



Rollout of the New Underwriting System Set for September

by Edward C. Kelleher

The countdown has begun. The industry is just two months away from full implementation of DTCC’s new underwriting platform, which will replace and consolidate the legacy systems that have been in place for decades, bringing major new efficiencies and straight-through processing benefits.

Called the Underwriting SOURCE (Securities Origination Underwriting & Reliable Corporate Actions Environment), [continued on page 6]

China Depository And DTCC Sign Agreement

by Steve Letzler

DTCC and the China Securities Depository and Clearing Corporation Limited (SD&C) signed a memorandum of understanding (MOU) on June 11 to foster an information exchange and cooperation on projects of interest.

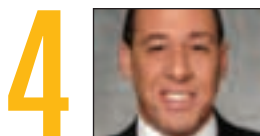
The agreement, signed in formal ceremonies in Beijing by SD&C Chairman Yaoxian Chen and DTCC Chairman Yaoxian Chen and DTCC Chairman-elect and Chief Executive Officer Donald F. Donahue, provides the legal and business framework for SD&C

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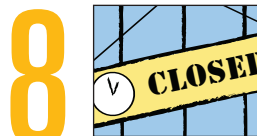
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Richard Macek Named Interim CEO for EuroCCP



Automation for Stock Loan Recalls



1 P.M. Deadline for Repo Collateral Substitutions

DTCC Names Interim CEO for EuroCCP

by Stuart Z. Goldstein

A leading DTCC senior executive, Richard Macek, has been chosen to serve as the interim chief executive officer (CEO) for EuroCCP, the new clearing and settlement platform that is being created to support the Turquoise pan-European trading platform.

Macek has been a member of DTCC's executive leadership team since the formation of DTCC in 1999, most recently as an executive managing director responsible for Risk Management, Finance and the firm's family of Wealth Management Services. He is also chairman of the board of Omgeo, a joint venture owned by DTCC and Thomson Financial.

Taking on a critical role

In taking on this critical leadership role for EuroCCP, Macek is relocating to London and relinquishing his current responsibilities for Finance, Risk Management and Wealth Management Services. He will, however, continue to serve as chairman of Omgeo.

"Rick is one of DTCC's most exper-

iented and knowledgeable executives," said Donald F. Donahue, DTCC chairman-elect and CEO. "He has more than 35 years of experience in financial services, focusing on finance and risk management issues. Rick was heavily involved in developing our proposal for Turquoise, and he has strong international experience through his chairmanship of Omgeo.

"During this start-up phase and launch of EuroCCP, Rick's appointment represents a significant commitment by DTCC to ensure the success of this new clearing corporation. We do plan, on a longer-term basis, to recruit a European executive to serve as the permanent CEO for this subsidiary," Donahue said.

Extensive industry experience

Macek was chief financial officer and managing director for DTCC from 1999 until April 2004. In 2003, he assumed the additional responsibility for all DTCC Risk Management activities, as well as being named CEO of DTCC's Fixed Income Clearing Corporation (FICC) subsidiary, which clears and settles U.S. government securities and mortgage-backed securities. In addition, he was named CEO of the Emerging Markets Clearing Corporation (EMCC), another DTCC subsidiary, in August 2003. Macek gave up the CEO positions at FICC and EMCC when he assumed the chairmanship of Omgeo in 2005.

Macek joined National Securities Clearing Corporation (NSCC) in 1998, prior to the formation of DTCC, as managing director, treasurer and chief financial officer. NSCC is now a DTCC subsidiary. He also was responsible for overseeing the financial operations of what was then known as the Government Securities



Richard Macek, interim CEO, EuroCCP

Clearing Corporation (GSCC) and Mortgage-Backed Securities Clearing Corporation (MBSCC), two organizations that later merged to form FICC.

Prior to joining NSCC, Macek had a 15-year career with Dillon, Read & Co., Inc., where he was managing director for the firm's finance and accounting operations in New York and London. Before that, he spent two years as a director with Morgan Stanley and 10 years with Arthur Young & Co. (now Ernst & Young) as an audit principal.

Macek, a certified public accountant, earned a bachelor's degree in business administration from Manhattan College. He served in the U.S. Army from 1969 to 1971 and was awarded the Bronze Star in Vietnam for meritorious service.

EuroCCP and Turquoise

EuroCCP was selected to provide clearing and settlement services to Turquoise, a consortium of seven major investment banks in Europe, after a major competition and is expected to begin operation at the end of this year. EuroCCP is a subsidiary of DTCC. The objective of Turquoise is the lower the costs of trading in Europe. @

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China Depository and DTCC Sign Agreement *Continued from cover*

and DTCC to work together and exchange information at both senior and staff levels.

This is the latest memorandum of understanding DTCC has signed with China, following one with the China Government Securities Depository and Clearing Corporation Limited (CDC) in December 2006.

'Bright perspectives'

"We're delighted to sign this agreement with SD&C to expand our relationships with key clearing and settlement organizations in China," said Donahue. "China is a country with dramatically increasing stock market participation, and as the financial industry becomes more and more a global business, China will play a major role. From our point of view, building relationships with organizations like SD&C will help us understand their

business better, and we hope we can assist in providing information to them from our perspective in the U.S."

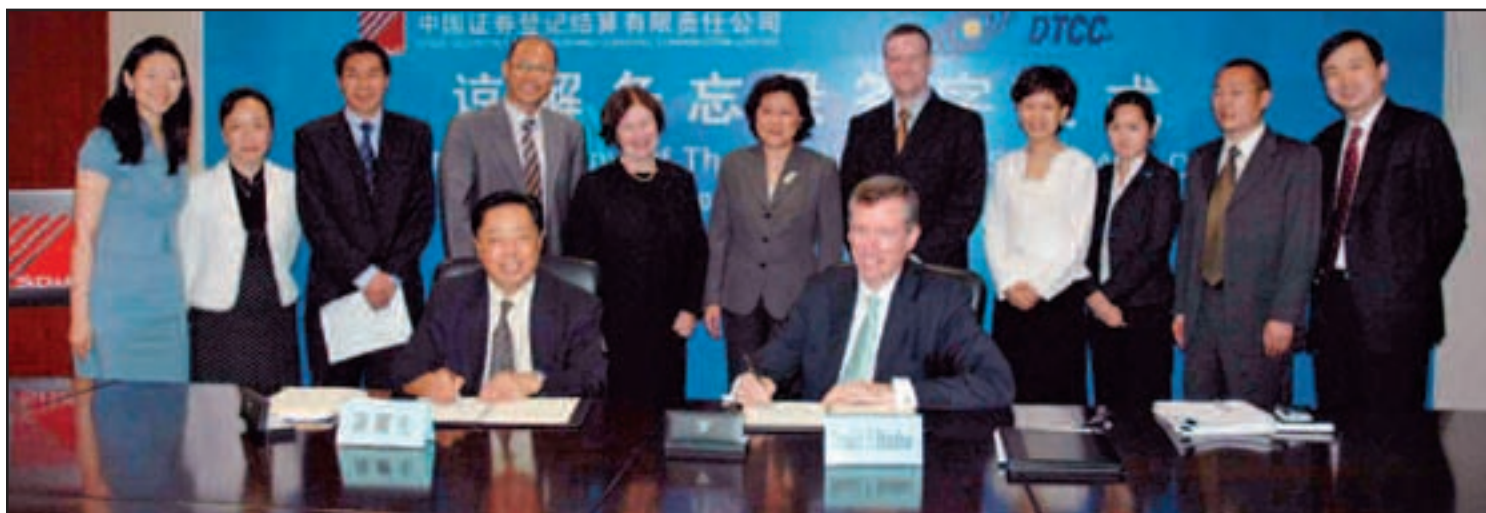
"DTCC and SD&C share the privilege of serving our respective capital markets industries, and both organizations have a common understanding of the importance of that role, which spurs the beginning of our cooperative relationship," said SD&C Vice Chairman and General Manager Madame Ying Jin. "SD&C firmly believes that we have bright perspectives and enormous cooperative opportunities regarding securities clearance, settlement and depository business and hopes that the signing of the MOU will promote our cooperative relationship.

"This MOU clearly defines the objective and purpose of our cooperation and establishes a formal channel of information

exchanges, which broadens the cooperative area in terms of business development and innovation. It is no doubt that the MOU will promote the initiatives regarding further practical cooperation and thus bring huge benefits to our industries," she said.

More on the MOU

Under the terms of the agreement, both sides will "establish a basis of cooperation in securities depository and clearing matters to help foster the prosperity of their financial markets, promote cross-border investment and explore opportunities for cooperation in both depository and clearing operations and in the establishment of an operation linkage." The pact also noted that the parties "anticipate developing a closer working relationship" in the future. @



SD&C Chairman Yaoxian Chen and DTCC Chairman-elect and Chief Executive Officer Donald F. Donahue sign the MOU in Beijing.

China Securities Depository and Clearing Corporation

The central registrar, the sole central counterparty and central securities depository of mainland China's securities exchange market, China Securities Depository and Clearing Corporation Limited (SD&C) was founded March 30, 2001, and is supervised by China Securities Regulatory Commission (CSRC).

SD&C's main functions include: establishment and management of securities accounts and settlement accounts; depository and transfer of ownership of securities; registration of the register of securities holders, as well as the registration of their rights and interests; clearing and settlement, as well as the relevant management of securities and funds; distribution of securities rights and interests as instructed by the issuer; providing inquiry, information, consultancy and training services relating to the securities registration and settlement business in accordance with the law; and undertaking of other business as approved by the CSRC.

Industry Gears Up for Automation of S

Here's another calendar entry for the industry: Sept. 30, 2007, is the securities lending community's target date for automating the transmission of stock loan recall messages. Although there is no regulatory mandate to meet this deadline, the firms that borrow and lend stocks have been working together, and with DTCC, to bring everyone on board to dispense with the existing paper-intensive process.

The service that delivers this capability, SMART/Track for Stock

Loan Recalls, is up and running, and in the coming months, firms will be taking the necessary steps to prepare for the transition.

"We're finally coming out of the dark ages," said Irving Klubeck, managing director, Pershing LLC and president of the Securities Industry Financial Markets Association's (SIFMA) Securities Lending Division. "Having an automated, auditable system for managing recalls will strengthen our ability to meet regulatory requirements and expedite the entire recall process,

A Primer on SMART/Track For Stock Loan Recalls

SMART/Track, rolled out in May 2003, represented something of a departure from The Depository Trust Company's traditional processing role in financial services, yet it was a natural fit.

"DTCC is uniquely positioned within the industry," said Margaret Koontz, DTCC director, Clearance and Settlement Product Management. "We have communications links with all the principal players in financial markets. SMART/Track leverages these connections to automate and streamline transmission of the messages that facilitate business among our customers."

No spaghetti, thanks

SMART/Track is an automated communications facility that centralizes communications among multiple parties, facilitating the notification, acknowledgement and maintenance of securities messages. These include notifications for stock loan recalls, as well as other transactions such as corporate action liability notices and buy-ins.

SMART/Track for Stock Loan Recalls automates the communications and notification process among parties, replacing faxes. This enables customers to create an audit trail indicating the information has been sent or received, which facilitates regulatory compliance and reduces market risk.

By providing a single point of entry for all customers, SMART/Track replaces the "spaghetti" environment of multiple connections to multiple parties. It also gives customers easy interoperability. In other words, a firm that has its own automated stock loan recall notification capability can communicate a recall with a counterparty that uses a third-party vendor or has its own recall notification capability via SMART/Track, and does not need to establish a direct link with each counterparty.

SMART/Track also establishes standards for communicating stock loan recall information so that all parties are speaking the same language through the use of ISO 15022 messaging formats.

Stock Loan Recalls

by Helen Cunningham

which translates into reduced financial exposure and lower costs.”

This industry initiative, which calls for the voluntary adoption of “automated recall management systems” (ARMS), is co-chaired by SIFMA’s Securities Lending Division and the Risk Management Association (RMA).

Why now?

A stock loan recall message is notification from a bank or broker/dealer that has lent securities to another firm that it is recalling the loan because it needs the position.

Although the Securities and Exchange Commission (SEC) requires firms to send notices of stock loan recalls, it has not mandated how those notices are sent. As a result, the industry has been making due with timeworn methods. “The last big change in this business was back in the late 1970s, when we moved from delivering recalls by hand to using faxes,” noted Klubeck. “Since then, the technology that has automated so many other industry segments has passed us by.”

The Depository Trust Company (DTC), a DTCC subsidiary, launched SMART/Track in May 2003 as a communications hub to handle a broad range of communications, including those for stock loan recalls. But industry uptake for stock loan recall automation was minimal.

“It’s a solution that requires an ‘everybody-into-the-pool’ approach,” explained Klubeck. “Broker/dealers were concerned that if they were the first to be automated, their higher level of efficiency could put them at the top of the lenders’ lists for recalls, so there was a natural resistance to becoming an early adopter of SMART/Track.”

Now, however, the securities lending community has joined forces to push for the voluntary elimination of manual processing in 2007. The change of heart is driven in part by heightened regulatory scrutiny of securities lending practices over the past several years, including Reg SHO, a set of rules adopted by the SEC in 2005 to address problems associated with failures to deliver.

“The current process is fraught with difficulties that delay the recall process, and this creates both regulatory and market risk,”

said Klubeck. “Automation via SMART/Track will help us better meet regulatory requirements for the timing of recalls and also provide proof of delivery. What’s more, the ability to turn around recalls more quickly will reduce costs, errors and market exposure, so it will make the entire process more reliable.”

Getting there

To meet the September deadline, a working group established by the RMA and SIFMA’s Securities Lending Division to focus on

the use of ARMS has planned three formal testing events beginning this June. The RMA and SIFMA will coordinate the testing, announcing details for the timetable and procedures. To participate, firms need to contact DTCC’s Participant Interface Planning group to establish connectivity to SMART/Track. (Call 888.382.2721, option 1, then option 3.)

“We pushed our target date to Sept. 30 to ensure everybody has sufficient time to be ready,” said Klubeck.

Customers have various options for connecting to the service. They can transmit the messages directly through DTCC, via their own systems or through a third-party vendor platform. Depending on

the method of connectivity, some programming work may be required for firms to go live with the service.

Testing the water

So, when it comes to automating stock loan recalls, is everybody ready to jump into the pool? “Let’s say everybody’s at the edge of the pool,” said Klubeck. “Testing over the summer will be the key.” @

[To participate in testing and establish connectivity to SMART/Track for Stock Loan Recalls, contact DTCC’s Participant Interface Planning group at 888.382.2721, option 1, then option 3. For more information about the service, contact Margaret Koontz, DTCC director, Clearance and Settlement Product Management, at mkoontz@dtcc.com or 212.855.5695 or Ashik Ramkalawon, DTCC manager, Clearance and Settlement Product Development, at aramkalawon@dtcc.com or 212.855.3558.]



Irving Klubeck, managing director, Pershing LLC and president of the Securities Industry Financial Markets Association’s (SIFMA) Securities Lending Division

Rollout of the New Underwriting System

Continued from cover

the system is scheduled to go into production for customers in early September. During July and August, a group of 25 customer firms and several information vendors will participate in a coordinated test of the new system.

Real-time information

The system will fundamentally streamline the process by which underwriters submit new-issue eligibility requests to The Depository Trust Company (DTC), a DTCC subsidiary. It also will introduce the New Issue Information Dissemination Service (NIIDS), a service that will disseminate information on new issues in real time to the industry. NIIDS was developed by DTC to help broker/dealers meet regulatory requirements for the prompt reporting of bond trades.

“Current notification practices on bond issues are decentralized and involve a variety of formats and manual processes including phone calls, faxes and emails,” said Denise Russo, DTCC director, Asset Services. “NIIDS will completely change this process, doing away with paper and moving the customer into real time.”

With NIIDS, underwriters will send new-issue information electronically to DTC, as well as any follow-up adjusted information. Once DTC has all the required reporting information, it will send the data to information vendors, dealers and other market participants so they can match, confirm and report trades in a timely and accurate fashion. DTC will distribute updates in a real-time electronic format until settlement day.

Reporting requirement

On January 1, 2008, it's anticipated that the Municipal Securities Rulemaking Board (MSRB) will issue a rule change requiring that, in most cases, municipal securities dealers report transactions to the MSRB within 15 minutes of the time of trade, compared to the current three-hour window.

“The launch of the underwriting system in early September will give our customers plenty of time to familiarize themselves with NIIDS and the anticipated MSRB requirements,” said Russo. “The NIIDS data

requirements will be optional in September when the new system goes live and will remain optional until the MSRB mandates that its member firms submit this data to DTC. We urge all municipal underwriting firms to begin submitting NIIDS data in September so they're ready to meet the MSRB mandate.”



Retiring old apps

All municipal underwriters must begin submitting new-issue eligibility requests through the new system in September. DTC will no longer accept hard-copy questionnaires or submission via the Participant Terminal System's PUND application or the Web application, WUN, said Russo.

All firms involved in the new-issue process – DTC customer underwriters, correspondent underwriters, clearing firms and custodian banks – must be registered with DTC for the new underwriting system in order to submit a new issue for DTC eligibility or, in the case of clearing firms and custodian banks, to approve a new issue submitted by a correspondent. @

[For more information on the new underwriting system, visit www.dtcc.com/reengineering or contact Denise Russo at drusso@dtcc.com or 212.855.3731.]

Corporate Underwriters Also Can Go Live in September

In addition to handling municipal bonds, the New Issue Information Dissemination Service (NIIDS) will be expanded to automate the collection and distribution of information on securities including corporate bonds, asset-backed securities and other fixed-income securities.

Like municipal underwriters, corporate underwriters can begin using the new underwriting system in September, but it is not immediately mandatory. Current functionality used by corporate underwriters – PUND, a PTS application, and WUN, a Web application – will be turned off for corporate issues on Oct. 1. At that time, corporate firms will have an option to begin using the new system or to continue submitting the paper eligibility form (the underwriting questionnaire). Firms will be able to use the paper questionnaire through Dec. 31, 2007. Beginning in January 2008, all requests for eligibility must be made in an automated format.

“Even though it is not anticipated that corporate underwriters will be required to use the new underwriting system until Jan. 1, 2008, they have the opportunity to acquaint themselves with the system and distribute information via NIIDS sooner if they choose to,” said Denise Russo, DTCC director, Asset Services.

DTCC Announces First-Time Fee Reduction For Insurance Services

by Karen Gregory

DTCC's Insurance Services business announced on May 21 the first fee reduction in its history, reflecting growing usage of its services. Insurance Services automates linkages and data exchange between carriers and their broker/dealer, bank and other distributor partners that market insurance products.

"Working in collaboration with the insurance industry, we have been able to bring the benefits of cost efficiency back to our clients," said John Ziambras, DTCC managing director and general manager, Insurance Services. "With volumes rising, we expect to further drive down costs and pass those savings along to our customers in the form of future fee reductions."

Ziambras added that the fee reduction is part of DTCC's at-cost business model, which requires a continual reassessment and "right-sizing" of fees to ensure full cost recovery and to then return excess revenues to customers as volumes grow.

\$2 million in customer savings

The fee reduction affects Positions & Valuations, Insurance Services' most heavily used service, and it is effective July 1, 2007. DTCC expects the fee reduction to save the insurance industry in excess of \$2 million during the first 12 months.

The reduction follows Insurance Services' record year of performance supporting the annuity and life insurance market, with volume for this service alone reaching 2.7 billion transactions in 2006, an 18% increase over 2005 and a 50% increase over 2004.

Positions & Valuations automates and standardizes the

transmission of annuity and life insurance contract details from carriers to distributors. It provides them with information on all assets under their management, including key contract data, current values, service features and parties to a contract. It is also used as a tool by the industry to comply with regulatory requirements, such as anti-money laundering and "Know Your Customer" statutes.

Customers respond

Jonnie Smith, senior vice president of Annuity Operations & Administration, John Hancock Financial Services, said, "John Hancock's annuities and life insurance businesses have increased dramatically in recent years. Therefore, reducing the fees for Positions & Valuations allows our firm to take advantage of the scale we enjoy today. When the industry set out to automate annuity and insurance processing, DTCC committed to lowering overall costs through its centralized technology infrastructure. They are delivering on that commitment, and we are very pleased with their decision."

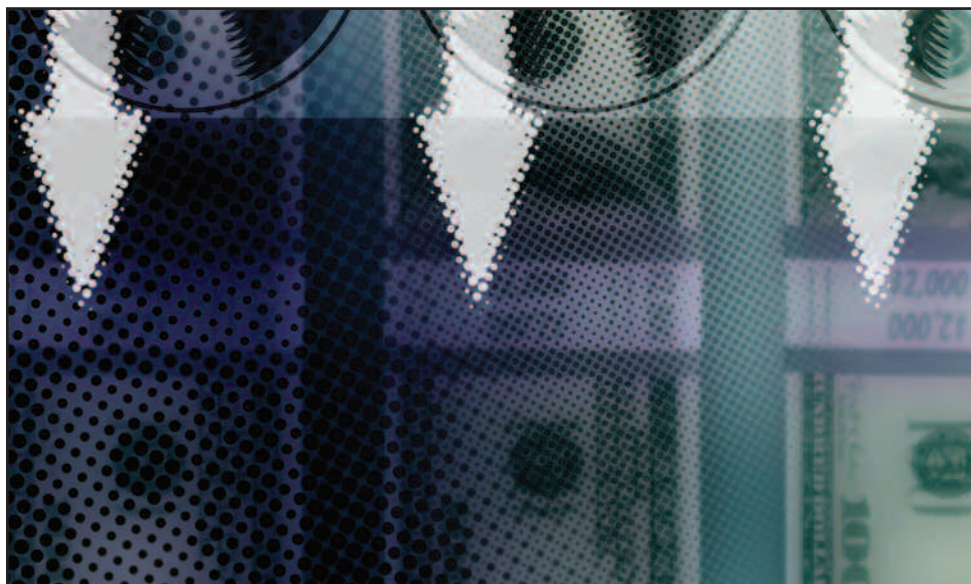
John Hancock is the U.S. division of Manulife Financial Corporation.

"Ten years ago the industry engaged DTCC to mainstream insurance processing due to its history of containing and reducing costs over time; this fee reduction affirms we made the right decision," commented Esther Stearns, president and chief operating officer, LPL Financial Services. "LPL continues to expand its utilization of Positions & Valuations, and this substantiates our commitment to automate the transfer of post-trade information to advance industry efficiency."

Usage-based fees

The fees for Positions & Valuations are based on levels of usage and calculated for every 1,000 transactions:

- For 4 million and over, the new fee will be \$2.00 vs. \$3.50, a 43 % decrease.
- For 2 million to 4 million, the new fee will be \$3.00 vs. \$3.75, a 20% decrease.
- For 500,000 to 2 million, the new fee will be \$4.00 vs. \$4.50, an 11% decrease.
- Transactions under 500,000 remain at \$8.00. @



FICC Sets 1 P.M. Deadline for Repo Collateral Substitutions

by James Conmy

As of Monday, June 4, Fixed Income Clearing Corporation's (FICC) window for repo collateral substitutions firmly closes each day at 1 p.m. Eastern time. Any substitution requests coming in after that are not processed until the next business day.

FICC established this deadline, or "hard close" in industry parlance, following more than two years of changes to collateral substitution procedures based on discussions with an industry working group and increased automation by FICC's Government Securities Division. The Securities and Exchange Commission (SEC) approved the change in April.

"Setting a strict deadline for submitting repo collateral substitutions marks the culmination of a multiyear initiative to reduce risk and cost in this market by standardizing and automating the substitution request process," said David Cosgrove, DTCC vice president, Operations.

A half-hour gain

The deadline for substitution requests under previous rules was 12:30 p.m. FICC processed substitution requests or replacement collateral that came in later, but firms had to pay a penalty fee and FICC worked only on a "good-faith basis," meaning it could not guarantee completion of the transaction.

Under the new SEC-approved deadline of 1 p.m. that took effect June 4, firms can still submit late substitution requests or new collateral specifications after FICC's 12:30 p.m. closing, but only for another half-an-hour and only with the understanding that FICC will process the request on a "good-faith basis." Any request that comes in after 1 p.m. will have to wait until the next day.

An exception to the rule will accommodate order flow when the Securities Industry and Financial Markets Association designates a "high-volume" day, such as the end of a quarter or a Treasury refunding. On these days, FICC will extend the 1 p.m. deadline by one hour to 2 p.m.

Growing volumes

Since the early 1990s, the U.S. market for repurchase agreements, or repos, has been averaging growth of more than

15% a year, according to a study by Celent, a financial research firm. Currently, outstanding term repo trades run to as much as \$2.7 trillion a day. In this large and growing market, swapping the collateral behind a repo – usually for a security of equivalent value – has emerged as a common industry practice.

In the past, FICC routinely processed most substitution requests manually. However, in recent years, the sharp climb in the number of substitutions has underscored the need to establish industry-wide procedures and automation.

What makes the substitution process somewhat complicated is that 9 out of 10 term repo trades coming into FICC for clearance and netting are "blind-brokered." Because the dealers speak only

to the inter-dealer broker and not to each other, they don't know who the other side of the trade is. As a result, collateral substitution requests all have to be coordinated through the broker, and then that information must be provided to FICC for processing. This often led to situations in which the original and substitute collateral flowed into FICC's clearing banks from dealers before the broker even had a chance to post a substitution request.

Quarterly spikes

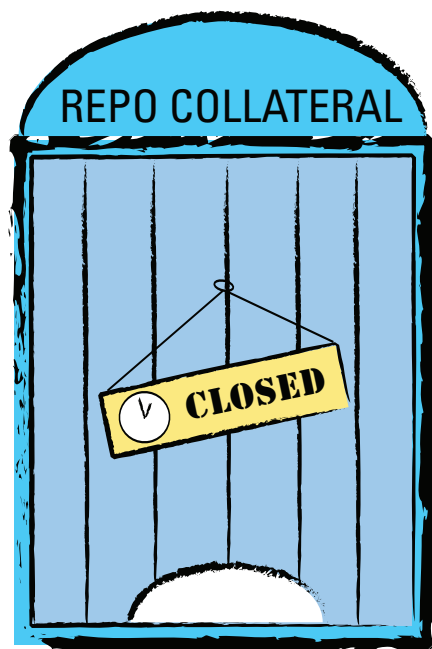
Substitution needs tend to climb at the end of each quarter when term repo transactions settle or firms recall securities they need to allocate to newly starting term repos. In mid-2004, when the end of the quarter coincided

with a hike in interest rates, so many substitution requests remained unprocessed at its participants that FICC requested an extension of the Fedwire closing time to process all outstanding requests and reduce the potential loans that could have been incurred by the Street.

At that point, FICC set about to automate its substitution process internally so requests could be processed electronically. The company also began discussions with dealers and inter-dealer brokers on ways to coordinate their still largely manual substitution requests with FICC's new automated process.

Steady progress

Today, FICC can process thousands of substitutions electronically within a short time frame. What's more, a reworking



of the timetable last spring breaks the whole substitution process into separate, more manageable pieces. Brokers now have more time to give FICC notice that a substitution is planned, and a notice automatically queues up other steps so that FICC and its banks will be prepared to handle the new collateral.

In an innovative step to remove risk and streamline the process even more, FICC now automatically instructs its bank to receive the original collateral and deliver it back to the dealer as soon as a substitution request comes in. At the same time, FICC substitutes general collateral for any replacement allocations that may not arrive in time.

"This allows us to keep the repo contract in force because there is a generic CUSIP in place as collateral to support the contract until we get the actual substitute collateral," Cosgrove said.

No more penalties

Now FICC is further strengthening this market's processing environment by extending the deadline by one-half-hour and making it mandatory for firms to submit their requests by 1 p.m. No longer will they have the option to pay a penalty for FICC to handle the substitution.

"Because this was a manual process for so many years," Cosgrove said, "some participants still want to come in after the deadline with the expectation that we can accommodate their requests. But now that we have completely automated the process, it is no longer possible to do it manually, penalty or not. The result is a more streamlined and secure market for collateral substitutions." @

[To learn more, contact Bart Schiavo at bschiavo@dtcc.com or 212.855.7590.]

New Report Projects Technology Spending for OTC Derivatives

by Judy Inosanto

Investment in technology solutions to support the global over-the-counter (OTC) derivatives market is expected to grow 5.5% annually, reaching \$232.5 million by 2011, according to Celent, a leading financial industry research and advisory firm.

In its recent report, "OTC Derivatives: The Post-Trade Landscape for Hedge Funds and Asset Managers," Celent anticipates that market participants will increase technology spending as they look to improve operational practices and better manage risk in a market where growth is outpacing capacity.

The 32-page report also assesses the current environment of the OTC derivatives market, the trends shaping its growth and the evolution in the technology being offered to market participants. In addition, it provides a description of the overall derivatives trade process.

Who's spending?

Nearly 64% of the spending on third-party technology solutions comes from the dealer community, observes Celent. While the larger and most active asset managers

and hedge funds are also making significant investments in automation, spending by buy-side firms has lagged.

Given the nascent stage of technology in the marketplace, the report notes it is likely that the buy-side is waiting for further advancements in automated service offerings. In addition, because the buy-side is generally more resource-constrained when it comes to technology investment, these firms are more apt to purchase services that enable them to manage a wide range of derivatives products on a single platform.

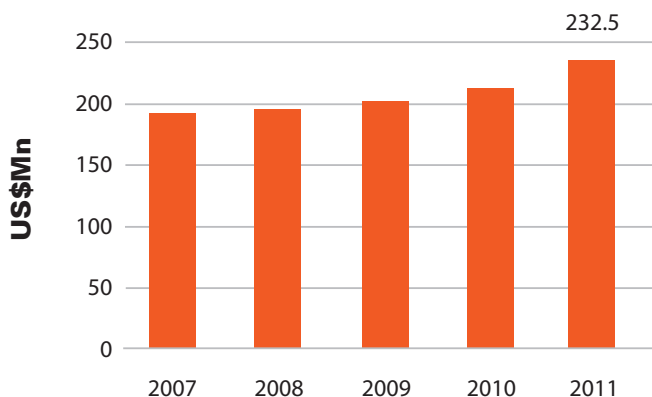
Toward 'a win for all'

"The challenge for money managers and broker-dealers is to automate processing," writes Celent. "Potentially, the next five years will be a new era of collaboration, technological creation and an amazing race where the finish line is a win for all."

The report estimates that less than 50% of OTC derivatives processing is automated and that up to 80% of trade confirmations contain errors. As the market becomes more mainstream, with a significant portion involving cross-border trading, the costs of these errors and the

[continued on page 10]

Global Technology Spend OTC Derivatives Processing, Post-trade/Pre-settlement



SOURCE: CELENT

Technology Spending for OTC Derivatives

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need to rebook or amend trade details remain concerns for the industry and global regulators.

Progress is well underway, notes Celent, particularly in the market for credit derivatives, where more than 80% of trades are now confirmed electronically and the total number of confirmations outstanding has been reduced by 70%. According to the International Swaps & Derivatives Association, by yearend-2006, 70% of credit derivatives confirmations were being sent out by T+1, up from 50% the year prior.

Setting aggressive goals

Celent sees the industry setting tough goals, extending automation to a more comprehensive list of instruments, with OTC equity derivatives garnering the greatest attention. The focus on equities is particularly evident following the global derivatives dealers' March 2007 letter to the Federal Reserve Bank of New York outlining their strategy and affirming their commitment to increase adoption of electronic processing in the equity space.

In addition, the industry aims to issue confirmations by T+1 and to complete confirmations by T+5 for "vanilla" products processed electronically, according to the report. For more complex products, the industry aims to issue confirmations by T+1 and have them completed by T+30.

'On the heels of success'

Moving forward, Celent sees the OTC derivatives community continuing to cope with its growth boom and the need for standards among the growing list of participants in the marketplace. "The key drivers to change are the broker/dealer community, organizations like ISDA, DTCC Deriv/SERV and the regulatory agencies, as well as very large traditional asset managers and hedge funds. It's a

collaborative effort that will take time but is launched on the heels of success in credit derivatives."

Celent also anticipates that the technology options in the marketplace will continue to grow rapidly. "The sector is a long way off from commoditization; regulators are collaborating globally; and the brokerage community is determined to make the pain go away." @

[For more information on Celent's report, visit www.celent.com.]

Celent on the Warehouse

Here's what the Celent report says about DTCC's Trade Information Warehouse, an extension of Deriv/SERV that provides a centralized and secure global infrastructure for processing over-the-counter derivatives over their lifecycle.

"An important global initiative launched in November 2006 by Deriv/SERV is the central Trade Information Warehouse, currently underway for credit derivatives. Deriv/SERV estimates it is receiving 80-85% of the credit derivative confirms. The project launched with credit derivatives because of the success Deriv/SERV experienced in broad dealer use for confirmations. DTCC hopes the central repository will ultimately become the 'golden copy' for all derivatives trades.

"Currently, broker-dealers have entered the second phase of the project, which entails back loading trades by broker-dealers and buy-side firms. This phase will likely take the balance of 2007. When completed, it will further support the ongoing bilateral administration and automation.

"Deriv/SERV clients include 800 buy-side firms, of which DTCC estimates there are 550-600 hedge funds. There is no cost to the buy-side."

Now on Screen: How DTCC Manages Liquidity Pressure

by Helen Cunningham

DTCC's risk management infrastructure includes regular outreach to customers to keep them informed about the organization's procedures and controls for handling potential market disruptions such as the 2003 blackout and 9/11, as well as insolvencies by member firms.

As part of this ongoing effort, DTCC recently produced a new Webcast that provides an overview of how The Depository Trust Company (DTC) and National Securities Clearing Corporation (NSCC) subsidiaries manage liquidity pressure. The presentation, which is being sent to customers via an email link, includes recommended best practices for firms to monitor their own liquidity.

Building knowledge

Over the past several years, DTCC has made presentations to various customers and regulators about the risk management procedures that protect the organization and the industry in emergency situations, including the possible inability of one or more firms to meet their settlement obligations.

"Post-9/11, we realized that many of our customers were not familiar with DTC's mechanisms and controls for handling the liquidity problems that could arise in emergencies," said Cheryl Lambert, DTCC managing director. "To address this knowledge gap, we created a presentation that described the depository's multi-layered plan for ensuring the markets have sufficient liquidity to complete settlement each business day, and we took it on the road."

In 2006, the Federal Reserve Bank of New York asked DTCC to formalize and expand the presentation to include NSCC, making it available to all DTC and NSCC member firms. The result is a new high-level Webcast, whose target audience consists of chief financial officers and executives who head the risk and operations areas of their firms.



"Both DTCC and regulators want to create wider understanding within the industry of how we manage potential liquidity pressure and the repercussions these events could have on both the financial system and member firms," said Douglas George, who recently joined DTCC from Citi in the newly created position of chief risk officer and managing director. "In addition to educating customers about DTCC's risk management procedures, we hope the Webcast will serve as a catalyst for firms to assess their own planning for possible liquidity crunches."

Sneak preview

To provide easy access to this educational piece, DTCC will be sending an email to firms this month, outlining the Webcast's purpose and providing a link for opening it.

The Webcast takes about 15 to 20 minutes to view. It begins by defining liquidity pressure, and is organized into separate sections on DTC and NSCC that outline the various risk management controls for the respective subsidiaries. (Future versions are expected to include DTCC's other subsidiaries.)

For instance, the DTC section gives a concise definition of the Participants Fund and its role in risk mitigation. ("If a participant fails to settle for any reason, the all-cash Participants Fund provides immediate liquidity to complete settlement without the need to draw down DTC lines of credit in most cases.")

The NSCC section includes a similar description of the Clearing Fund. ("NSCC functions as a central counterparty and calculates a Clearing Fund amount for each member every business day. If a member firm has a Clearing Fund deficit, these funds are due in to NSCC in the early morning.")

The presentation also includes several scenarios, ranging from a small insolvency to a possible catastrophic event, and describes how DTCC would manage these events from a liquidity point of view. For example, one scenario examines a failing DTC participant that has an end-of-day settlement obligation of \$600 million.

The Webcast concludes with recommended best practices for firms to monitor potential liquidity problems.

"In all business continuity planning, preparedness is critical to the successful management of unforeseen events," said Lambert. "As the Webcast illustrates, DTCC has a rigorous program in place for handling potential liquidity pressures. Familiarizing the marketplace with our procedures strengthens our ability to respond quickly and effectively in an emergency; it also strengthens confidence in the resiliency of the U.S. financial system." @

[To receive a link to DTCC's Webcast on managing liquidity pressure, contact training_administrator@dtcc.com.]

Dematerialization Makes Steady Gains

Physical certificates are fast becoming the black-and-white televisions of U.S. capital markets, thanks to the financial services firms and public companies that are utilizing a range of services offered by DTCC's Depository Trust Company (DTC) to advance dematerialization. The result for all parties, including exchanges and individual shareholders, is lower cost and risk, along with greater efficiency and convenience.

One gauge of the industry's forward march is DTC's shrinking vault inventory. As of May 2007, the depository held 2.7 million paper certificates, a 60% decline from 6.7 million in 2001.

DRS prescription

A key driver of dematerialization is the Direct Registration System (DRS), an electronic book-entry service administered by DTC that allows investors to hold securities positions in their names, directly on the books of the transfer agent or issuer. DRS also allows shares to be transferred between a transfer agent and a

broker electronically.

"Two years ago, less than 5% of all withdrawals from the depository were made in DRS statement form. Today that figure is over 60% and climbing," said John Mancuso, DTCC vice president, Securities Processing. "This translates into dramatically fewer paper certificates in circulation and far more efficient transfers."

In 2006, the major exchanges gave dematerialization a big boost via a listing requirement rule change that took effect Jan. 1, 2007, mandating exchange-listed issuers to be eligible for DRS for all new securities issued on the New York Stock Exchange, NYSE Arca, Nasdaq and the American Stock Exchange. Regional exchanges also adopted corresponding listing rules. By 2008, all existing listed issues will be required to be DRS-eligible.

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

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

Brokers and issuers

Many of the leading brokerage houses and banks already default to DRS statements. In other words, for withdrawals from DTC, if an investor does not specifically insist on a paper certificate, the shares automatically are registered electronically and the investor receives a DRS statement.

Take the case of one brokerage firm that defaulted to DRS in July 2005. In June of that year, it received 3,311 requests for paper certificates and just a single request for a DRS statement. Fast forward to January 2007, when the firm received 130 requests for paper certificates and 1,218 requests for DRS. In percentage terms, requests for DRS statements grew from less than 1% in June 2005 to over 90% in January 2007.

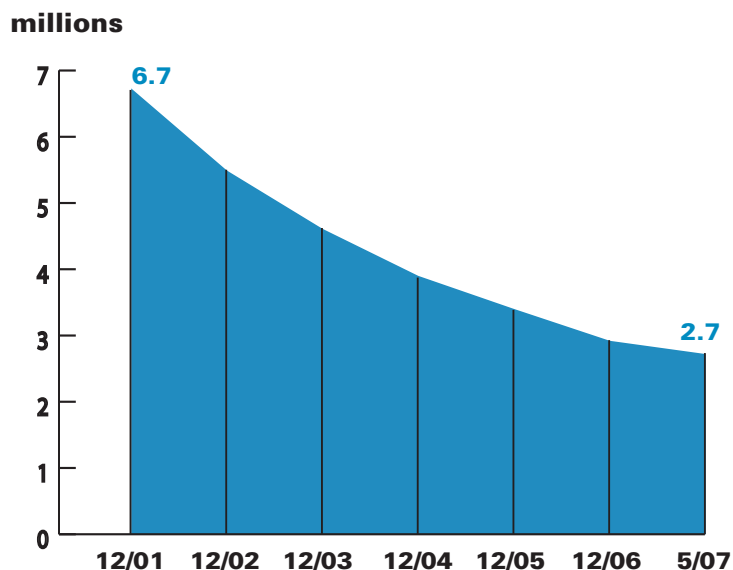
On the issuer side of the equation, an expanding roster of major companies such as Microsoft, UPS, Nuveen, Intel, Chevron Corporation, Federated Department Stores, Inc. and NCR Corporation are also coming on board with dematerialization. They no longer issue physical certificates for their offerings.

Shred and done

Another DTC program, the Destruction of Non-Transferable Securities, takes excess paper out of circulation by helping firms to rid themselves of issues that are no longer transferable.

The program allows firms to take inactive positions that may have resulted from companies going out of business or various corporate actions processing, and

Certificates in DTC's Vaults



move the shares from their account to an internal account at DTC. After an issue has been inactive for more than six years, DTC places all firms on notice for a 90-day period that the certificates are scheduled for destruction, and eventually shreds the certificates. DTC electronically images the deposits upon both receipt and prior to

destruction, keeping the records on file, in the rare case they will be needed at a future date. Since August 2004, DTC has shredded more than 515,000 certificates through the program.

Paperless 'legal' transfers

The Paperless Legal Program is a related piece of the dematerialization puzzle, eliminating the need for accompanying paper documentation on "legal" securities transfers. "Legal" is industry parlance for securities transfers that must be accompanied by paper legal documents, such as trust agreements or death certificates.

This program

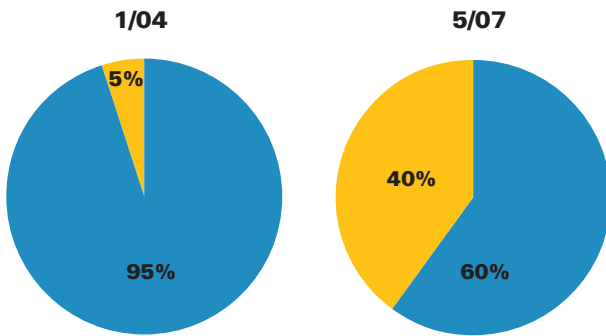
supports dematerialization by eliminating the longstanding industry practice of handling multiple copies of paper legal documents among broker/dealers, DTC and transfer agents. It operates on a medallion guarantee that certifies the person endorsing the certificates is fully authorized to do so and the proper documentation is in possession of the broker and in good order.

Pushing forward

"DTCC has a longstanding commitment to partnering with the industry to move the U.S. markets toward a certificate-free environment," said Joseph Clemente, DTCC product manager, Asset Services. "We're making good progress and we will continue to look for new ways to create or expand services that advance this industry goal." @

Requests for Withdrawals

■ Statements
■ Certificates



The Case for Paperless

Paper certificates are undeniably inefficient. They slow transaction processing, whereas electronic records expedite the transfer and sale of securities, giving investors greater security and flexibility in purchases and sales of securities assets.

Certificates are also expensive to issue, store, ship and insure. For example, the annual cost to the industry associated with issuing paper securities is \$350 million, which includes an estimated \$50 million to replace certificates that are reported lost, stolen or counterfeited.

Electronic records, on the other hand, eliminate the risk of losing certificates, and because statements have no underlying value, if one is lost, another can be issued at a fraction of the cost. In 2006, the cost of a withdrawal in DRS statement form was just \$5, compared to over \$60 for issuing a paper certificate.

What's more, when corporate actions occur, the use of statements saves all parties the hassle of tracking down certificates. With DRS, a single statement can replace the time-consuming process of locating certificates, transferring them to new parties and re-mailing them to investors. "With the increased number of corporate actions, the impact of this efficiency is tremendous," said John Mancuso, DTCC vice president, Securities Processing.

The competitiveness of the U.S. financial system is another consideration. Indeed, the United States is lagging countries that have already gone paperless, including China, India, Australia, France, Denmark, Switzerland, Argentina and Brazil, to name a few.



DTCC Expands and Renames a Business Unit by Karen Gregory

DTCC now has a Wealth Management Services business unit, incorporating Mutual Fund Services, the Managed Accounts Service and a new proposed service for alternative investment products.

Until recently, DTCC's long-established Mutual Fund Services served as the umbrella for all three fund businesses. The name change reflects DTCC's expansion over the past two years into these new and growing product areas.

"Managed accounts and alternative investment products present complex processing dynamics," explained Ann Bergin, DTCC managing director and general manager, Wealth Management Services. "Our customers have asked us to create solutions for these products that will help them reduce processing risk and related errors, ensure business continuity, support regulatory compliance and increase operating margins."

Managed Accounts Service

DTCC introduced the Managed Accounts Service last September to provide the industry with an automated, centralized platform that streamlines communications between sponsor broker/dealers and their investment managers. This service is offered by DTCC Solutions LLC, a DTCC subsidiary.

Managed accounts include separately managed accounts, unified managed accounts and other similar types of portfolios. These investment vehicles are increasingly popular with U.S. investors, particularly those with rising net worth who are looking

for nontraditional avenues to expand their wealth.

Alternative investments

DTCC's service for alternative investment products, currently in pilot, will standardize and automate the processing and settlement of a range of products, including hedge funds, funds of hedge funds, real estate investment trusts, managed futures and commodity pools. Subject to approval by the Securities and Exchange Commission, it will be offered by DTCC's National Securities Clearing Corporation subsidiary.

Higher-tier investors also are turning to alternative investment products. Hedge funds alone reached \$1.89 trillion in worldwide assets in 2006, according to a

report released by Institutional Investor News and HedgeFund.net, and institutional demand for them could triple by the end of the decade.

"Wealth Management Services is committed to fully supporting the expanding asset management industry with new services, as well as enhancements to our traditional ones, many of which have become industry standards," Bergin said. "At the same time, we will leverage our experience and create partnerships with global providers to develop technology solutions that address the ever-growing range of our customers' businesses and their increasingly complex processing requirements." @



Wealth Management Services Quarterly is DTCC's new publication providing news and information on DTCC's three services for the funds industry. This publication replaces Mutual Funds News, a former DTCC publication for the mutual fund industry.

To subscribe to Wealth Management Services Quarterly, send an email to editor@dtcc.com and include your full name, title and mailing address.

New DTCC Service for the Funds Industry Wins Award by Karen Clarke

DTCC's Managed Accounts Service won a first-place award in the Efficiencies/Streamlining category in the 2007 Source Media's Fund Operations Awards sponsored by Money Management Executive magazine. DTCC's service was honored for bringing "an unprecedented level of efficiency that will help the managed accounts industry take its impressive growth to new heights."

Ann Bergin, DTCC managing director and general manager, Wealth Management Services, also was recognized in the Leadership category as a "dynamic leader and innovator in the financial services industry."

"The Depository Trust & Clearing Corporation's Managed Accounts Service is being honored this year as a top winner in two categories," said Lee Barney, editor of Money Management Executive. "Since the biggest challenge facing the separately managed account industry today is integrating money managers' systems with the proprietary platforms of sponsors, the fact that DTCC has created a centralized communications platform through which the two can communicate will be a tremendous boost to the industry," she added.

Service and leadership

"DTCC is honored to receive this industry recognition for one of our newest services and for an executive who has a history of leadership in the funds industry," said Donald F. Donahue, DTCC chairman-elect and CEO. "Ann and her team's ability to bring the Managed Accounts Service to market at a time of rapid growth in this industry segment reflects our commitment to work with customers to meet their expanding business needs. As DTCC grows its funds business into new areas, the industry will

benefit from the vision Ann has demonstrated in the mutual funds market over the years."

The winners, featured in the June 11 issue of Money Management Executive, were honored at the National Investment Company Service Association's General Membership Meeting.

First-of-its-kind

DTCC has been working with The Money Management Institute to develop communication standards for the managed accounts industry, and Bergin was quick to acknowledge the contributions of both internal and external partners in bringing new efficiencies to the industry.

"I want to recognize the contributions of everyone in Wealth Management Services who works so closely with the industry and our customers," Bergin said. "Collaboration is the foundation of our business unit, and this approach has helped us successfully expand into new market segments and create partnerships with industry groups."

DTCC introduced its Managed Accounts Service in 2006, a first-of-its-kind, automated communications service that links managed account sponsors and investment managers to a centralized communications platform. Bergin forged an alliance with Citigroup Smith Barney, the industry's leading sponsor of managed accounts, as the charter firm for the service. The partnership served to jump-start momentum toward an unprecedented level of efficiency in the rapidly growing managed accounts industry.

When DTCC launched the service, a report in the online publication FUNDfire stated, "Industry experts are hailing DTCC's announcement and Citigroup's involvement, calling it one of the largest



Ann Bergin, DTCC managing director and general manager, Wealth Management Services

victories to date in the effort to build a centralized, SMA-focused system."

More on the awards

Money Management Executive began the SourceMedia Fund Operations Awards five years ago to recognize service providers in three key areas: Leadership, Innovation and Efficiencies/Streamlining. This year, six judges reviewed more than 100 nominations, according to Barney.

"We will be keeping a close eye on how DTCC's Managed Accounts Service gains traction beyond charter member Citigroup Smith Barney and the other initial participants once it launches this fall," she added.

Other winners in the Efficiencies category are Goldman Sachs, a global investment banking, securities and investment management firm, and SEI, a global provider of outsourced asset management.

Executives joining Bergin in the Leadership category are Christopher Wilson, president of Columbia Funds, Inc., and Steve Kirchmar of Putnam Investments. @

Mortgage-Backed Securities: Matching of Specified Pool Trades Goes Live

by James Conmy

After months of customer testing, Fixed Income Clearing Corporation (FICC) went live in June with its new matching service for specified pool trades of mortgage-backed securities.

The new service uses FICC's Real-Time Trade Matching (RTTM) system to make it easier for firms to submit specified pool trades, to match

them bilaterally and to report the matches in real time. FICC then is able to give its clearing customers immediate trade notification and status information in the same way that it has long done for to-be-announced (TBA) trades.

Customers began submitting specified pool trades to RTTM in June.

Central counterparty

The rollout of this functionality is an important milestone in the planned creation of a central counterparty (CCP) for mortgage-backed securities. "We have been working behind the scenes – and with customers – on the CCP for several years and the activation of this new matching service marks the first deliverable of a new capability," said Dennis

Paganucci, DTCC director, Clearance and Settlement Product Management.

FICC now provides two new end-of-day reports dedicated to specified pool trade activity. The reports correspond to clearing reports for TBA trades and, as a result, customers can now utilize both sets of reports to reconcile their specified pool trade activity submitted to RTTM.

The handful of firms that hadn't fully completed testing by June were obliged to use RTTM-Web to enter or affirm specified pool trades, according to Melanie Sterman, DTCC director, Clearance and Settlement Product Management.

Next steps

The next step in the process for specified pool trades will involve final money calculation and repricing. RTTM will automatically calculate final money.

Testing of the second phase is set for later this year. @

[To learn more, contact Melanie Sterman at msterman@dtcc.com or at 212.855.7614.]



'We have been working behind the scenes – and with customers – on the CCP for several years and the activation of this new matching service marks the first deliverable of a new capability.'

– Dennis Paganucci, DTCC director, Clearance and Settlement Product Management



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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