



DTCC Offers ISO 15022 Version Of GCA Validation Service

By Lisa Argento

DTCC has adopted the ISO 15022 international messaging standard for its Global Corporate Action (GCA) Validation Service to meet global interest in the service.

In addition, several corporate action solutions providers have certified their interoperability with ISO 15022 GCA Validation Service output, including Xcitek, Information Mosaic, [continued on page 9]

DTC Establishes New Settlement Link with Canadian Depository

By Edward C. Kelleher

The Depository Trust Company (DTC), a DTCC subsidiary, plans to establish a link with The Canadian Depository for Securities, Ltd. (CDS), the national central securities depository of Canada, that for the first time will support the processing and settlement of Canadian dollar transactions at DTC. The new link, which is subject to regulatory approval, is scheduled to be implemented for select pilot participants in the third quarter [continued on page 5]

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DTCC Expands Deriv/SERV Platform To Support Interest Rate, Equity and Variance Swaps

By Judy Inosanto

The Depository Trust & Clearing Corporation (DTCC) announced today its Deriv/SERV platform was once again expanding to provide affirmation and automated matching and confirmation services for interest rate swaps and swaptions, equity swaps and variance swaps.

The expansion of Deriv/SERV was the result of intensive collaboration with both the dealer and buy-side communities over a period of months. Support for interest rate swaps and swaptions will begin immediately and equity swaps and variance swaps will begin next month.

"We are pleased to have worked with DTCC along with other key members of the OTC derivatives market to add these products to the Deriv/SERV platform," said Ann Marie Davis, managing director, Global Operations, Citadel Investment Group LLC. "The ability to process trades for all our derivatives products through a single platform is of particular interest to us and other market participants. This expansion in Deriv/SERV's services is an important move in that direction."

"These recent enhancements reflect DTCC's commitment to delivering a fully-automated processing solution for a broad range of products in the OTC derivatives market," said Janet Wynn, managing director and general manager, DTCC Deriv/SERV. "We believe that these additions will be particularly attractive to our 100 buy-side customers, who are charged no fees to use our various OTC derivatives processing services, as well as the 23 major global dealers, who will benefit from higher trade confirmation rates."

The addition of these new products leverages Deriv/SERV's capabilities already in place for single reference entity credit default swaps, credit default swap indices, equity index options and equity share options. As with these other products, Deriv/SERV's two-sided, real-time matching and confirmation for equity swaps and variance swaps will also handle such trade life cycle events as new trades, full or partial terminations, increases, amendments and exits.

The interest rate swaps and swaptions service will support affirmation or matching using a short form record designed specifically for the buy-side, including new trade and exits events, with support for assignments, allocations, amendments and full

and partial termination capabilities and a long form record being added during 2005 and early 2006.

Customers currently using the Deriv/SERV platform will be able to begin affirming, matching and confirming transactions for these new products immediately. For new customers, they can access the service through an easily accessible Internet connection.

"We have worked hard to fashion flexible, automated confirmation processes for both interest rate swaps and equity and variance swaps that offer firms a choice of affirmation or two-sided matching that are well suited for the dealer-to-customer market," said Peter Axilrod, managing director, Business Development for DTCC.

DTCC first entered the OTC derivatives market in November 2003, in response to requests from major dealers and banks that were looking to develop automated processing solutions that could help them efficiently and safely manage the industry's rapid growth rate. First supporting real-time, two sided matching and confirmation for credit default swaps, Wynn noted that the service has been an important driver in helping increase automation rates in these products.

According to the International Swaps and Derivatives Association (ISDA), automated confirmation of credit derivatives trades has grown from about 6% in the beginning of 2004 to over 40% by the end of June 2005. DTCC points to this progress in confirming trades as evidence of Deriv/SERV success in helping to bring added efficiency and greater certainty in this market space. @



FICC Receives OK to Ban Pre-Netting Practices; Move Will Reduce Risk in U.S. Government Securities Market

By Nicholas Clarke

In a move to bring added safety and soundness to U.S. government securities processing, Fixed Income Clearing Corporation (FICC) has received regulatory approval from the Securities and Exchange Commission (SEC) to prohibit certain affiliates of FICC netting members from pre-netting their government securities trades outside of FICC. FICC is a subsidiary of DTCC.

Pre-netting involves any trade submission practice other than submitting transactions directly to FICC on a trade-by-trade basis as executed, and which identifies the actual parties to the trade. The ruling, which is effective immediately, expands FICC's trade submission requirements to all netting-eligible trades executed by certain affiliates of FICC netting members, who are U.S.-registered broker-dealers, banks, or futures commission merchants. Failure to comply with the new ruling could lead to fines or termination of FICC membership.

"This change validates what DTCC has long known, and that is the risk caused by pre-netting poses a considerable threat to the safety and soundness of FICC's clearance and settlement services and the market itself," said Jeff Ingber, managing director and general manager for DTCC's Fixed Income Clearance and Settlement.

Indeed, it was recognition of this risk by the industry that was the driving force behind the creation of the Government Securities Clearing Corporation, a predecessor company of FICC, almost 20 years ago, he noted.

"That some FICC members and their affiliates are engaging in pre-netting runs counter to the spirit and intent of why FICC was formed in the first place," Ingber continued. "With FICC ultimately guaranteeing the settlement of each government securities transaction it accepts into the net, members gain assurance about the accuracy of settled trades and any potential credit losses associated with unsettled trades."

On average, FICC's netting process safely eliminates some \$2.8 trillion a day in settlement risk posed by more than 100,000 government securities transactions a day.

Industry Input

FICC consulted with a number of industry organizations and members before its SEC filing to prohibit pre-netting and broaden trade submission and reporting requirements.

Eric Foster, vice president and associate general counsel of The Bond Market Association, said, "As the only U.S. government securities clearing agency registered under the Securities Exchange Act of 1934, FICC plays a crucial role in maintaining

the proper functioning of one of the largest fixed income markets in the world: the primary and secondary market for U.S. government securities. Anything that takes away from FICC's internal risk management and dilutes the FICC guarantee that is a cornerstone of the government securities market is a serious

threat, and one that the SEC has rightly defused with its ruling."

Ending Pre-Netting Risks

The issue with pre-netting is that it masks member trading activity and information and undermines the transparency that is at the heart of FICC's clearing and settling process.

For example, one form of pre-netting, called "compression," allowed a clearing member to submit netted trade data to FICC's Government Securities Division (GSD) in a way that conceals the party that executed the transactions. Another form of pre-netting is "internalization," whereby a clearing member executes affiliates' trades within its own record-keeping system and fails to report data on those trades to FICC.

Yet another example of pre-netting is "summarization," a technique under which a clearing member delays submitting individual trades to FICC when they occur and holds them until additional trades can be combined and submitted as a single trade.

"With the huge and growing market in government securities, the failure of FICC members and affiliates to submit all eligible trading activity could impede FICC's ability to accurately identify its risks and collateralize its exposure," explained Tom Quaranta, managing director, FICC Client Support. "That's why it's imperative for FICC members to promptly stop any pre-netting and start working immediately on identifying their covered affiliates and determining how those affiliates will be submitting their trading activity to GSD."

"The new affiliate trade submission and reporting requirements are a necessary change and should pay dividends to FICC, our members, and the broader government securities market," added Bob Trapani, vice president, FICC Marketing. @



Intel Among First to go Paperless Following Delaware Law Change

By Jim Conmy

As the first splash in what many securities industry executives hope will grow into a swelling stream, Intel Corporation announced that as of August 1, it began issuing its common stock only via paperless electronic ownership records.

Now that the state of Delaware has eliminated its law requiring companies incorporated in the state to issue paper stock certificates, Intel Corporate Affairs Group Senior Attorney Doug Stewart said the company plans to issue all its shares through the Direct Registration System (DRS). DRS allows investors to keep ownership of their shares registered electronically directly with the issuing company or its transfer agent, so that no paper certificates are involved. Shares can also be held electronically in “street name” through a broker.

Intel and its transfer agent, Computershare Investor Services, said that as of August 1 – the date Delaware’s new law took effect – the company began issuing all new shares electronically through DRS. While Intel has been steadily issuing its stock through DRS for several years, the company also has a sizeable percentage of its stock outstanding in paper form – represented by about 400,000 certificates – because of Delaware’s law.

Change by Attrition

“Intel is making the switch to electronic ownership easy,” said Computershare Transfer Operations Manager Lisa Brooks. “Intel shareholders are not required to turn in their physical certificates,” she explained, “although they can do so at any time if they want to take advantage of electronic ownership. However,” she noted, “from now on Intel will simply no

longer issue paper certificates for any transactions involving its stock.”

Shareholders who purchase Intel stock will receive a statement of electronic

ownership rather than paper certificates that have to be placed in safekeeping.

DTCC’s depository, which manages DRS

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And Then There Were . . . Two

After Delaware passed HB 150 allowing public companies incorporated there to issue uncertificated shares, Louisiana and Missouri enacted similar legislation. This leaves Arizona and Puerto Rico as the only remaining U.S. jurisdictions that still require public companies incorporated there to issue paper stock certificates.

Delaware's new law (HB 150) went into effect August 1, 2005. Louisiana's new law (HB 645) became effective on Aug. 15, and Missouri's bill (HB 678) goes into effect on Aug. 28.

For readers who want more information, here are the Internet sites that offer details for each state:

- **Delaware HB 150:**
<http://www.legis.state.de.us/LIS/LIS143.NSF/93487d394bc01014882569a4007a4cb7/7bb625ddc7b0a3c585256fe80069641c?OpenDocument>
- **Louisiana HB 645:**
<http://www.legis.state.la.us/billdata/byinst.asp?sessionid=05RS&billtype=HB&billno=645>
- **Missouri HB 678:**
<http://www.house.state.mo.us/bills051/bills/hb678.htm>

FICC Sets New Processing Records For Government, Mortgage-backed Securities

By Nicholas Clarke

Reflecting continued strong demand for both U.S. Government and mortgage-backed securities, DTCC's Fixed Income Clearing Corporation (FICC) recently set two new processing records.

- On June 30, FICC's Government Securities Division (GSD) processed an unprecedented \$6.1 trillion in government securities trades into the netting system, an 11% rise over the previous daily record of \$5.5 trillion set earlier this year on March 31. On an average day, GSD nets more than \$3.6 trillion in government securities.
- And on June 9, FICC's Mortgage-Backed Securities Division (MBSD) processed an all-time high of 44,532 Electronic Pool Notification (EPN) messages, eclipsing the previous daily record of 40,368 notifications by 10%.

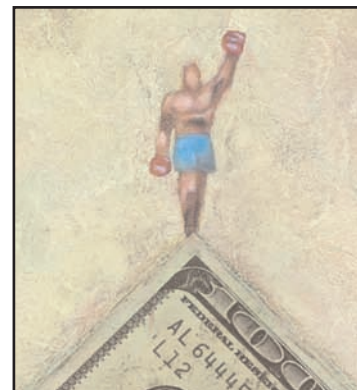
"What distinguishes our processing milestones is that each time we continue to achieve them without missing a beat," said Jeff Ingber, DTCC's general manager, Fixed Income Clearance and Settlement. "And, as is true for all FICC solutions, our netting and EPN services contribute to the safety and soundness of the industry and protect our customers in a marketplace that

continues to grow in both size and complexity."

Several factors account for the growing volume in government securities trades and EPN messages processed by FICC, said Ingber. Looking at government securities, one reason is the addition of new members as well as new

executing firms who clear their government securities transactions through GSD's direct members. For instance, GSD added 37 executing firms in the past year, bringing the total number of such firms to almost 1,000.

Another contributing factor to increasing GSD processing numbers, Ingber said, is the rise in the number of transactions being submitted to FICC by electronic trading systems (ETs). In addition, he said that the number of collateral substitutions for repurchase agreements (repos) – larger than usual – was effected



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DTC Establishes New Settlement Link *Continued from cover*

of 2005 and available to all DTC customers in the fourth quarter or early in 2006.

The proposed link, the first DTC link to support settlement in a foreign currency, will provide participants with a single depository interface for U.S. and Canadian dollar transactions. This will reduce cross-border processing costs and inefficiencies by eliminating problems associated with maintaining split inventories in Canadian issues. In split inventories, some portion of a position in a dually listed issue is maintained in CDS for Canadian dollar settlement and the remainder is with DTC for U.S. dollar settlement. The new link will permit DTCC customers to concentrate all U.S.

and Canadian security positions in their DTC accounts.

"Since the early 1980s, DTCC subsidiaries and CDS have developed linkages and close working relationships," said John Abel, DTCC vice president, Product Development. "The existing links between CDS and DTCC are among the most robust inter-market links in the world, processing more than a million transactions each month. But up until now, these links only supported transactions involving U.S. dollars."

The new link, which will be implemented using a DTC omnibus account at CDS, will support transactions sent by a DTC participant to a CDS broker or custodian as well as those sent by CDS

brokers and custodians to DTC participants. It will also support Canadian dollar transactions between DTC participants.

As with U.S. dollar transactions, participants' security positions received via Canadian dollars will immediately be available for redelivery in DTC. DTC has also developed an end-of-day settlement process to settle Canadian dollar obligations; these obligations will be calculated and displayed to participants via new DTC display screens.

Editor's Note: For more information on the new settlement link with The Canadian Depository for Securities, Ltd., contact John Abel at (212) 855-8434 or jabel@dtcc.com. @

Sorting Out the Future of Post-Settlement

DTCC's Janet Wynn, managing director and general manager of DTCC's Asset Services, Deriv/SERV and International businesses, talks about the changes she sees ahead for asset servicing as new financial instruments, rocketing trade volumes and trans-global deals all make traditional ways of servicing assets and administering corporate actions look increasingly outmoded.

@dtcc: You talked about the need for new asset servicing models at the SIA's Operations Conference in May. What's behind this need?

Wynn: Size and complexity. Post-settlement processing – things like reorganizations, redemptions and dividend payments – is a multi-trillion dollar business today. The capital markets have demonstrated enormous innovation over the years, so that what started out as simple dividend and interest payments have become a lot more complicated. Trading across markets and new asset classes like structured and synthetic securities have introduced new challenges.

@dtcc: For example?

Wynn: Well, if you're a depository holding \$100 million worth of IBM stock, which might be 1.2 million shares, the dividend payout is straightforward. It goes from one source or paying agent to DTCC to many institutional shareholders. On the other hand, if you're holding \$100 million worth of asset-backed securities, first of all, you might have 20 issuers; so at a minimum you need to collect paying information from more sources. In addition, the calculations are more complicated. They vary each period because of pay-downs, for which there are many more post-payable adjustments and recalculations – not to mention potential delays in receipt of the information. And if you had a \$100 million in over-the-counter derivatives, like credit default swaps, which are actually contracts, you wouldn't have 20 issuers. You'd likely have 20 firms on one side and 20 firms

on the other with 20 bilateral contracts, and so you'd have a "many to many" payment situation. Also, there's no simple way to do the payment calculations; each contract is unique. Thus, unless there is a central service provider, we see the potential for firms having to connect to and exchange payments information with a very large number of end points.

@dtcc: How is DTCC approaching these challenges?

Wynn: One of the things we're doing is totally reengineering our underwriting and corporate actions systems. We want to automate as much of the underwriting process as possible in order to reduce costs and risk. We also want to readily accommodate new asset classes and capture information on new securities, such as payment obligations, right during the underwriting process.

Later, that information can be fed automatically into any corporate action announcements. We're also building an entirely new platform for corporate actions and dividend processing. We need to make this a far more automated and standardized business that can be scaled up to handle rising volumes and cross-border, multi-currency transactions as well as the kind of "many-to-many" information and payment scenario I just mentioned. Really, what we're trying to do is rebuild the technology backbone we think we'll need to meet the post-settlement processing challenges we see coming.

@dtcc: What else are you doing?

Wynn: Well, we're very focused on improving the quality of all of our

services. In the traditional cash markets for equities, corporate bonds and municipal paper, we have honed the processes for interest and dividend payments so that we're up close to the "three 9s" (99.9%) for reliability and accuracy and completion. Our "stake in the ground" is that we're committed to striving for that level of reliability and accuracy for every kind of asset class we service or expect to service.

@dtcc: Even for the new asset classes you mentioned, such as asset-backed securities, credit-default swaps and other over-the-counter derivatives?

Wynn: Yes, and here's why. As we come to grips with the complexity of many of the new instruments and asset classes, we're stepping back to look at this as an industry service provider, and we can see there's an important role we can play. We can function as an asset-servicing hub, where we gather and dispense information and instructions from all the parties involved: issuers, paying agents, individual counterparties and so on. The idea, obviously, is to leverage our role in the center of the industry to get all the sides to a transaction to communicate with each other and to encourage STP.

@dtcc: And are you making progress toward this "hub" concept?

Wynn: We are. In the new OTC derivatives arena, for example, we've implemented a real-time reconciliation service that handled more than 840,000 payments in the second quarter alone with a 90+% match rate. The service has been growing at more than 50% each quarter. We're also working toward

ment Processing

By Jim Conmy

bilateral netting and managed settlement. Some of our customers have even suggested creating a sort of “trade warehouse” where the payments for all parties could be calculated centrally. So, if you look across our services and what activities we’re going to be doing in the next five years, this is the direction we’re going. This is why we’re moving more toward a “hub” notion, because we have the challenge of linking multiple issuers or payers to multiple payees.

@dtcc: Where do corporate actions fit into this concept?

Wynn: This is another key area of challenge for us, and it has a common theme involving payments, the multiplicity of standards and the growing diversity of asset classes. Years ago, no one could have imagined the volumes we see today – our Global Corporate Action Validation service handled more than 900,000 announcements last year – and the risks inherent in that. If a financial institution gets wrong information, it can process something wrong for 100,000 clients. The cost of a mistake can then be multiplied by 100,000. And no one could have imagined the side effects that have come from the globalization of the capital markets, even without cross-border trading. We used to have overseas companies and U.S. companies each in their own sphere. Now we have, say, a Japanese company that may take over another company in Australia and the transaction ends up as a corporate action that has to be processed for U.S. shareholders, as well as for all the shareholders in Asia and Australia.

@dtcc: What’s DTCC doing to address this?

Wynn: As we look at corporate actions, two key themes strike us. One is the announcement process, which has been expanding and altering and becoming

more diverse than it used to be. So one of the things we’re working on is a more explicit separation of corporate action announcements from the subsequent transaction processing. In the past we bundled this all together and, if we held your IBM stock in our depository, you’d get an announcement that you would receive a dividend, and then we provided you with payment of the dividend...and you had a kind of one-to-one correlation. We never charged for the announcement itself because it was part of the dividend transaction.



Janet Wynn

@dtcc: Are you planning to charge separately for the announcement service now?

Wynn: With the explosion in the kinds of corporate action announcements we handle, we’re finding that a large percent of our staff time is actually dedicated to the announcements themselves, as distinct from the subsequent transaction processing. So we’re moving to unbundle this service and improve the way it’s offered, with a more explicit recognition that there’s more heterogeneity of assets. And you’ll hear more about this.

@dtcc: You mentioned two trends in corporate actions. What’s the other?

Wynn: The second key aspect of corporate

actions is the quality of the announcement...how good or accurate it is...and is there an efficient way to receive it or respond to it? This is why we’ve created our Global Corporate Action Validation Service. We’ve recognized that we need to be dedicated to “at source” data that’s scrubbed once so that we’re not passing any faulty data down the long communications chain. That’s why we have three processing centers across the world with good local knowledge and the capacity to handle corporate actions in 16 languages. We’re also committed to improving the flow of elections from our customers using open communications standards that are universally accepted and support easy responses. If it’s a voluntary action, for example, we need to make it easy for our customers to respond with their elections or choices.

@dtcc: What’s the ultimate goal of all this?

Wynn: Our vision here is “the Golden Copy” of the announcement, where a credit event is gathered “at source,” double- or triple-checked and then loaded into the asset servicing hub or “trade warehouse.” From there it can be communicated both down and upstream to all the parties involved. This gives us a full circle and a complete cycle for asset servicing...for any type of asset. This is a long evolution from the very homogeneous service we used to offer to what were very homogeneous capital markets. It is a redefining of our traditional processes to reflect the need to offer the same very high level of service and quality for the increasingly heterogeneous and diverse parts of our industry. The markets are changing. We need to change how we service the markets. @

Intel Among First to go Paperless

Continued from page 4

for all markets, notified its bank and broker/dealer customers that the transfer of ownership on all Intel shares would result in the issuance of DRS statements, not paper certificates.

In the first half of 2005, according to DTCC Senior Product Manager Joe Trezza, the depository handled nearly 4,000 requests from Intel shareholders or their brokers for paper certificates following a transaction versus fewer than 100 requests for DRS statements. “Obviously, this is going to change, and it will affect our business as well,” he said.

“More than half of all public companies in the United States – including Intel and numerous other Fortune 500 companies – are incorporated in Delaware,” said Janet Wynn, DTCC’s managing director for Asset Services. “Consequently, Delaware’s

elimination of its requirement for paper certificates is likely to prompt many companies to switch to electronic share ownership. Intel is taking the lead.”

Since Delaware changed its law, two other states that also required companies to issue paper certificates – Missouri and Louisiana – have also revised their statutes. (See related article on page 4.)

Nearly 123,000 of Intel shareholders have physical stock certificates, compared with 4,289 whose ownership is electronically recorded through DRS. However, Stewart noted, most Intel stockholders hold their positions as beneficial owners via brokers – in other words, in “street name.” “So they’re unlikely to be directly affected by this,” he said.

More than 1,000 public issues are now

part of the book-entry DRS, and the number of investor accounts holding DRS securities is in the neighborhood of 38 million.

“We anticipate that many other public companies will also convert their share ownership to paperless electronic registration,” Wynn said. “It’s safer, cheaper and more convenient for investors than dealing with paper. It also seems appropriate that Intel be among the first companies to do this,” Wynn added, “because Intel’s computer chips help us manage paperless markets.”

Editor’s Note: For more information on dematerialization, send an email to nomorepaper@dtcc.com or contact Joe Trezza at 212 855 4400. @

FICC Sets New Processing Records

Continued from page 5

at the end of the second quarter and contributed to GSD’s record processing. GSD handled over 525 substitutions that day with a total market value of more than \$238 billion – a five-fold increase over a normal substitution day.

“Processing repo substitutions over a quarter end is no small matter, with little margin for error,” Ingber said. “In fact, this process impacts not only FICC participants but potentially the entire government securities market place.”

Regarding the reasons for the surge in EPN messages, Ingber said that this is attributable to continued investor demand for new mortgages and refinancings.

FICC’s netting service is a key benefit for GSD members. The service aggregates the offsetting of long and short positions from members’ daily trading activity, which, in turn, reduces the number of individual settlements, providing members with significant cost and operational benefits.

“Our netting service is a perfect example of how FICC leverages technology to help enhance growth in the government securities marketplace and in our customers’ businesses,” said Ed Leithead, GSD product manager. “The record value of

transactions settled by GSD clearly highlights the growth that is occurring in the industry and our expanding role in it.”

The same can be said of MBS’s EPN service and its latest processing record. The EPN service, which provides real-time pool notification for mortgage trades, has been a boon to the mortgage-backed securities marketplace, said Dennis Paganucci, managing director, MBS Product Management. By allowing buyers and sellers to transmit information quickly, efficiently, and reliably, EPN helps them reduce risk and streamline their operations by automating what used to be a highly manual, error-prone process that resulted in billions of dollars in mortgage transaction fails. Firms do not have to be members of MBS’s clearing services in order to take advantage of EPN.

“The market for mortgage-backed securities would not be as efficient as it has been these past few years were it not for EPN, nor would our customers be enjoying the same degree of success,” said Paganucci. “EPN has made a huge contribution to both, and we continue to upgrade its performance and capacity in anticipation of the industry’s and our customers’ future needs.” @

ISO 15022 Version *Continued from cover*

Mondas, N Tier, Vermeg, and CheckFree.

The GCA Validation Service provides a centralized source of “scrubbed” information about corporate actions, including tender offers, conversions, stock splits, and nearly 100 other types of events for equities and fixed-income instruments traded in Europe, Asia-Pacific and the Americas. The service delivers comprehensive, accurate and timely information, helping to reduce operational losses and optimize front-office trading. It is provided through Global Asset Solutions LLC, a DTCC subsidiary.

“The implementation of ISO 15022 addresses the growing interest among financial services firms worldwide for a central source of global corporate action announcements,” said James Femia, DTCC managing director and head of the Global Corporate Action business. “Our service centers in New York, London and Shanghai make the GCA Validation Service the most comprehensive corporate actions resource available in the global marketplace.”

“Many European and Asian firms use the ISO 15022 messaging format,” said Steven Cotton, DTCC’s GCA European Relationship Manager based in London. “Expanding access to the GCA Validation Service with 15022 will make it easier for

any firm – whether a bank, broker, investment manager, hedge fund or insurance company, no matter where they are located – to begin using the service. And by partnering with these corporate action solutions providers, we’re striving to give our customers the greatest level of flexibility in how they access the service.”

The ISO 15022 format is being offered in addition to the GCA Validation proprietary format, which is now used by a number of global customers of the service. “We also offer a real-time Web browser application for GCA Validation, making it easier for both front-office traders and back-office professionals to access GCA announcements from their desktops,” Cotton said.

GCA Validation

The GCA Validation Service created 900,000 announcement records in 2004, its first full year of operation. Close to 30% of these announcements involved securities outside the U.S. Last year, a custodian verification feature was also added to the service to further improve the quality of information and eliminate customers’ handling of custodian notifications. Today, the GCA Validation Service processes data from more than 80 custodians worldwide.



Steven Cotton

ISO 15022

ISO 15022 is a standard format for electronic messages exchanged among securities firms. It was developed by the International Organization for Standardisation, a network of the national standards institutes of 148 countries, and provides financial services firms worldwide with a common structure for electronic messages, thereby facilitating the automation of and reducing risks associated with securities processing, including corporate actions.

Editor’s Note: For more information on the GCA Validation Service, please visit www.dtcc.com/gca or contact Steven Cotton, DTCC’s GCA European Relationship Manager based in London at +44 (0)20 7444 0417. @

“Expanding access to the GCA Validation Service with 15022 will make it easier for any firm – whether a bank, broker, investment manager, hedge fund or insurance company, no matter where they are located – to begin using the service.”

Alternative Investments: Hedge Fund Evolution Speeds Up

By Nicholas Clarke

The first half of 2005 was a roller-coaster ride for alternative investments – hedge funds, managed futures, private equity/debt, and other nontraditional stock and bond instruments. As reported by hedge fund analyst CogentHedge, average returns were down in the first quarter but up in the second.

Despite the market's uneven performance, alternative assets, particularly hedge funds, retained their luster, with investors pumping more than \$38 billion into hedge funds globally in the past two quarters, as calculated by HedgeCo.net. Leading the surge were affluent individuals, endowments, insurance companies, and, increasingly, public pension plans.

According to the *Wall Street Journal*, during the last five years, assets managed by hedge funds have doubled to \$1 trillion as the number of funds has soared to 8,000. But as this investment class plays a bigger role in daily market moves, hedge

funds face several strategic issues that are reshaping the marketplace from a regulatory, compliance, and operations perspective.

- **Regulatory pressures.** One result of the rapid growth in hedge funds in the U.S. is increased scrutiny from the Securities and Exchange Commission (SEC), which now requires that certain fund managers register with the SEC as investment advisers under the Investment Advisers Act of 1940. The new SEC rule, due to go into effect February 1, 2006, applies to hedge funds larger than \$25 million and with more than 15 investors. Excluded from the rule are funds with lockups that prohibit investors from redeeming their money for two years or more. Currently, about a third of hedge fund managers are registered with the SEC, according to the Knowledge@Wharton newsletter, published by the Wharton School of the University of Pennsylvania.

- **Compliance and reporting.** Under the SEC rule, funds will be subject to regular audits and inspections and will have to provide details of their trading strategies and how they value their portfolios, among other requirements. That means they'll have to step up their compliance, and many are hiring chief compliance officers to handle that job. But it is not just the SEC driving this change. As pointed out in a recent report on hedge funds by KPMG, pension funds and other institutional investors are also behind it, drawn by what many of them see is a need for greater transparency in fund compliance and reporting.

- **Operational and risk control.** In addition to forcing greater transparency, institutional investors – especially pension funds – are changing how hedge

funds operate. Institutional investors want to know exactly what they are investing in. They have their own stringent controls that they must follow, and they are demanding that hedge funds do the same by maintaining reliable back-office operations and risk management procedures, according to Peter Hess, senior vice president of Advent Software, in a recent column he wrote for *Securities Industry News*. To maintain credibility with investors, said Hess, some hedge funds are allowing institutional investors to review their infrastructures – including the software used to monitor trading, as well as compliance and reporting processes – to meet more rigorous risk management objectives.

In late 2004, DTCC formed an Alternative Investment Products Advisory Committee that has since grown from the original 15 members to nearly 30 broker/dealer, fund and service provider firms. Charged with developing a standard, streamlined platform for processing and settling these investments, DTCC and the committee are working toward defining technology specifications necessary to launch a pilot program.

“Alternative investment products have very specialized characteristics and requirements,” explained Ann Bergin, managing director of DTCC's Distribution Services and head of the advisory committee. “The solution we are proposing will directly address the industry's very specific needs and correct large inefficiencies. By providing a model that leverages DTCC's vast experience in other securities' marketplaces, we can help the alternative investment community reach its full growth potential.” @



DTC Settlement and P&I Payments Hit Record Levels in June

By Justin Saper and Edward C. Kelleher

June was a big month for The Depository Trust Company (DTC), a DTCC subsidiary. Not only did DTC break records for settlement, it also set new standards for processing of principal and interest payments.

Settlement figures for DTC hit record levels this June for both the number of transactions processed and for the value of transactions processed.

On June 29, DTC processed a record 983,190 transactions, which was 7,000 more transactions processed than on the previous record day, November 16, 2004, when there were 975,807 transactions. The June 29 total included a record of more than 500,000 Institutional Delivery transactions. The average number of daily transactions for the first quarter of 2005 was 709,763.

“This settlement record was driven primarily by the rebalancing of the Russell Indices and the settlement of institutional trades,” said John Kiechle, vice president, Product Management at DTCC. “The rebalancing – in which brokers bought and sold securities to restore their original proportions in the various Russell portfolios – occurred on June 24 and settled on June 29.”

On the following day, June 30, DTC settled a record \$906.6 billion, surpassing a previous peak of \$876.6 billion reached on March 23, 2005. The average daily settlement for the first quarter of 2005 was \$698.7 billion. The settlement record was primarily due to money market maturity presentments, which set a record of their own, with \$223.1 billion in maturity presentments in one day, compared to a previous peak of \$206.3 billion reached May 17, 2000.

P & I Records

Principal, interest and reorganization

(P&I) payments processed by DTC hit record levels on June 15, 2005, totaling \$69.4 billion, the highest P&I allocation ever and the second record set in 2005.

Earlier in the year, P&I payments reached a record level of \$58.2 billion on April 25. The April figure was surpassed again on June 27 when P&I payments totaled \$59.5 billion, the second highest amount on record.

The payments included a record payout of \$38.3 billion in redemption proceeds, the most redemptions paid in a single day to date. Dividend and interest payments on corporate bonds, municipal bonds and collateralized mortgage obligations (CMOs) accounted for the rest.

“The last week of June topped off the entire month,” said Alan Hutton, managing director of the Southern Business Center. “Three factors converged to make the week beginning Monday, June 27, a memorable one. The 25th of every month represents a peak payable date for principal pay-downs of asset-backed securities. And because it fell on the weekend, the payment date moved to the next business day – Monday, June 27. Next, Thursday, June 30, marked the end of the second quarter, typically yet another peak payment date. And the week ended on July 1 is historically one of the largest payment dates on the year. The whole week saw DTC collect and allocate payments in excess of \$150 billion for nearly a quarter million corporate action events.”

Marcelo Mejia, DTCC director of P&I Cash Processing, said that while the actual figures for June 15 were a record, they did not surprise him, given similar figures seen in recent months.



“Historically, June is probably the highest peak payable month of the year,” he said. “In addition to regular monthly and quarterly income payments, June is a typical payment cycle for bonds. In retrospect, we were more surprised by the number of payments made on April 25, which I think prepared us for what we saw in June.”

A number of factors continue to contribute to the high volume of payments. One of them is that investors continue to take advantage of the attractive interest rates in the market, Mejia said.

“Since interest rates are relatively low, investors continue to either finance or refinance existing loans. This is particularly evident in the real estate market,” he said. “In the end, more financing results in more debt service by the industry and by extension, DTCC.” @

Insurance E-Learning Service Launched By John Celock

Customers of DTCC's Insurance Services will now be able to obtain information about services by letting their fingers do the walking.

On July 1, Insurance Services (IS) launched a new e-learning service on the training page of the DTCC Insurance Services Web site. This training program is initially being introduced for Commissions, but plans are in place to extend this offering to other IS services. Insurance Services' Commissions processing enables the electronic transmission of information regarding commissions and compensation from insurance carriers to distributors for annuity and life insurance products and also provides same-day money settlement.

"Our goal is to provide our customers with as much automated help as needed," said Randi Gordon, product manager in Insurance Services. "E-learning is a key part of that goal, as it allows customers, at their own convenience, to educate themselves on our services in a user-friendly, accessible online environment."

The Commissions e-learning course was developed with ease of use foremost in mind. Customers will be issued a user ID and password to access the e-learning section of the DTCC Insurance Services Web site and will then be prompted into the Commissions class. Once in the site, users will be able to follow graphic and text presentations of the material.

An audio feed accompanies the visual material to further explain the Commissions processing service. Screenshots are incorporated into the teaching format. The online course contains both a general overview of the entire system, and specific pages dedicated

to portions of the service.

E-learning is designed to enhance Insurance Service's customer support, Gordon noted. By allowing customers to easily obtain online information on processes, layouts and error codes, calls to IS support areas are reduced. Gordon said she expects that staff members will now dedicate more time to assisting customers with more complex issues and introducing new products and services.

In addition to allowing staff members to focus on more value-added customer collaboration, the e-learning service will help bring greater speed and efficiency to how a client accesses desired information on Insurance Services.

Anthony Pietanza, DTCC director for Implementation, explained that prior to offering e-learning, all inquiries needed to be handled via telephone or email, which could result in longer response times. With e-learning, Pietanza says customers will be able to find many routine answers a mouse click away.

The new e-learning course was demonstrated to over 150 customers attending Insurance Services annual user meeting in New York City earlier this summer. According to Gordon, feedback from attendees was extremely positive, and customers are excited to see additional products become available. Some long-time customers have mentioned that the new service will be an excellent tool to train their in-house operations staff, she said.

E-learning programs are currently being developed for other IS services. A program for Positions and Valuations is currently under review and should launch in the coming weeks. A course on the Insurance

Services ACATS/IPS product, dealing with the transfer of insurance assets from one brokerage account to another, is expected to launch in the fourth quarter of this year.

"With the advent of more e-learning courses in Insurance Services, we know customers will see enhancements to the level and quality of service DTCC provides," Pietanza said. "We

are excited to use technology this way and anticipate that many of our current and future customers will use our e-learning features moving forward."

Editor's Note: For more information on how to sign up for Insurance Services E-Learning Programs, please contact Randi Gordon at 212 855 5654 or Anthony Pietanza at 212 855 5682. The Web site for Insurance Services is insurance.dtcc.com. @



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