

# IMPORTANT NOTICE

**The Depository Trust Company**



**#:** 7045-10  
**Date:** August 3, 2010  
**To:** All DTCC Participants, Paying Agents and Issuers  
**Category:** Operations, Asset Servicing, Dividends  
**From:** DTCC Asset Services  
**Attention:** Operations Managers, Officers  
**Subject:** P&I Payment Refinement – An Industry Update

In November 2009, DTCC released to the industry a White Paper entitled “P&I Payment Refinement: A Move to Further Reduce Payment Risk.”<sup>1</sup> This document described the current practice employed by DTCC’s depository subsidiary, The Depository Trust Company (DTC), for:

- the allocation of P&I cash entitlements<sup>2</sup> due on DTC-eligible securities
- how this practice contained inherent risks, and,
- DTC’s decision to eliminate these risks through changes to the current practice that will be effective in early 2011.

This Notice will summarize the existing condition, describe the changes to be made to the current allocation methodology and update the industry on the progress made within all links in the payment chain to support this effort.

DTC will move from a practice of allocating virtually all entitlements on the payable date – regardless of the timing of payments or their identification at a CUSIP-level – to one where only timely paid and identified entitlements<sup>3</sup> are allocated to DTC participants. The current practice includes inherent risks associated with allocating late-funded and unidentified payments – the failure of an issuer or participant between the allocation of an entitlement and its reconciliation. The revised allocation methodology eliminates that risk by only allocating an entitlement once its receipt can be confirmed at a CUSIP level. In addition, the methodology creates a consistent approach to entitlement processing as P&I payments will now follow an approach similar to the manner in which Reorganization corporate actions and MMI payments have long been handled.

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<sup>1</sup> Available for download at [http://www.dtcc.com/downloads/leadership/whitepapers/Payment\\_Refinement.pdf](http://www.dtcc.com/downloads/leadership/whitepapers/Payment_Refinement.pdf)

<sup>2</sup> P&I payments include dividend, interest, periodic principal, redemption and maturity payments on non-MMI securities.

<sup>3</sup> The established cut-off for timely payments and CUSIP-level detail is 3:00 p.m. ET.

Non-Confidential

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DTC appreciates the attention and support this issue has received from all stakeholders and the continued improvement in both payment timeliness and identification of payments – key components to ensuring payable date allocation upon implementation of the revised methodology.

By announcing its intent to sunset the current allocation practice well in advance of implementation, DTC has given customers and key stakeholders more than 13 months to prepare for the coming change. Upon release of the White Paper, DTCC customers asked for a tool to measure the impact of this change at a participant level and identify current allocations occurring in a manner not consistent with the proposed methodology. In January, a weekly report was added to DTCC SMART/Search that allows participants to measure the impact of imprecise allocations on their organizations, as well as build a history of noncompliant payments to assist in allocation decisions.

Also in January, DTC formed an industry task force of participants, paying agents and relevant industry groups to ensure broad-based participation of stakeholders as they moved toward a revised P&I allocation process. Comprised of more than 20 organizations, the P&I Refinement task force has met five times so far in 2010 to:

- review and discuss performance critical to supporting the revised allocation practice
- investigate ways to reduce the number of late and unidentified payments, and,
- propose enhancements to current reporting.

Certain enhancements to participant reporting have already been delivered, including the ability to download Same-Day Allocation Reporting (SDAR). Others are being developed for deployment in late 3Q 2010 such as increasing the transmission frequency of allocation information and the timing of information on unallocated CUSIPs to allow participants to make their allocation decisions based on the most up-to-date issuer and agent funding to DTC.

The P&I processing public metrics posted to dtcc.com have been revised and the universe of paying agents on whom performance is reported<sup>4</sup> has been expanded. The revised metrics are critical measures supporting the refinement effort and by expanding the number of agents on whom performance is reported, statistics are now reported for 80% - 90% of all P&I payments to DTC – up from the original coverage of 60%. In an effort to further promote awareness, DTC has also presented to a number of industry groups and will continue to do so as we move closer to implementation.

Paying agents have also been working diligently to prepare for the revised allocation methodology by reviewing the timing of funding from issuer customers and operational processes to ensure optimized payment routines, as well as timely funding and delivery of CUSIP detail. Agents have actively reviewed late payment detail provided by DTC. Many of the largest agents are now investigating this information to identify the root cause of defects and make certain that entitlements will still make their way to share and bondholders on the payable date. The identification and reporting of these conditions will cause those parties to revise processes, and these individual improvements will reflect greater operational efficiencies accruing to agents, DTC and participants.

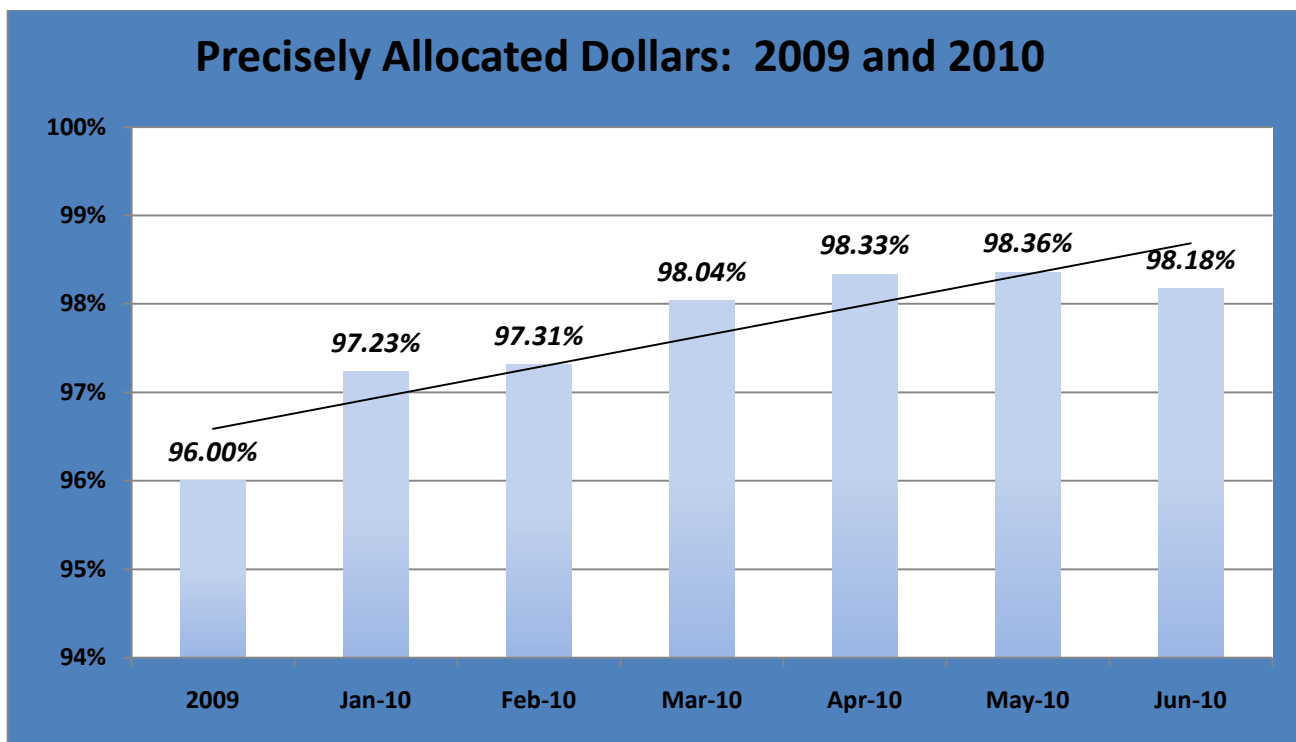
Awareness of P&I allocation refinement has also been aided through the direct contact of nearly 4,000 different issuers and agents making entitlement payments to DTC. P&I processing staff have shared

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<sup>4</sup> Available at [http://www.dtcc.com/products/asset/report\\_card\\_sigmas\\_cash.php](http://www.dtcc.com/products/asset/report_card_sigmas_cash.php)

the White Paper with their agent and issuer contacts, explained the change to processing and how the timely funding and delivery of CUSIP detail is critical to assure continued payable date credit of entitlements to DTC customers.

The performance improvement stemming from the efforts of paying agents, issuers and DTC has been clear and sustained. The two most important measures supporting a smooth transition to P&I refinement have both shown strong gains since 2009. These two measures – the timing of payments to DTC and the percentage of entitlements allocated in a manner consistent with the refined P&I allocation methodology (“precise” based on timely identified funding) – have improved throughout 2010. As the chart below shows, DTC allocated 96% of P&I payments in a precise manner in 2009 and that measure has averaged more than 98% for March through June 2010. As awareness continues to permeate and benefits continue to accrue from process improvement, the expectation is that this positive trend will continue.



Additionally, DTC will launch later this quarter a new P&I web page on its website that will provide P&I news and updates, links to the White Paper and Operational Arrangements, appropriate user guides, FAQ’s, best practice and metrics. The online resource will serve as a complete repository of resources for issuers, paying agents, service providers and DTC customers.

Participants with questions regarding this SMART/Search or this Notice should contact their relationship manager. Paying agents or issuers with questions or comments should contact the following P&I processing managers: Ed Collins ([ecollins@dtcc.com](mailto:ecollins@dtcc.com)), Joseph McGuire ([jmcguire@dtcc.com](mailto:jmcguire@dtcc.com)) or Robert Olivari ([rolivari@dtcc.com](mailto:rolivari@dtcc.com)).