



Achieving Straight Through Processing for US Corporate Actions

By Brett Lancaster, vice president of The Depository Trust & Clearing Corporation

It's no great secret that corporate actions remain one of the most risky and costly areas within financial services. The key challenges in corporate actions communication have been clear for some time, but a convergence of factors has presented an historic opportunity and provided a definite solution that can remove the risk and cost almost entirely from the process.

The Current State of Corporate Actions

Corporate actions face four broad challenges:

- No definitive list of all corporate action event types. The current standard, ISO 15022, defines about 60 types, with further sub-classifications, but some are missing, (for example, 'plan of re-organisation') and some are too flexible (for example, 'OTHR').
- No definitive list of underlying data fields for each event. About 200 fields are missing from the standard (for example, tax details, instruction details, status flags).
- No unique identifier. Currently, explicit identification of a corporate action between financial intermediaries is difficult. A unique ID would function in the same way that an ISIN, SEDOL or CUSIP is used in static security data.
- Highly inefficient dissemination process. Issuers fulfil their obligation by sending out a press release, prospectus or legal filing written in free text, ungoverned by formal standards or market practice. Regulation in the US by the Securities Exchange Commission (SEC) mandates filings into the EDGAR system, but this covers only a subset of event types, does not list all data fields and does not mandate electronic disclosure.

An acceptable solution to this mess has eluded the industry for many years and the financial services industry continues to pay the price. If a company makes a decision based on incorrect corporate action information (for example, a date or a payout rate is incorrect) the financial exposure can be significant. Events don't often go wrong, but when they do, it can be costly. Oxera has estimated the actual losses to be between US\$400 and US\$900 million globally, per year. Change is afoot, however, with the 'perfect storm' of current economic events and the availability of new standards and technology.

The Drivers of Change

Four disparate factors have marked this time of change:

- Economic conditions. The recent financial market turmoil has increased the focus, especially from regulators, on reducing risks, improving transparency and protecting the investor.
- Customer demand. Customers need to do 'more with less' and can no longer afford to pay the huge price tag for market inefficiencies. They are demanding high STP solutions that align with standards and use a universal unique ID.
- Standards maturity. Swift and ISO are driving the next generation standard, ISO 20022, which builds upon the success of ISO 15022.
- XBRL maturity. XBRL, which enables seamless electronic disclosure, is already being institutionalised to issuers in the US with the SEC mandate for the GAAP quarterly financial reporting that came into effect on 15 June 2009. We have a unique opportunity to solve the corporate action problem, starting

with the US and our implementation of a three step plan is already underway.

Step 1: Drive the 'next generation' industry standard for corporate actions

Swift standards with market practice groups have done much to cement ISO 15022 as the corporate actions standard, but it has too many gaps. The next generation standard, ISO 20022, will be global and holistic. Scheduled for release in December 2009, it allows the addition of all the 'missing' data elements.

However, simply having a standard is insufficient; it must be part of a firm's day to day activity, or it doesn't get used. To help overcome this enforcement issue, the DTCC depository for the entire US market will become an early adopter of ISO 20022, making the standard the backbone of its Corporate Actions Re-engineering - a major, multi-year, project spanning announcements, elections to payments. DTCC will be offering ISO 20022 messages, targeted for the end 2010, decommissioning all existing proprietary files on, or before, 2015.

Step 2: Implement a registration system to issue a 'unique ID'

As part of Corporate Actions Re-engineering, DTCC will create a 'unique ID' process to explicitly label all corporate action announcements from the beginning, thus eliminating ambiguity in the update process and the identification of an event between all parties.

The registration system will also allow for additional validation, if needed, by the issuer, (for example, to check that rates are within historical norms and that dates are set logically).

Step 3: Drive issuer-based data tagging with XBRL

The proven technology of XBRL can bring an end to the madness of paper-

based documentation and the problems of accuracy, timeliness and event misidentification that come with the manual entry and re-entry of data.

XBRL is an international, non-profit consortium dedicated to driving transparency through enhanced business reporting. XBRL enables issuers to electronically 'tag' data from within Microsoft Word. The issuer, when writing the press release or prospectus, follows the regular process, except they tag key data. The tagged data is 'embedded' within the saved .pdf or .doc file. Further, the XBRL taxonomy will be seamlessly aligned with ISO 20022.

For corporate actions, XBRL will be a quantum leap forward, but, once again, it will not be a sufficient condition to achieve STP without enforcement. Since the SEC mandated XBRL for GAAP quarterly financial reporting, we seek to leverage this precedent and achieve the same treatment for corporate actions.

Benefits

This initiative will deliver significant change with significant benefits, from issuer to investor:

- For issuers. The intent and content of the originating offer will be clear to the investor and conveyed in a timely fashion without fear of misinterpretation due to manual manipulation. Issuers will incur marginal additional effort in tagging the data but will follow exactly the same process as they undertake today.
- For the financial services industry. It will significantly reduce interpretation, re-keying and manual exceptions. It will result in lower risk exposure to investor decisions based on incorrect information, (estimated at US\$10 billion annually) and reduce need for manual processing (estimated at US\$200 million annually). The lower costs and risks can reduce fees to investors.
- For investors. Investors can make decisions with guaranteed accurate information from the source document

without third party manual interpretation. It will allow more response time as custodians and investment managers will no longer have to artificially compress deadlines to compensate for the manual processing of elective information. It also lowers costs, as transaction fees should be reduced. The solution is clear and attainable. By implementing ISO 20022, a unique ID and XBRL, we can eliminate significant costs and risks, and realise STP for US corporate actions.

With a successful implementation of the pilot in the US, we would like to see XBRL expanded into other markets. Certainly, we applaud the great strides that have already been achieved using XBRL within corporate actions, especially by Japan (Tokyo Stock Exchange) and by China (Shenzhen Stock Exchange). We want to further collaborate with the local markets to determine how to use XBRL as the backbone for corporate actions reporting on a global basis.

XBRL Revolution

Reducing Risk for Corporate Actions

"The benefits to the industry will be significant, as the tagging of information at the source with XBRL (and then aligning the data with ISO standards) will fundamentally change corporate actions. Issuers will be assured that the intent and content of the originating offer are clear to the investor. Financial intermediaries can significantly reduce the levels of interpretation, re-keying and manual exceptions, and investors can make decisions with guaranteed accurate information. The costs and risks now absorbed by the industry will disappear."

— Brett Lancaster, DTCC Vice President

Join Brett Lancaster for the Tuesday, 15 September SIBOS session at 14:00. Topic: XBRL and SWIFT join forces to improve transparency and increase automation.



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