-east-and-africa/israel/settlement-process-israel-1281448>.

[11] See European Commission, "Regulation on securities settlement and on Central Securities Depositories in the EU ('CSD Regulation') – Frequently Asked Questions" (April 16, 2014), *available at* https://ec.europa.eu/commission/presscorner/detail/fr/MEMO_14_312.

[12] See Securities and Exchange Commission, "SEC Adopts T+2 Settlement Cycle for Securities Transactions" (March 22, 2017), *available at* <https://www.sec.gov/news/press-release/2017-68-0>.

[13] See European Union Economic and Financial Committee, "Responses from members of the EFC Subcommittee on EU Government Bonds and Bills Markets" (2019), *available at* <https://economic-financial-committee.europa.eu/system/files/2020-01/5%20-%20Market%20conventions.pdf>.

[14] See NSDL, "Roadmap for Introduction of T+1 Rolling Settlement Cycle in Equity Market" (Nov. 8, 2021), *available at* <https://nSDL.co.in/downloadables/pdf/Press%20Release%20-%20Joint%20Press%20Release%20for%20implementation%20of%20T+1%20Settlement.pdf>; The Times of

India, "Blue chips will shift to T+1 settlement cycle on Jan 27" (Jan. 16, 2023), *available at* <https://timesofindia.indiatimes.com/business/india-business/blue-chips-will-shift-to-t1-settlement-cycle-on-jan-27/articleshow/97016925.cms?from=mdr>.

[15] See Reserve Bank of India, "Government Securities Markets in India—A Primer" (April 1, 2020), Question #16, *available at* <https://www.rbi.org.in/commonperson/English/Scripts/FAQs.aspx?id=711#16>.

[16] See Japan Exchange Group, "Shortening of Settlement Cycle for Stocks and Other Securities (T+2)" (July 3, 2023), *available at* <https://www.jpx.co.jp/english/clearing-settlement/tplus2-settlement-cycle/index.html>.

[17] See Ministry of Finance, Japan, "Japanese Government Bonds" (May 2018), *available at* https://www.mof.go.jp/english/policy/jgbs/publication/newsletter/jgb2018_05e.pdf.

[18] A-shares securities are Chinese companies listed on Shanghai and Shenzhen exchanges.

[19] See Nomura Research Institute, "Stock Exchange of Hong Kong (SEHK) and China Stock Connect (CSC) Settlements: NRI Support," *available at* <https://www.nrifintech.com/stock-exchange-of-hong-kong-and-china-stock-connect.html>.

[20] See U.S. Department of Veterans Affairs, "The Origins of Memorial Day," *available at* <https://www.va.gov/opa/publications/celebrate/memday.pdf>.

[21] See Financial Technologies Forum, "T+1 in Canada: Same Goal, Different Plays" (Nov. 30, 2023), *available at* <https://www.ftfnews.com/blog/t1-in-canada-same-goal-different-plays/>.

[22] See CCV, "Announcement to Market Participants" (July 11, 2023), *available at* <https://www.dtcc.com/ust1/-/media/Files/PDFs/T2/CCV-y-AMIB-T1-Anuncio-Ingles>.

[23] See Securities and Exchange Commission, "SEC Adopts Rules to Improve Risk Management in Clearance and Settlement and Facilitate Additional Central Clearing for the U.S. Treasury Market" (Dec. 13, 2023), *available at* <https://www.sec.gov/news/press-release/2023-247>.

[24] See "SEBI Chairperson Madhabi Puri Buch On T+0 Settlement | BQ Prime" (Nov. 26, 2023), *available at* <https://www.youtube.com/watch?v=4WJ7VI26JE4>. In these markets, it tends to be on a post-transaction, net settlement basis. This allows for the benefit of netting, which reduces risk in the system.