

DTCC Boosts Processing Capacity for Equity Clearance and Settlement by More Than 150%

by Michael Bellini

To keep ahead of transaction volumes that have been rising sharply over the past several years, DTCC has significantly increased the capacity of its mainframe database for equity processing. The system, called Trade Repository Processing (TRP), can now process at least 160 million sides per day. This 167% increase is nearly triple the previous [continued on page 2]

DTCC Partners with Citigroup to Launch Gateway for Managed Accounts

by Karen Clarke

DTCC announced plans to introduce a new service to centralize and streamline the processing of managed accounts on September 12. Citigroup Smith Barney's Consulting Group and Global Transaction Services, a business unit of Citigroup Corporate and Investment Banking, will partner with DTCC to launch the service, which is open to the entire managed accounts industry.

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Benefits of DTCC's Insourcing Project

DTCC Boosts Processing Capacity *Continued from cover*

capacity of 60 million sides.

What's more, the TRP can handle the additional volume within the same time frames, thanks to changes that make the system perform more efficiently. In addition, for current volumes, the upgrade allows DTCC to deliver certain participant reports, such as the Consolidated Trade Summary, up to 45 minutes earlier.

The redesign, which required no systems changes on the part of customers, went live August 11, following months of testing.

More horsepower and transparent, too

"Imagine retooling your car's engine so that, instead of going 60 miles per hour, it can now go 160 with better gas mileage," said Robert Yodice, DTCC director, Clearance and Settlement Group. "That's analogous to what we've done with the TRP."

The project to upgrade the TRP entailed a full-scale structural reconfiguration, yielding dramatic increases in capacity, performance and efficiency. "We recognized an opportunity to make significant improvements by reengineering several of the system's core processes, rather than simply enhancing them," Yodice said.

The redesign was transparent to the industry, leaving customers' systems unaffected and keeping all existing formats and procedures in place.

Ahead of the curve

The original TRP database, rolled out in 2003 with processing capacity of 60 million sides per day, handled the industry's steady volume increases without a blip.

But by 2005, DTCC decided it was time to expand the system's capacity. Peak processing volumes, which have been climbing steadily over the past several years, hit 36.5 million transactions in 2005. Through July of this year, the average number of transactions processed grew to 32.8 million per day, with peak days of more than 50 million transactions. This trend is attributable in part to the

industry's smaller trade sizes due to decimalization, algorithmic trading activity and the expansion of new trading platforms.

"The completion of this project ensures the industry is well ahead of the volume curve, and also has more than sufficient capacity to handle peak days," said Jacob Feuchtwanger, DTCC managing director, Information Services, who oversaw the project.



Jacob Feuchtwanger, DTCC managing director, Information Services

Full-court press

The TRP redesign began during the fourth quarter of 2005. "Having observed the system in operation since 2003, the staff was able to identify efficiencies that could be gained by re-engineering the database and some of the trade process components," said Al Gambale, DTCC vice president, Information Services. "We eliminated redundancies and expanded trade capacity by organizing the data more efficiently."

Concurrently, DTCC upgraded its risk database to accommodate higher volumes, as every incoming trade must be filtered through DTCC's risk assessment system. Database-specific system upgrades were implemented, as well as changes to the

application software, to improve the system's speed and efficiency. In addition, various processes in Risk Management's overnight cycle were eliminated to compress timeframes for processing.

DTCC completed initial testing of the system in May, and then followed up with tougher tests. These included stress testing up to three times the current peak-day trading volume, and running the new TRP database parallel with the existing system for eight weeks to ensure functionality.

Key changes

One major improvement is that the TRP has been restructured to index all incoming trades by settlement date. Yodice used the example of a file cabinet to explain how this works. "Now the system creates separate 'drawers' for all trades settling on specific dates, whereas before all incoming trades were lumped together," he said.

This pre-sorting feature means that now the TRP only has to access one day's settlement drawer, which streamlines netting and settlement by eliminating the need for the system to sift through all trades residing in the system every day. The indexing of trades up front also yielded another efficiency: the elimination of a separate database whose function was to net down the trades.

A new approach to the handling of trade records is an additional change. Now, only information necessary for netting and settlement is entered into the TRP system, which enables the system to run more efficiently by decreasing the size of each record received by almost 70%.

This also eliminates unnecessary redundancy between the TRP and Risk Management system, which retains all details of the trades in its historical database. Now the sole repository for this information will be Risk Management, which increased the capacity of the historical database as part of its systems upgrade. @

Certificates Get a Big Push Toward Retirement

by Edward C. Kelleher

The securities industry has dealt another blow to paper. In a change marking a watershed in the use of certificates in U.S. capital markets, companies that trade on the New York Stock Exchange (NYSE), NYSE Arca, Nasdaq and the American Stock Exchange will be required to offer DTCC's Direct Registration System (DRS), which enables investors to register ownership of their shares electronically with either the issuing company or its transfer agents.

The eventual goal is the elimination of paper certificates, whose use "has long been identified as an inefficient and risk-laden mechanism" for holding and transferring securities, according to the Securities and Exchange Commission (SEC).

The SEC approved the rule change after the four organizations requested earlier this year that DRS be made a listing requirement.

The timetable

Under the rule change, newly listed issues coming to market on or after January 1, 2007, will be required to be DRS-eligible on the first day of trading. Existing listed issues will have to become DRS-eligible by January 1, 2008.

DRS enables companies and investors to do away with paper certificates altogether. It provides for electronic direct registration of eligible securities in an investor's name on the books of a transfer agent or issuer, and allows transfer agents and brokers to transfer shares between each other electronically. Shares also can be held electronically in street name through a participant of The Depository Trust Company (DTC).

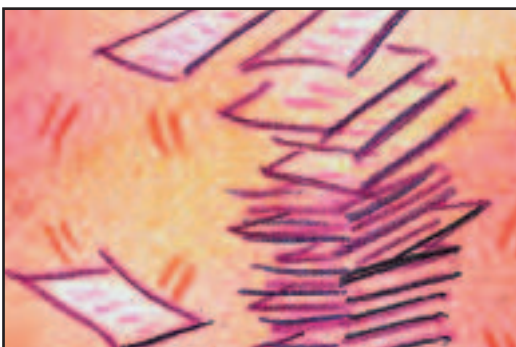
More efficiency; less risk

In approving the requirement, the SEC wrote that DRS should provide "more accurate, quicker and more cost-efficient

transfers; faster distribution of sale proceeds; reduced number of lost or stolen certificates and a reduction in the associated certificates replacement costs...."



Catherine R. Kinney, NYSE president and co-chief operating officer



Lawrence Morillo, managing director of Pershing LLC and chairman of the SIA's Operations Legal and Regulatory Committee

"The NYSE welcomes the SEC's approval of the Exchange rule change that will require listed companies to be eligible to participate in DTCC's DRS system," said Catherine R. Kinney, NYSE president and co-chief operating officer, who is also a DTCC director. "This rule change is another example of how the exchanges, DTCC and the securities industry continue to work closely together. Participation in DRS will provide public companies, their shareholders and the transfer agents with greater efficiencies and reduced costs in connection with securities processing," Kinney said.

"This is a major step in advancing the industry goal of dematerialization and the eventual elimination of paper certificates," said Donald F. Donahue, DTCC's president and CEO. "In addition to reducing costs, DRS gives investors greater security and greater flexibility in transferring or selling the securities."

The Securities Industry Association (SIA) estimates that the industry's cost for handling paper certificates each year is more than \$250 million, and that about 2 million certificates are lost each year, with a replacement cost of approximately \$50 million.

Spreading the word

"The ruling will get people to focus on DRS sooner rather than later," said Lawrence Morillo, managing director of Pershing LLC and chairman of the SIA's Operations Legal and Regulatory Committee, which has been pushing for the reduction and eventual elimination of physical securities certificates.

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Certificates Get a Big Push *Continued from page 3*

"I'm optimistic that investors will start choosing DRS and DRS statements once they learn the cost difference is significant – a statement may cost \$6 while a certificate may cost \$60 or more," said Morillo. "At Pershing, we're going to be pro-active with DRS and start to default to it when a security becomes DRS-eligible."

Educating the industry about DRS now becomes more important than ever. "We have to look at those issuers that have not moved yet on DRS," said Katie Sevcik, senior vice president and manager of operations for Wells Fargo Shareowner Services. "Even though DRS will become a listing requirement, it is anticipated that some companies may have to amend their bylaws and have the change approved at their annual meetings. There will need to be a more in-depth education effort for front-line brokerage firms and their investors, advising the investors about the benefits of both 'street' and DRS

ownership," Sevcik added. "Some investors are still asking for certificates because they think it's the only way they can move their shares." She said some transfer agents, and issuers that are their own transfer agents, will also need to be brought up to date on DRS, how it works and what its benefits are.



Katie Sevcik, senior vice president and manager of operations, Wells Fargo Shareowner Services

Choosing DRS

"More companies are electing to offer DRS each year because they know that savvy investors will choose to register their shares electronically," said Joseph Trezza, DTCC vice president, Asset Services.

The number of issues that are DRS-eligible has grown to 1,234 at present. Trezza said the new listing requirement will add approximately 10,000 issues by 2008, and potentially an additional 250 existing transfer agents will join the program. @



Going Certificateless – Globally

With the major exchanges and markets now requiring that all listing companies offer DTCC's Direct Registration System (DRS), the U.S. securities industry has taken a major step toward the elimination of paper stock certificates.

Industry officials applaud the move and say it will eventually lead to dematerialization – the elimination of all paper certificates in the U.S. market. "It's the closest we have come to going paperless for several years," said one industry official.

The U.S. is hardly leading the way in going certificateless, however. Instead it is following in the footsteps of more than two dozen countries that have already gone paperless.

"In Europe, Denmark and France went for electronic registration of securities more than 20 years ago and

many other European countries followed suit," said Joseph Trezza, DTCC vice president, Asset Services. In some countries, such as New Zealand, companies that insist on issuing paper certificates are prohibited from listing on exchanges.

Many other European markets no longer use paper securities, including Finland, Greece, Hungary, Iceland, Norway, Poland, Slovenia, Sweden, Switzerland and Ukraine. Ireland also is moving toward going paperless. In the Americas, Argentina and Mexico are paperless, and in Brazil, although companies can still issue paper securities, only one does.

Elsewhere around the world, leading markets that are paperless include Australia, China, India, Jordan, Malaysia, Pakistan, Singapore, South Africa and Sri Lanka.

DTCC Launches Enhancement to Help Mutual Funds Meet Regulatory Requirements on Market Timing

by Karen Gregory

DTCC launched a service enhancement on August 7 designed to help the mutual fund industry comply with an impending deadline under a new Securities and Exchange Commission (SEC) rule designed to combat short-term trading and market timing.

The SEC's Rule 22c-2, scheduled to take effect October 16, requires fund companies to create agreements with intermediaries in order to access shareholder data within omnibus accounts and evaluate trading patterns for possible market-timing activity.

Leveraging technology called Networking, which already exists within one of its key Mutual Fund Services, DTCC has developed a solution that will allow funds to more accurately track and record instances of frequent trading in omnibus accounts (a pool of individual accounts combined into one account, usually in the name of an intermediary firm), and then use that information to impose short-term redemption fees, if applicable.

What the service offers

Networking is provided by DTCC's subsidiary, National Securities Clearing Corporation (NSCC). It is used by the mutual fund industry to exchange and reconcile customer account-level activity between fund companies and broker/dealers and other distributors, and offers centralized settlement of cash dividends and capital gains distributions.

A new data stream in the service, created specifically to support the industry's compliance requirements, will provide fund companies with an automated, standardized and centralized method of requesting and receiving information through DTCC's secure and reliable infrastructure.

Called Networking for Standardized Data Reporting, the service enhancement allows fund companies to request, and distributors to transmit, information at two levels:

- **Summary level** for super omnibus accounts (comprising multiple plans, trusts and/or investor omnibus accounts). Data can include account numbers, dollar amounts and numbers of buys and sells.
- **Detail level**, where a fund company uses summary level data to request more specific information, such as details on shareholders in a 401(k) or retirement plan.

Ahead of the deadline

"With close collaboration from a working group of the

Investment Company Institute, we've been able to deliver a solution two months ahead of schedule and provide the industry with ample time to program and test prior to the SEC's October 16 deadline," said Barbara Simon, DTCC vice president, Relationship Management.

Kathy Joaquin, director of Operations & Distribution, Investment Company Institute, explained that the group cooperated on multiple levels. "While the working group provided guidance in dealing with the requirements of the SEC ruling, three additional task forces dealt specifically with key initiatives we identified as critical to the development and implementation of a solution – communications, guidelines and technical design."

Open to secondary intermediaries

Frequently, more than one firm exists in the intermediary chain, which can mean that the primary intermediary does not have the level of information that a secondary intermediary – a recordkeeper, for example – has.

For firms using Networking, the information can be passed automatically through the service. For firms in the chain that are not Networking participants, NSCC offers a Data Services Only (DSO) membership, which has fewer requirements than a full-service Networking membership, and allows for information-exchange only. In this case, a DSO member would be able to use Networking to pass information directly to the funds requesting it, or to their transfer agents. @



Gateway for Managed Accounts *Continued from cover*

Growing demand for managed accounts

Managed accounts have grown dramatically in recent years, with assets under management currently estimated at \$740 billion, compared to \$678 billion at the end of 2005. The industry is projected to reach \$1.5 trillion by 2011, spurred by an increasing number of high-net-worth households and a wave of baby boomers facing retirement who want customized investments and tax-sensitive portfolio management.

Citigroup Smith Barney's Consulting Group is the largest sponsor of managed accounts with nearly 30% of the market and an estimated \$200 billion in assets under management. Global Transaction Services is a leading provider of operations services to investment managers responsible for more than \$120 billion in separately managed accounts assets. The communication gateway will be offered through DTCC Solutions LLC, a subsidiary of DTCC.

"We are extremely pleased that the leading managed account sponsor and outsourcer have agreed to pilot this service with us,"

said Ann Bergin, DTCC managing director and general manager, Distribution Services. "The combination of Citigroup's leadership position in this market, coupled with our operational capabilities and infrastructure, will bring an unprecedented level of efficiency to this growing segment."

Partnership focus: premier client service

"Ultimately this is about growing the managed accounts industry and helping investors reach their goals," said Paul Hatch, managing director of Smith Barney's Consulting Group. "This service will enable Citigroup to leverage its leadership position as sponsor and outsourcer to help the industry deliver the full potential of managed accounts, while eliminating industry inefficiencies that seize the manager's focus at the expense of customization and premier client service."

"Our strategic partnership with DTCC solves an intractable problem associated with delivering efficient processing of separately managed accounts," said Neeraj Sahai, managing



director and global head of Securities and Fund Services for Citigroup Corporate and Investment Banking. “With Global Transaction Services’ translation platform, Smith Barney will be able to support industry standards for communicating account information through DTCC’s gateway, without costly reconfiguration of existing systems.”

“DTCC has a proven track record of delivering innovative solutions that have become the operational standards in other financial services markets,” Bergin said. “Our managed accounts service will provide the solid infrastructure and connectivity that will help the industry grow, through a network that is proven to be resilient, safe and secure.”

How the service will work

Managed accounts encompass a variety of financial instruments designed for high-net-worth investors that include separately managed accounts, multi-style portfolios and unified managed accounts, among others. Unlike mutual funds, where investors have an interest in a large pool of securities, a managed account holds the securities of just one investor. Investment managers offer individualized service and customized strategies tailored to the specific goals and needs of that investor.

DTCC’s managed account service will automate the process of opening new accounts as well as streamline the flow of information required to maintain various types of managed accounts – a process that is now highly manual – and increase efficiencies while reducing errors and operational risks.

The service will link managed account sponsors, investment managers and service providers, streamlining the multiple connections and disparate

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Neeraj Sahai, managing director and global head of Securities and Fund Services, Citigroup Corporate and Investment Banking

processes that now exist between parties. It will standardize the format and communication of critical information necessary to facilitate the account opening and maintenance of a broad variety of managed account products, including separately managed accounts, multi-style portfolios and unified managed accounts, through a single gateway.

DTCC’s managed account service is built with open architecture and message standards endorsed by industry leaders and the Money Management Institute. Standardized messages seamlessly flow through a central platform for account set-up, maintenance and reporting. The hub serves as a conduit for messages to be submitted, acknowledged, accepted or rejected.

The initial phase of the service will include messages with all the data points required to establish a new account. Account maintenance functions like the addition or subtraction of assets from an account and account termination notifications will also be available. Client profile updates can be made using standard messages to modify a client’s investment strategy, distributions or dozens of other changes. The second phase of the service will include messages to automate changes in restrictions, custodians, investment manager style, account fees and tax harvest requests.

The service is open to all industry participants, and can be accessed via the Internet or an existing DTCC secure connection. Messages are transmitted using XML, a highly recognized and flexible messaging format that can be used by a broad range of participants. Optional sponsor translation services will be available through Citigroup GTS. @

SEC Approves Rule Change Formalizing Procedures For OFAC Screening of Securities

by Michael Bellini

With the aim of reducing potential money laundering related to narcotics, terrorism and other prohibited activities, the Securities and Exchange Commission (SEC) recently approved a Depository Trust Company (DTC) rule change that will mandate certain procedures for DTC's Deposit, Custody and Withdrawal-by-Transfer services.

The changes are based on guidance from the Office of Foreign Assets Control (OFAC) of the U.S. Department of the Treasury.

What is required?

The aspect of the rule change that impacts participants pertains to deposits. It requires U.S. participants to certify to DTC that the current owners of certificates contained in each deposit have been screened against the OFAC lists of Specially Designated Nationals and Sanctioned Countries. The "party" the participant must screen is the individual in whose name the security is registered or, if the security has been assigned, the most recent assignee. Once DTC receives the U.S. participant's OFAC certification, it credits the participant's securities account with the depository.

In the case of deposits made by non-U.S. participants (which are not subject to U.S. regulations), DTC will perform the OFAC screening before crediting their accounts.

The rule changes also formalize DTC's internal OFAC screening program for Custody and Withdrawal-by-Transfer services. For these transactions, DTC screens the registration on the certificates being deposited and the registrations being requested for Withdrawal-by-Transfers against OFAC's lists.

"DTC has been conducting OFAC screenings since 2003 and continues to expand screening activities for products and services where DTC receives identity or ownership information," said Patrick Mapp, DTCC director, Office of Corporate and Regulatory Compliance.

Phase 1 for deposits: done

DTC is implementing the new OFAC certification procedures for deposits in two phases.

Phase 1, which took effect on August 7, 2006, applies to Deposit Automation Management (DAM) and restricted deposits created via the Participant Terminal System (PTS), a relatively small category of deposits. While this phase required no systems changes by participants, DTC needed to tweak its systems to facilitate full compliance.

Now, deposit-related PTS functions have an "OFAC certified" field, in which participants must enter a "Y" to confirm that they have screened the registration or most recent assignee for all certificates contained in each deposit and that there are no valid matches against the OFAC lists.

Phase 2 for deposits: Q4

Phase 2, scheduled for implementation in December 2006, is for deposits created through computer-to-computer facility (CCF) expectancy files transmitted to DTC. This change will require system enhancements by both participants and DTC. Since the beginning of 2006, DTC has published several Important Notices to keep participants apprised of the necessary preparations, the CCF file layout changes required and the implementation/testing timeframes.

The aspect of the rule change that impacts participants pertains to deposits. It requires U.S. participants to certify to DTC that the current owners of certificates contained in each deposit have been screened against the OFAC lists.

To accommodate this phase, DTC is enhancing and developing the relevant systems, functions and processes. "Phase 2 is more extensive due to the larger volume of transactions and systems changes required by all parties," said Thomas Joyce, DTCC director, Securities Processing. "Completing this phase formalizes the screening procedures to ensure both DTC and the industry are in full compliance with OFAC regulations."

Maintaining efficiency

The Anti-Money Laundering Committee of the Securities Industry Association (SIA) was instrumental in working with DTC to help shape the rule requirements, particularly the stipulation that only current owners of certificates being deposited undergo screening for certification.

"The recommendations by the SIA that were incorporated into the final rule change will help the industry ensure the screening process is swift and efficient, which will in turn allow DTC to preserve the same-day crediting of deposits that our participants have grown accustomed to," said Mapp.

DTC provides custody and asset servicing for more than 2.6 million securities issues from the United States and 100 other countries and territories, valued at \$31.2 trillion. @

Leveraging Synergies: How DTCC's Global Corporate Action Service Can Benefit Deriv/SERV Customers

by Steve Letzler

The growing popularity of equity derivatives (see article, page 12) underscores an important linkage between these instruments and corporate actions.

"Corporate action events, such as stock splits or extraordinary dividends, may impact an equity derivative through its effect on the underlying instrument," said Gina Ghent, DTCC vice president, Business Development. "A merger, for example, may cause a firm to cancel or change the terms of an equity derivative trade."

This relationship is why corporate action information is an essential part of post-trade processing of equity derivatives. "Whatever the impact, finding out the information is very important from a risk management perspective," said Ghent. "Firms expose themselves to various risks, from market to operational and legal risk, if they are not aware of a corporate action on an equity derivative's underlying instrument."

Sourcing the information

For firms trading equity derivatives, a key business consideration is where to obtain timely, accurate data on corporate actions.

One of the market's most reliable and comprehensive sources for this information is offered by DTCC via its Global Corporate Action (GCA) Validation Service. Voted "Best Corporate Actions Provider" in 2004 and 2005 by readers of *Waters* magazine on five continents, the service combines data from multiple vendors into a single, integrated and standardized information stream, covering almost 1.5 million securities from more than 150 countries.

In 2005, the GCA Validation Service handled 826,400 corporate action events. The GCA Validation Service is offered by DTCC Solutions LLC, a subsidiary of DTCC.

For front and back offices

While the GCA Validation Service offers broad coverage, it is tailored specifically to each client's needs. Firms specify the securities they want tracked and pay based on the securities being tracked.

Customers, including brokerage/banking firms such as JPMorgan Chase Securities and Merrill Lynch, are increasingly using the information not only for their back offices, but for their trading desks, as well.

This trend corresponds to the findings of a recent report issued by Oxera, an independent economics consultancy based in Europe, and sponsored by DTCC. The study noted that corporate actions can have a significant impact on trading prices, trading volume and trade price volatility.

"The Oxera report highlights the need for firms to make sure their trading desks have access to data on corporate actions in

order to execute proper trading strategies," said James Femia, DTCC managing director, Global Corporate Actions. "It also demonstrates that all organizations, especially buy-side firms, increasingly need accurate corporate actions information quickly throughout their operations."

Given the service's value for front offices, DTCC recently launched a marketing campaign targeting hedge funds and other buy-side firms.

More on the Oxera report

The Oxera study, which analyzed five different corporate action event types, found "strong



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Trade Information Warehouse: Testing, 1-2-3 by Lisa Argento

DTCC Deriv/SERV is on track with its rollout plan for the trade information warehouse, working closely with industry participants on issues such as testing, backloading and the introduction of subsequent deliverables.

The warehouse will provide a central trade database, maintaining the “official legal record” for all contracts eligible for automated Deriv/SERV confirmation, as well as basic economic information for other contracts. It will also provide a central processing capability to automate and standardize “downstream” processing of payments and other post-confirm events.

“Developing the warehouse has been a high priority for DTCC and its customers in the over-the-counter derivatives market since DTCC first announced its plans in February,” said Peter Axilrod, DTCC managing director, Business Development.

The warehouse will start out supporting credit derivatives, and then extend to other over-the-counter (OTC) derivatives products including rates, equities, FX and commodities – depending on market

demand and input from the Global Senior Oversight Group working with DTCC in guiding the initiative.

Populating the database

The testing of the warehouse’s functionality began September 18 and will continue through yearend. It is expected that users will complete their testing of core features during this period. In addition, backloading, which involves populating the warehouse database with trade data on existing contracts, will start in the coming month, and continue through 2007.

After successful testing, all new trades and post-trade events submitted to Deriv/SERV for electronic confirmation will automatically be loaded into the trade information warehouse.

The next phases, supporting payment calculation and payment settlement, will be released in 2007.

Like a depository

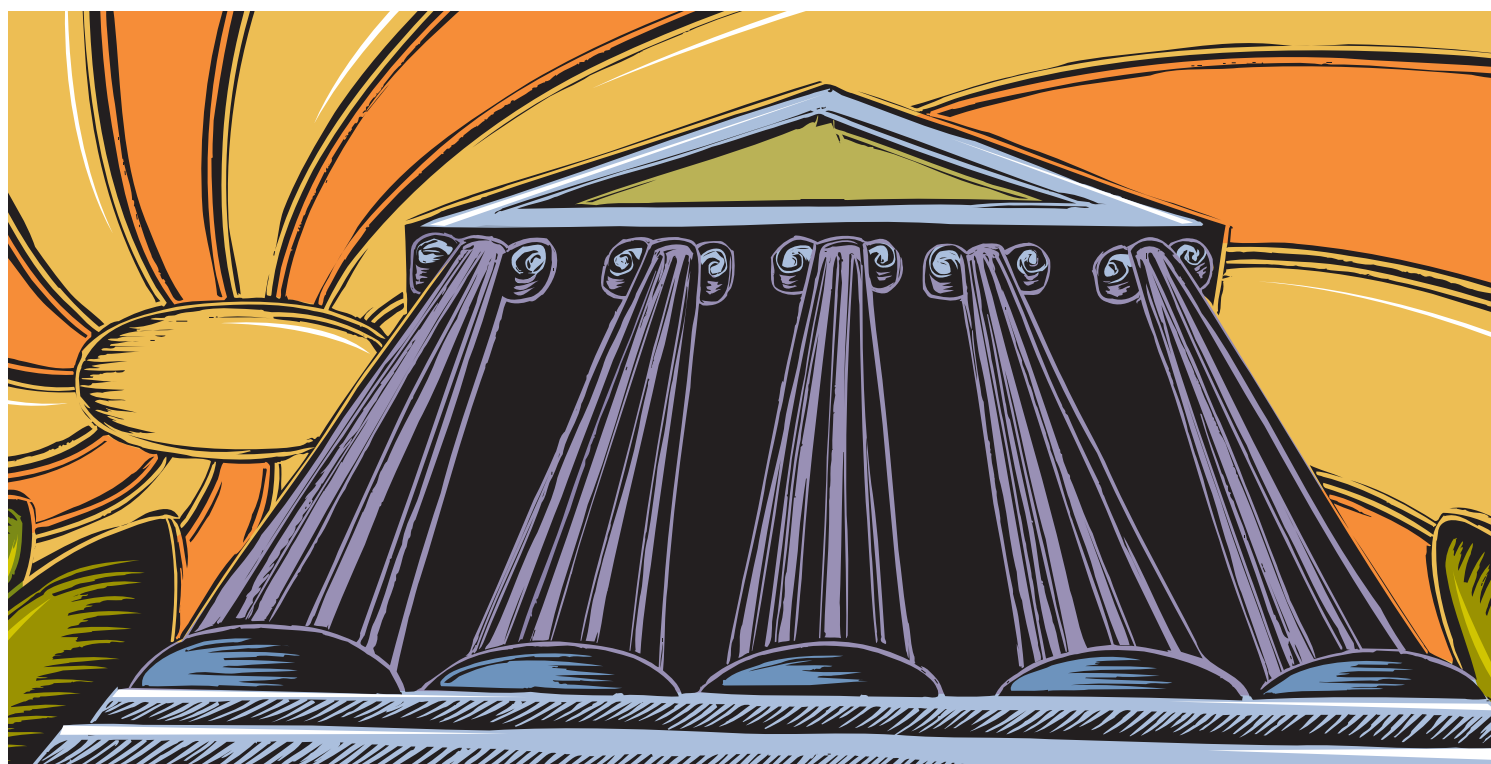
Janet Wynn, DTCC managing director and general manager, Deriv/SERV, said developing the warehouse is analogous to

starting up a central securities depository – without the vaults. “What we’re really building is an electronic industry utility to centrally store and safeguard contract information on OTC derivatives. And like a depository, we’re not simply maintaining the assets, we’re also going to keep track of changes and handle the servicing of the assets over their life.

“The idea is to leverage our role in the center of the industry by connecting market participants, while building on our experience running a depository and developing Deriv/SERV,” Wynn explained.

Since February, development work on the warehouse has been proceeding at an aggressive pace.

“We’ve had to understand our customers’ business requirements, determine the functions of the warehouse, design an operating model, set processing standards and build the underlying software platform,” said Axilrod. “And through it all, we’ve received invaluable guidance and input from a global team of senior experts from dealer and buy-side firms that has been working closely with us.” @



New Credit Derivatives Report Tracks Trends, Technologies and Costs

The processing cost per trade for a credit default swap (CDS) is projected to drop to \$190 by 2008 versus \$420 in 2006, a 55% decline, “and additional automation will continue to aid in lowering costs.”

This is according to a report titled “Shaking Up the Credit Derivatives Market: Profiling the Electronic Trading Platforms & Top Post-Trade Vendors,” published in July by the Aite Group, a research and advisory firm focused on the financial services industry.

Aite also anticipates that, despite sharply rising volumes, the industry’s aggregate CDS processing expenditures globally will peak in 2006 at about \$690 million and then begin to trend downward, falling to \$620 million in 2008.

Thanks to...

Technology is the reason for the dramatic turnaround in costs. “Increased investment in technology infrastructure, as well as ROI from technology investments, will reduce the trade capture, affirmation, confirmation, matching and settlement costs for CDSs over the next two years,” states the 50-page report.

While Aite projects that overall IT expenditures will continue increasing through 2008, the rate of growth in investment will slow significantly. For instance, the industry’s costs in 2006 are expected to rise 45% over 2005, reaching \$490 million, while 2008 costs are projected to grow 15% over 2007, to \$720 million.

More on expenditures

“The speed at which the credit derivatives market has grown has astonished many,” said Brad Bailey, senior analyst at

Aite Group and the report’s author.

“Trading has grown so quickly it’s put extraordinary pressure on firms to keep up with the pace. Both buy- and sell-side firms have increased their operations and technology spending significantly.”

And exactly how are the resources being allocated? “The essential areas where increased electronic trading and automated processing is taking place is broadly divided into three areas: the electronic point of trade; the electronic representation of documentation and providers of workflow handlers; and affirmation, confirmation, matching and settlement functions,” states Aite.

The report also notes that benefits of these outlays will go beyond cost reduction. “The increased use of electronic messaging, automated confirmation generation, affirmation at the point-of-trade and electronic matching will be large factors in not only lowering processing costs but minimizing operational risks and lowering costly and time-consuming errors.”



Brad Bailey, senior analyst, Aite Group

Who are the players?

In addition to analyzing processing and IT expenditures, Aite provides an overview of the major service providers and technologies for the electronic trading and automated processing of credit derivatives. The study includes brief descriptions of a handful of companies “with interesting offerings in the [continued on page 12]

Aite on Deriv/SERV

The de-facto matching service in the credit derivative world is DTCC’s Deriv/SERV,” states the Aite Group in its new report, titled “Shaking Up the Credit Derivatives Market: Profiling the Electronic Trading Platforms & Top Post-Trade Vendors.” DTCC features prominently in the report’s section on post-trade processing.

The Aite write-up includes a succinct overview of Deriv/SERV and its connectivity options. “Deriv/SERV is quickly evolving,” the report states. “It has met the challenges faced by the industry and has been aggressive in offering solutions.” The report also covers new developments, such as AffirmXpress and the Trade Information Warehouse.

“Vendors have built much of their value proposition around the evolution and success of DTCC Deriv/SERV,” says Aite. “As a result, many vendors are leveraging this effort and building solutions around connecting dealers and buy-side firms to the DTCC.”

Next Focus for Derivatives Automation

With the over-the-counter derivatives community making significant progress to improve operating efficiency for credit derivatives, market observers anticipate equity derivatives, another rapidly growing instrument, to be next on the automation agenda.

DTCC introduced equity derivatives to the Deriv/SERV platform in December 2004, following the successful launch of its automated matching and confirmation service for credit default swaps (CDS) the previous year.

"We are continuously enhancing the service to provide equity derivatives dealers and buy-side firms with a complete, robust platform that will enable them to increase automated processing of their transaction data," said Janet Wynn, DTCC general manager, DTCC Deriv/SERV.

Heightened focus on equities

To manage the expansion of Deriv/SERV's equity derivatives capability, DTCC has formed a dedicated team that will focus on meeting the market's expanding and evolving needs. Headed by Gina Ghent, DTCC vice president, Business Development, this team will include technology professionals, along with expanded relationship management, customer service and operational support.

"The equity derivative market is facing challenges similar to those faced by credit derivatives a few years ago, but equities have

their own distinct challenges due to the number of dynamic products and the geographic uniqueness related to the market," said Ghent. "The industry is now working with DTCC to automate equity derivatives to reduce unconfirmed trade backlogs and mitigate operational risk."

Wynn added, "We are following many of the same steps we took in building the CDS platform, but at a level much further up the learning curve."

Partnering with the industry

Wynn attributes DTCC's close collaboration with major dealers and buy-side firms in developing Deriv/SERV's capabilities for credit default swaps as an important element in the industry's rapid adoption of this service.

Now, to help guide the development of Deriv/SERV's equity service, DTCC has formed a working group that includes a number of dealer and buy-side firms. The group currently meets weekly to discuss industry needs, issues and action items related to fostering rapid adoption of electronic processing solutions.

Also planned is the creation of an Equity Derivatives Steering Committee, consisting of senior-level sell- and buy-side representatives, with a mandate to help guide the overall priorities and initiatives of the working group, and to provide input on implementation plans for the service.

New Credit Derivatives Report *Continued from page 11*

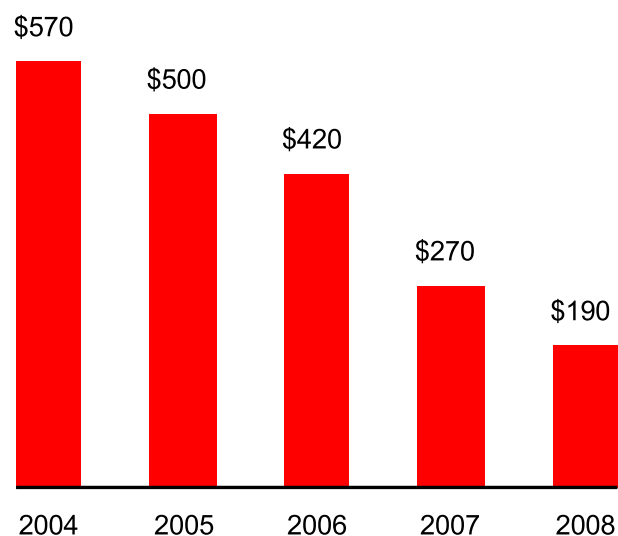
space, as well as several offerings that are scheduled to come to market before the end of the year."

The report concludes with a look ahead at the world of credit derivatives. Changes that the Aite Group anticipates in the coming 12 months include "significant consolidation in this space in the form of acquisition, strategic partnerships and mergers."

Aite also expects, "The growth in the prime brokerage of OTC derivative products and credit intermediation will drive prime brokers to offer solutions that ease workflow, build connectivity to electronic matching engines, and mitigate operational risk for their hedge fund client base." @

[To learn more about the Aite report, contact Frank Rizza at 617.338.6021. For more information on Aite, visit www.aitegroup.com.]

Credit Default Swaps Estimated Processing Cost per Trade



Source: Aite Group, LLC

Equities capabilities

When DTCC first introduced equities to the Deriv/SERV platform in 2004, it supported equity index and share options. Since then, the service has been extended to include swaps and variance swaps. It also accommodates relevant lifecycle events including new trades, full and partial terminations, increases, amendments and exits.

Going forward, DTCC plans to continue adding new equities products to the platform on a regular quarterly basis, starting with Asia Ex-Japan share and index options, scheduled for release by yearend. @

[For information on Deriv/SERV matching and confirmation for equity derivatives, contact Gina Ghent, DTCC vice president, Business Development at 212. 855.5624 or gghent@dtcc.com.]



Overview of Equity Derivatives

Growth in equity derivatives, such as options, swaps and variance swaps, has been strong, with the total notional value outstanding for equity derivatives more than doubling to \$5.5 trillion at the end of 2005 from \$2.4 trillion three years earlier, according to the International Swaps and Derivatives Association (ISDA®).*

Investors, such as pension funds, are increasingly adding these products to their portfolios to protect against market volatility. What's more, financial research firm Boston Consulting Group forecasts that investment banking revenue related to equity derivatives will reach \$20 billion this year compared to \$14 billion in 2004.

Like credit derivatives prior to concerted efforts to automate operational practices, equity derivatives processing is performed mostly through manual, paper-based methods, which are inherently prone to errors. According to the ISDA 2006 Operations Benchmarking Survey, equities, along with non-vanilla swaps and commodities, are the least automated product in the OTC derivatives market. The survey also noted that errors in trading non-vanilla equity derivatives more than doubled to 20% last year and that the level of unconfirmed trades and days' outstanding of such trades were also up.

The market for equities derivatives is multi-dimensional, according to Gina Ghent, DTCC vice president, Business Development, which means it requires greater attention and documentation efforts for both market participants and DTCC.

"ISDA has worked with the market to create general terms confirmations or Master Confirmation Agreements [MCA] for the various equity products and regions," said Ghent. "Once MCA execution occurs, market participants can then use Deriv/SERV's equity derivatives service to match the trade-specific details for each trade, and provide a quick and efficient means to execute confirmations."

*ISDA® is a trademark of the International Swaps and Derivatives Association.

Industry Reaps Benefits of DTCC's 'Ins

Sometimes “insourcing” pays off more than outsourcing. Until last year, two DTCC subsidiaries outsourced all their infrastructure support activities to the Securities Industry Automation Corporation (SIAC). Now, following the completion of a multi-year initiative, DTCC has cut costs and bolstered business continuity by insourcing the activities previously performed by SIAC into DTCC's infrastructure. The two subsidiaries are National Securities Clearing Corporation (NSCC) and Fixed Income Clearing Corporation (FICC).

The project, completed in late 2005, meets a continuity recommendation from the 2003 “Interagency Paper on Sound Practices to Strengthen the Resilience of the U.S. Financial System,” issued by the U.S. Federal Reserve Board, Office of the Comptroller of the Currency and the Securities and Exchange Commission (SEC).

Greater resiliency at a lower cost

Since SIAC's computer operations are both located in the metropolitan New York region, NSCC and FICC processing capabilities were at risk in the event of a New York-regional emergency. As a result, DTCC's insourcing of applications and network connections from SIAC has significantly strengthened the industry's business continuity by extending out-of-region backup capabilities to all DTCC subsidiaries, using DTCC's distant Remote Data Center facility.

The initiative has also reduced DTCC's overall costs, with millions of dollars in savings already accruing to customers.

Leveraging infrastructure

“Our primary goal with insourcing was to provide out-of-region data recovery for FICC and NSCC by leveraging the DTCC infrastructure,” said George Perretti, DTCC managing director, Corporate Business Continuity. He added that this was a major concern of the SEC, which closely monitored the initiative. “We gave the regulators ongoing status reports,” he noted.

On top of strengthening the industry's business continuity and infrastructure, the project is yielding financial benefits, enabling DTCC to cut the industry's overall operating expenses. In 2006, by leveraging DTCC's processing capabilities, insourcing has reduced DTCC's annual operating expenses an estimated \$42 million, said William Aimetti, DTCC's chief operating officer. This was one factor that enabled DTCC to lower its fees in 2006.

“By capitalizing on DTCC's existing infrastructure and equipment to support NSCC and FICC, we have been able to consolidate our systems, resulting in significant savings for both DTCC and the industry,” said Aimetti.

Two components of the project

The project, approved by DTCC's board in late 2002 and initiated in 2003, had two components.

The first entailed migrating from the SIAC data centers all mainframe and distributed applications for NSCC and FICC into the DTCC data centers, while taking advantage of its

infrastructure. The second component brought customers' network connections into DTCC as opposed to SIAC, thus providing direct connectivity to DTCC's out-of-region facilities.

Bringing in the apps

The strategy for insourcing the applications – approximately 100 in total – was to ensure the transition was seamless and transparent to customers, with no impact on processing.

“We built an environment in our data centers that mirrored the SIAC environment for FICC and NSCC,” said Perretti. “We also had a team dedicated to massaging the incoming applications to ensure they were running smoothly through our systems.”

In addition, DTCC took the opportunity to conduct a thorough review of all the applications being migrated. “We retired some of the legacy applications and replaced them with new ones,” said Perretti. “For example, we were in the process of rewriting the Continuous Net Settlement [CNS] system,” he noted. “Rather than insource the legacy CNS, we developed, tested and brought up the new CNS on our systems.”

What's more, DTCC ensured that the industry would benefit from the project as it progressed. “As we insourced the mainframe apps, we immediately took advantage of our out-of-region capability,” said Perretti.

The project's timeline called for the NSCC applications to come first, followed by those for FICC. According to Perretti, NSCC was completed in October 2004 and FICC in October 2005, both ahead of schedule.



George Perretti, DTCC managing director, Corporate Business Continuity

outsourcing' Project *by Helen Cunningham*

Onto the network

As the FICC applications were being migrated, DTCC simultaneously began insourcing the network connections, which would allow customers to connect directly with DTCC rather than sending their data to SIAC first.

To implement this piece of the project, DTCC collaborated closely with customers. "We worked with each firm to make the necessary changes to their systems for the new circuits," said Perretti. Noting that every customer had a cutover date, he added, "We could not have completed the network insourcing as quickly and efficiently as we did without the full cooperation of our customers."

This conversion was finished in late 2005, also ahead of schedule. Now, all NSCC and FICC data are transmitted directly to and from DTCC over DTCC's Securely Managed and Reliable Technology (SMART) network or SIAC's Secure Financial Transaction Infrastructure (SFTI) network, which is bridged to SMART.

What's ahead?

With the entire insourcing finished, DTCC is giving its consolidated network a review to identify opportunities for further cost savings and consolidation, according to Perretti. "For

example, we are looking at the number of circuits per customer and assessing with customers whether they can consolidate circuits to reduce their monthly expenses," he said. DTCC expects to complete these assessments in 2006 for all firms.

(Customers wishing to review their firms' configurations can contact their relationship managers.)

DTCC has already made recommendations for more than \$6 million in communications savings and, to date, \$3.3 million has been approved by customers and implemented.

Going forward, the centralization of DTCC applications and circuits within DTCC will also benefit the industry by providing a single point of contact for matters such as testing circuits, ordering services and continuity testing. @

On top of strengthening the industry's business continuity and infrastructure, the insourcing project is yielding financial benefits, enabling DTCC to cut the industry's overall operating expenses. In 2006, by leveraging DTCC's processing capabilities, insourcing has reduced DTCC's annual operating expenses an estimated \$42 million.

Reminder: Sign Up for the October Certification Exam

DTCC Learning will offer its certification exam for Asset Services on October 19. The exam covers the following services of DTCC's depository subsidiary, The Depository Trust Company: Custody, Deposits, Dividends, Reorganization and Withdrawals.

The test, comprising 84 multiple-choice questions, will be given at DTCC's New York headquarters and at the Southern Business Center in Tampa, Florida. DTCC will also offer it over the Internet for customers who meet all test condition requirements. The exam costs \$300 per person for first-time takers, \$125 per person for subsequent retesting.

For complete information about certification, visit the DTCC Learning Website at <http://learning.dtcc.com>, send an email to training_administrator@dtcc.com, or call 888.258.6393. @



Leveraging Synergies *Continued from page 9*

evidence that announcement dates of corporate actions often result in significant and systematic share price movements. The significance of the impact differs depending on the corporate action type.”

Oxera also found that, in general, the most significant price movement, volatility and volume changes occurred on the announcement day and in the immediate two or three days following the announcement.

“Potentially most important, these effects often emerge in a predictable manner around critical corporate action processing dates,” the report states. This means when firms disseminate corporate action information quickly and accurately throughout their operations, the front offices are direct beneficiaries because the data can help trading desks improve trading decisions and strategies.

(To obtain a free copy of the Oxera report, titled “Share prices and trading activity over the corporate action processing cycle,” visit DTCC’s Web site at www.dtcc.com/Publications/oxera2006.pdf.)

Checking with custodians

The GCA Validation Service also provides several unique features, including “custodian check.” This allows the custodians for the customer firm to feed their information on corporate actions events into the GCA feed on a private basis, so firms can compare that information to the validated composite record provided by the GCA Validation Service. Currently, about 85 custodian banks globally are connected to the service. @

[For additional information on DTCC’s GCA Validation Service, contact GCA Sales in New York at 212.855.4144, in London at +44 (0)20 7444 0403, or via email at gcainfo@dtcc.com.]



When it comes to trading, slow doesn't win the race

When you're trading, you need fast, accurate information on corporate actions to make the right decisions. In fact, according to a recent study by Oxera, a U.K. economics consultancy, such data is essential to take advantage of short-term trading opportunities caused by even routine corporate actions.

DTCC's Global Corporate Action Validation Service **collects and quickly distributes complete information on almost 1 million other corporate action events from more than 150 countries involving 1.5 million securities.** No one else offers broader, better global coverage.

Trading is tough enough even when you know what's going on. You need every advantage you can get.

For more information, contact DTCC Solutions LLC at gcainfo@dtcc.com or by phone at: **GCA Sales: New York** Phone: +1 212-855-4144

GCA Sales: London Phone: +44 (0)20 7444 0403

GCA Service Center:

Shanghai Phone: +(86 21) 3220-4710 x8021

For a free downloadable copy of the Oxera report, go to <http://www.dtcc.com/Publications/oxera2006.pdf>



DTCC's purpose is to help grow the world economy by furthering the development of low-cost, efficient capital.

DTCC's mission: By 2010, to be the acknowledged world-class provider of servicing solutions to financial markets through leadership, innovation, technology, risk management and strategic alliances.

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Stuart Z. Goldstein
Managing Director

Helen Cunningham
Editor

Troy Cavaliere
Design

Toni Bellise
Production Manager

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