



# European Regulators' Recommendations Affirm EuroCCP Proposal by Melanie Best

In a report aimed at increasing the safety and soundness of central counterparties (CCPs) in the European Union, the region's central banks and securities regulators recommend that interoperating CCPs in Europe prudently manage the risks arising from their linkages. These recommendations affirm the concerns raised by EuroCCP in recent months. The report from the European System of Central Banks (ESCB) and Committee of European Securities

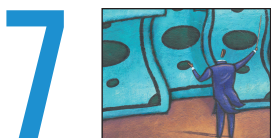
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## Donahue Stresses Importance of Central Repository For OTC Derivatives

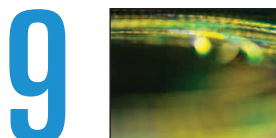
Donald F. Donahue, DTCC chairman and CEO, stressed that a central trade repository for over-the-counter (OTC) derivatives contracts is essential to mitigating risk and enhancing transparency in the market. Donahue made his remarks as part of his July 21 keynote address at a U.S. Chamber of Commerce discussion titled "Modernizing Derivatives Oversight: Developing Policy for the 21st Century." "DTCC strongly urges Congress and regulators to codify into law the continued

[continued on page 4]

### in this issue



**Loan/SERV's Reconciliation Service Reaches 1,200+ Funds**



**Streamlining Equity Trade Capture and Reporting**



**Un-sponsored ADRs Get Tax Relief**

Regulators (CESR) could bolster support for an Interoperability Convention to be signed by all CCPs that interoperate, a proposal EuroCCP made public in mid-June.

## Interoperability risks

Interoperability – the arrangement among CCPs that enables market participants to choose which CCP they use – is the next stage in Europe's market evolution. The arrival of new pan-European trading platforms and the expansion of stock exchanges beyond their national markets have given trading firms more choice of trading venues and reduced their trading costs. Interoperability among CCPs, when fully implemented across Europe, introduces competition in clearing by enabling market participants to use the CCP of their choice regardless of where they trade.

But interoperability involves certain risks, as the ESCB and CESR recognize. In their report issued June 23 (Ref. CESR/09-446), the two authorities recommend that clearing houses conduct risk assessments

before establishing links with each other, and that such links be built and operated in a way that effectively reduces the risks associated with the link. In particular, the report advises, "regulation and contractual rules should be designed such that no CCP is exposed to unexpected obligations or distortions of rights/obligations vis-à-vis the other one."

As the ESCB/CESR report implies, much of the risk of interoperability stems from the fact that CCPs differ, sometimes significantly, across key parameters like membership standards, collateral requirements and risk management procedures. With interoperability, weaknesses in one CCP are no longer isolated to that entity. Furthermore, while CCPs' raison d'être is to protect their participants from the failure of a counterparty, CCPs themselves can go bankrupt. The default of a CCP that interoperates with others could have wider and more complex market impacts than the failure of a large trading participant, notes the report.

## EuroCCP proposal

To date, four CCPs – EuroCCP, Fortis EMCF, LCH.Clearnet Ltd. and SIX x-clear – have announced plans to interoperate, and more may join this roster in the coming months. Although multiple bilateral agreements might seem the quickest path to activating interoperability, bilateral contracts cannot capture the multilateral nature of interlinked CCPs.

While bilateral agreements are a step in the right direction, establishment of a single, standard Interoperability Convention, signed by all CCPs, publicly disclosed and accessible to market participants, trading venues and regulators, would mitigate interoperability risk. By making clearing houses' interoperability arrangements transparent,

such a convention also would accelerate the connectivity process across Europe and enhance the region's ability to attract investment capital as the global recession abates.

EuroCCP has been promoting an Interoperability Convention this year in discussions with fellow CCPs and with regulators, and in a June 17 press release the company went public with its proposal. While the ESCB and CESR

**By making clearing houses' interoperability arrangements transparent, such a convention also would accelerate the connectivity process across Europe and enhance the region's ability to attract investment capital as the global recession abates.**

recommendations calling for contractual terms that reduce the risks arising from interlinking CCPs add weight to the rationale for an Interoperability Convention, they are purely advisory.

Interoperability negotiations are now underway between EuroCCP, Fortis EMCF and SIX x-clear on the principles and procedures for serving clients in the Nasdaq OMX Nordic markets of Denmark, Finland and Sweden. The agreement crafted here could become the foundation of an Interoperability Convention to be used by all interoperating CCPs throughout Europe. @

## Contents

1. European Regulators' Recommendations Affirm EuroCCP Proposal
1. Donahue Stresses Importance of Central Repository for OTC Derivatives
3. EuroCCP Gears Up for January Launch in Nordic Markets
5. U.S. Chamber of Commerce Event Sparks Debate On OTC Derivatives Regulation
6. DTCC Names Industry Expert as General Manager of Trade Information Warehouse
7. Loan/SERV's Reconciliation Service Reaches 1,200+ Funds
8. DTCC Nears Finish Line on Options Symbology Revamp
9. New System Will Streamline Equity Trade Capture and Reporting
10. Unsponsored ADRs Get Tax Relief
11. Paying Agents Ace Structured Securities Report Card
12. Asset Services Introduces New Customer Publication

# EuroCCP Gears Up for January Launch in Nordic Markets

by Melanie Best

**E**uroCCP, Fortis EMCF and SIX x-clear – the three central counterparties (CCPs) that will interoperate to serve clients of Nasdaq OMX's stock exchanges in Denmark, Finland and Sweden – have agreed to a Jan. 29, 2010, start date for their interoperability.

Establishing the timetable is one of several agreements EuroCCP and its fellow CCPs are tackling in preparation for the opening of these Nordic markets to competitive clearing services. The CCPs must also finalize the terms of their interoperability agreement and work out testing schedules.

EuroCCP is meeting with potential customers and getting ready for the expansion of its services to clear for its first national stock exchange, a significant milestone in the business development of EuroCCP.

"We're preparing for a busy August and fall," said Neil Henderson, DTCC managing director, EuroCCP Product Management. "Beyond the legal work on the interoperating agreements, we'll focus on explaining EuroCCP services and risk management capabilities to prospective clients and helping them with our onboarding procedures."

## Competitive clearing

The arrival of multiple CCPs in Denmark, Finland and Sweden will mark a critical milestone in the evolution of post-trade processing there. At present, Fortis EMCF is the sole provider of central counterparty clearing to Nasdaq OMX users in the Nordic region, and this is an optional service. But, starting Oct. 9,

2009, subject to regulatory approvals, Nasdaq OMX intends to make CCP clearing mandatory for the exchanges in these markets. Fortis EMCF will remain the only CCP option until January 29, when users will be able to switch to EuroCCP or SIX x-clear.

and will make the arrangements safer."

So far in 2009, EuroCCP representatives have met often with regulators and securities dealers associations in the region. In the coming months, as the company conducts extensive outreach to prospective customers in the three



Interoperability between the three CCPs will enable each member of Nasdaq OMX Nordic's exchanges to choose the clearing house that will clear and settle its trades.

"EuroCCP looks forward to helping deliver a truly competitive choice of clearers to firms trading on the Nasdaq OMX Nordic exchanges," said Diana Chan, CEO of EuroCCP. "Furthermore, we hope our work in drawing up an interoperability agreement with EMCF and x-clear will provide the foundation for an Interoperability Convention all CCPs that link up in Europe can sign. An Interoperability Convention will make it transparent to market participants, trading venues and regulators how the CCPs manage their risk exposure to each other,

markets, EuroCCP representatives will make even more frequent trips to the region. In addition to one-on-one meetings, EuroCCP plans to organize seminars for prospective clients to assist with their membership application process.

EuroCCP and corporate parent DTCC are becoming more active in financial services sector activities in the Nordic region. In late September the companies will participate in the Eurofi Financial Forum, taking place September 29-October 1 in Göteborg, Sweden. EuroCCP is a co-sponsor of this year's forum, and Donald F. Donahue, DTCC chairman and CEO, will participate in a panel on September 30. @

# Donahue Calls for Central Repository

*Continued from cover*

operation of a central global repository for OTC credit derivatives,” Donahue said. “We believe that having all of this information residing in a single place is a crucial contribution to reducing risk and promoting market efficiency. When markets are in turmoil, it is critical that regulators have the ability to see the full details on the underlying trading positions of derivatives contracts from a central vantage point to quickly assess systemic risk across the financial system – and to bring greater transparency to the market. This snapshot of the market can only be provided by a single global repository.”

## Role in OTC derivatives market

DTCC operates the Trade Information Warehouse – the only comprehensive repository and post-trade processing infrastructure for OTC credit derivatives in the world. The Warehouse handles the calculation, netting and central settlement of payment obligations between counterparties, and automates the processing of “credit events” – situations where the protection against default provided by a credit default swap is activated.

In addition, DTCC’s Deriv/SERV matching engine, which electronically captures, confirms and matches over 95% of all credit derivatives traded globally, supplies the Warehouse with more than 41,000 transaction sides daily. The Warehouse connects and services over 1,400 global dealers, asset managers and other market participants in 35 countries. The trade repository was also designed to be extended to other OTC derivative asset classes.

## Support for CCP services

DTCC has publicly stated that it will support all efforts to create central counterparty (CCP) services planned in

the U.S. and overseas, on a non-discriminatory basis.

“We believe that when central counterparties and a global repository work in tandem to support each other’s functions, risk can be significantly mitigated, and transparency

enhanced in the marketplace,” Donahue said. “This powerful combination is what is needed to ensure the business community has the necessary risk benefits and financing flexibility, and our policymakers have the assurance that the integrity of the financial system will be maintained.

“If we consider that globally there are about six CCPs planned to be launched either in Europe or in the U.S., we can recognize the potential for fragmentation of data about the market, if there’s no central repository storing all the data in one place,” Donahue said. “If we recognize that these CCPs will only clear a portion of the market, the need for a central repository is further emphasized.”

## More on DTCC

Since last year, DTCC has seamlessly processed, or is processing through the Warehouse, more than 40 credit events, including the Lehman Brothers and Washington Mutual bankruptcies as well as the conservatorships for Freddie Mac and Fannie Mae. Because the industry had in place a robust, centralized infrastructure for the CDS market in the wake of last year’s financial turmoil, market participants were able to manage the



Donald F. Donahue, DTCC chairman and CEO, speaks to the U.S. Chamber of Commerce on July 21

multiple processing and operational challenges they faced with a greater degree of certainty and efficiency.

DTCC has been working closely with market participants and regulators to achieve that vision. Since November 2008, DTCC has been publishing weekly on its website key statistics and data from the Warehouse on the size and turnover of the CDS market.

Following the Lehman bankruptcy last year, DTCC played a significant role in unwinding over \$500 billion in open trading positions from trades in equities, mortgage-backed and U.S. government securities, without any loss to the industry – and avoiding additional burden on taxpayers.

DTCC General Counsel Larry E. Thompson, who recently testified before the Capital Markets Subcommittee of the House Financial Services Committee, served as a panelist during the Chamber of Commerce event (see article, page 5).

To view the entire text of Donahue’s speech, go to DTCC’s website at [www.dtcc.com](http://www.dtcc.com) and click Thought Leadership. @

# U.S. Chamber of Commerce Event Sparks Debate On OTC Derivatives Regulation

by Judith Inosanto

Speaking before an audience of approximately 150 corporate executives at a recent U.S. Chamber of Commerce briefing on regulation of the over-the-counter (OTC) derivatives market, Larry E. Thompson, DTCC managing director and general counsel, said, “Congress is reviewing a variety of ways to create transparency and reduce risk in the OTC marketplace. This includes standardizing OTC contracts as much as possible so that trades can be cleared through a central counterparty or CCP, but also leaving some flexibility for the trading of non-standard contracts designed for individual company needs.”

The July 21 Washington D.C. event, “Modernizing Derivatives Oversight: Developing Policy for the 21st Century,” was put on by the Chamber’s National Chamber Foundation (NCF). NCF is a non-profit affiliate of the U.S. Chamber of Commerce dedicated to identifying and fostering public debate on emerging critical issues. Donald F. Donahue, DTCC Chairman and CEO, gave the keynote address at the conference, which brought together experts from diverse sectors to educate and engage the public about the use of OTC derivatives and their role in the markets. (See page 1 for article on Donahue’s comments.)

## Transparency and systemic risk

Thompson participated in a panel discussion, “Examining Derivatives and Systemic Risk.” Other participants included Kevin Gould, Markit North America president and global head of fixed income; Theo Lubke, Federal Reserve Bank of New York senior vice president; Cynthia Meyn, PIMCO senior vice president; John Shay, International Derivatives Clearing Group LLC founder and chief marketing officer; and Don Thompson, managing director, JPMorgan Chase & Co. Sharon Brown-Hruska, Ph.D. and vice president, National Economic Research Associates, Inc., moderated the session, which focused on the operational issues related to improving oversight and transparency in OTC derivatives trading and how that fits within a broader goal of reducing systemic risk.

“We now have an opportunity to comprehensively reform regulation of our capital markets – and we must get it right,” said David Chavern, U.S. Chamber of Commerce executive vice president and COO, during his opening remarks for the event. “The Administration and the Chamber agree on many common goals, including more comprehensive oversight of systemic risk, greater transparency, and improved customer and investor protections. Of critical importance is how to regulate complex financial instruments such as over-the-counter derivatives.

“Businesses from diverse sectors use OTC derivatives not to take speculative positions, but to hedge against legitimate business risks, including fluctuations in materials prices,



Panel discussion on “Examining Derivatives and Systemic Risk” (from left): Theo Lubke, Federal Reserve Bank of New York senior vice president; Larry E. Thompson, DTCC managing director and general counsel; and Kevin Gould, Markit North America president and global head of fixed income

commodities, fuel, interest rates and foreign currencies. The policy question to be addressed is this: how can we enhance transparency and oversight of the derivatives markets while maintaining an over-the-counter market and the important risk management function it serves for companies of all kinds? This question is fundamental to a return to well-functioning capital markets,” Chavern added.

[continued on page 6]

## Debate on OTC Derivatives Regulation

*Continued from page 5*

### Market soundness

A separate panel session, "Fostering Efficiency and Transparency," consisted of representatives from the key regulatory bodies and corporate investors in derivatives products. This group focused on developing policies that will protect the soundness of the capital markets while upholding the important risk-management function these financial instruments perform for companies and market participants.

Panelists included Megan Ivory Carr, 3M Company, manager, Federal Government Services; Michael Cosgrove, GFI Group, Inc. managing director and head of Commodities and Energy Brokerage, North America; Elizabeth King, U.S. Securities and Exchange Commission associate director, Division of Trading and Markets; Michael Shapiro, Zimmer, Inc. associate director, Treasury; and Ananda Radhakrishnan, Commodity Futures Trading Commission, director, Division and Intermediary Oversight. The panel moderator was Russell B. Mallett, III, PricewaterhouseCoopers LLP, Financial Services Technical Leader, National Professional Services Group.

"As Congress looks at the value of creating a systemic risk regulator, there is always a need for a strong and robust infrastructure like the one DTCC has provided, ensuring that risk can be viewed from a central vantage point," Thompson advised during his panel session. "We believe DTCC should continue to serve as a lynchpin of the regulatory reforms under consideration." @

## DTCC Names Industry Expert as General Manager of Trade Information Warehouse *by Judith Inosanto*

DTCC announced on July 7 that Stewart Macbeth, an industry-recognized expert in the over-the-counter (OTC) derivatives market, has joined DTCC as managing director, DTCC, and general manager of the Trade Information Warehouse.



Stewart Macbeth, managing director, DTCC, and general manager, Trade Information Warehouse

The Warehouse is the market's only central repository and post-trade processing infrastructure for OTC credit derivatives contracts, supporting global dealers and 1,400 buy-side firms that trade these instruments from 35 countries.

### Continued Warehouse development

Macbeth, who will be based in DTCC's London office, will be responsible for all aspects of the day-to-day operations and continuing development of Warehouse services globally. He reports to Peter Axilrod, DTCC managing director, Business Development and Deriv/SERV.

"Having someone with Stewart's extraordinary experience and extensive knowledge of this complex market positions us well to expand the benefits of DTCC's central repository with services for

CDS and to determine the extendibility of the Warehouse to other OTC derivative asset classes," said Michael Bodson, DTCC executive managing director, Business Management and Strategy.

### Background in the industry

Macbeth comes to DTCC with more than 15 years of OTC derivatives industry experience. He was most recently managing director, global head of operations risk and business architecture at UBS, a position he held from 2007. From 1996 to 2002, he ran fixed income derivatives operations globally for the firm, managing credit derivatives support activities, which also included designing and implementing settlement and confirmation applications. In 2002, he became global head of all OTC derivatives operations, at which time he assumed responsibility for equity derivatives.

Prior to UBS, Macbeth was at KPMG in London, in its financial services practice, where he qualified as a chartered accountant. He earned a bachelor's degree in mathematics from Nottingham University and a master's degree from the University of London.

### Warehouse Trust Company

"DTCC has been a proven leader in bringing greater efficiency and risk mitigation to the OTC derivatives market, and the Warehouse played a critical role in helping market participants safely manage the unprecedented market challenges they faced this past year," said Bodson.

In May, DTCC announced that it had filed applications with the Federal Reserve system and with the New York State Banking Department (NYSBD) to form a limited-purpose trust company that will house the functions of the Warehouse. The

# Loan/SERV's Reconciliation Service Reaches 1,200+ Funds

by Edward C. Kelleher

new company, to be called The Warehouse Trust Company LLC, will become a wholly owned subsidiary of DTCC Deriv/SERV LLC, which operates DTCC's automated

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– Michael Bodson, DTCC executive managing director, Business Management and Strategy

services for OTC derivatives. It is expected that the Warehouse Trust will also become subject to a collaborative global regulatory framework involving interested regulators in Europe as well as the U.S.

## Warehouse's global services

As of June 26, the total gross notional value of the approximately 2.1 million contracts maintained in the Warehouse was about US\$26.5 trillion.

DTCC is also working with market participants to bring contracts from more customized, or bespoke, instruments such as CDS on collateralized debt obligations into the Warehouse. The Warehouse was also designed to be extensible to other OTC derivatives instruments such as interest rates, equities and commodities.

In addition to its global trade repository, Warehouse automated services include centralized payment calculations, netting, and in partnership with CLS Bank International, settlement of payment obligations between counterparties of a CDS transaction. @

**D**TCC announced that more than 1,200 funds administered by more than 70 leading fund managers are now linked to its Loan/SERV Reconciliation Service.

DTCC's Loan/SERV Reconciliation Service helps automate and streamline the processing of syndicated commercial loans by enabling agent banks and lenders – in this case, funds – to track, view and reconcile loan positions on a daily basis. The service, already in full production with leading global banks such as J.P. Morgan, Citi and Deutsche Bank, now provides information on more than 75,000 loan positions.

Leading investment firms that have recently linked their funds to Loan/SERV for the Reconciliation Service include PIMCO, Oak Hill Advisors, Highland Capital Management and KKR.

## Same page

“Leading global investment management firms realize they need to make sure their loan positions are on the same page as the agent banks to ensure the accurate and timely servicing of these loans,” said Chris Childs, DTCC vice president, Global Loans Product Management. “Loan/SERV provides this data access in real time. By linking to Loan/SERV, these fund managers are introducing cost savings, boosting efficiencies and providing greater transparency in the syndicated loan market.”

In June, DTCC also announced that its Loan/SERV advisory committee endorsed plans to add cash-settlement capabilities, including Delivery versus Payment (DVP), to its



Loan/SERV suite of services. A timetable for testing and production will be issued shortly. The advisory committee includes the Bank of New York Mellon, Barclays Capital, Citi, Deutsche Bank, J.P. Morgan and the Royal Bank of Scotland, all agent banks serving the syndicated loan market.

## Reducing risk

“Our multi-currency DVP service, coupled with Loan/SERV Reconciliation, will dramatically reduce risk and provide greater certainty in the syndicated loan market,” said Childs. “More and more investment firms realize the benefits that come with this automation, and it's why we've seen such a dramatic jump in the number of funds linking to the Reconciliation Service. In the past month

alone, more than 25 fund managers signed up for it.”

Along with its Reconciliation Service, DTCC introduced its Loan/SERV Messaging Service in 2008, which provides a safe and automated network for the transmission, receipt and online storage of industry-standard loan messages. @

# DTCC Nears Finish Line on Options Symbology Revamp by Craig Donner

**D**TCC is on pace to meet the February 2010 deadline for an industry-wide initiative that will streamline and bring greater clarity to the way exchange-listed option contracts are represented and reported in the financial marketplace.

Under the Options Symbology Initiative (OSI), which is being spearheaded by the Options Clearing Corporation (OCC), the confusing and antiquated method of identifying options contracts will be replaced with a more investor- and processing-friendly symbology key. The changes will affect equity options, index options, yield-based options, short-date options and flex options.

“The new symbols should reduce processing errors, improve investor comprehension, enhance efficiencies for symbol elections and support the long-term growth of the options market,” said Susan Cosgrove, DTCC managing director, Clearance and Settlement/Equities.

## Services impacted

To become compliant with the new symbology key, National Securities Clearing Corporation (NSCC) and The Depository Trust Company (DTC) have been making adjustments to several products and services that process transactions related to options. These include the Automated Customer Account Transfer Service (ACATS), the Cost-Basis Reporting Service (CBRS), Collateral Loans (OCC Pledges and Releases) and Premium Payment Orders (PPOs).

“We are working closely with market participants to ensure that our systems and products will be fully data compliant,” said Cosgrove. “We’ve already completed part of the project and are making steady progress to meet the deadline.”

## Ahead of the curve

DTC completed the majority of the required OSI modifications to the input and output formats of its Collateral Loan System for OCC Pledges and Release Requests in October 2008. DTC implemented these changes without incident, and the transition has been seamless for market participants.

In addition, DTC is on track to implement changes for PPOs by supporting a migration period that will allow customers to submit transactions in the new compliant formats by the end of October 2009.

At NSCC, changes for both ACATS and CBRS will be implemented in production on February 8, 2010 – four days ahead of the industry-wide mandate.

“In ACATS, we will need to run a conversion process to ensure that all option assets that are included in a current transfer are updated to the new formats,” said Louis Lepore, DTCC product

manager, Clearance and Settlement/Equities. “To ensure a seamless conversion and reduce the risk of potential processing errors, we will be running the conversion over the weekend prior to the industry implementation date. We understand the significance of this project and want to ensure that all the pieces are in place for a smooth switch-over to the new formats.”

## Replacing OPRA

The current method of identifying exchange-listed option contracts dates back to the early 1980s and uses a combination of Options Price Reporting Authority (OPRA) codes (or tickers) that can range between three and five characters. The first one to three characters represent the option root symbol and the remaining characters identify the expiration month, call/put indicator and strike price. For example, IBMHO refers to an IBM call option that expires on August 21, 2009, with a strike price of 75.

“The current symbology key looks more like alphabet soup than an easy identifier of a financial instrument,” said Cosgrove.



“It’s not uncommon for investors, traders and others in the industry to refer to detailed charts to determine which option is being traded, when and at what price – creating serious operational risk issues in front-, middle- and back-office processes.”

OSI is replacing the OPRA codes and fractions currently in use with a new identifier that will use the commonly recognized underlying security symbol and also include data on the option expiration day (as part of the expiration date) and the submission and reporting of strike prices in decimal format only.

Under the new symbology key, that same IBM option would be represented as IBM 09 08 21 C 00075 000 – which is much more intuitive. @

# New System Will Streamline Equity Trade Capture And Reporting

by Craig Donner

National Securities Clearing Corporation (NSCC) has embarked on the most comprehensive redesign of its equity trade capture systems in decades. The multi-year initiative, which will consolidate and modernize the trade-capture and reporting process to bring greater efficiency, reduced risk and cost savings to the industry, also dovetails with NSCC's plans to accelerate its trade guarantee.

The new system, called Universal Trade Capture (UTC), will replace the multiple trade-capture applications currently used by NSCC with a single validation and reporting engine. It will introduce a standardized input record from all marketplaces and standardized real-time, message-based output to participants. Marketplaces and participants will have the option to migrate to the new universal format at their own pace or may continue using the legacy formats. UTC is scheduled to go live in the second half of 2010.

"UTC will lower operating costs for NSCC and its customers by streamlining and standardizing formats and processes," said Susan Cosgrove, DTCC managing director, Clearance and Settlement/Equities. "This initiative will give participants the opportunity to receive unified, message-based output for all marketplaces. Once UTC and the accelerated guarantee are implemented, firms will have contract data in hand as well as confirmation that their trade is guaranteed by NSCC within minutes of execution, which will speed up their reconciliation process and mitigate operational and counterparty risk."

Another benefit of UTC is that it will increase NSCC throughput and reduce

storage costs, which will boost efficiencies and accommodate future growth in trading volume.

## Four is not better than one

Under the current system for equity trade recording, each marketplace uses its own unique format for submitting input data to NSCC, which employs four different applications to accommodate the lack of standardization across execution platforms. After NSCC receives the data, it edits and produces contract reporting in four different reports in a machine-readable-output (MRO) data file format in batches throughout the day.

"The current process creates an unnecessary degree of operational risk for firms and hinders their ability to efficiently reconcile millions of equity trades intra-day," said Cosgrove.

## The new paradigm

To ensure maximum flexibility, the UTC system will be able to accept, process and provide output in both the new format as well as in the legacy formats for participants and marketplaces. DTCC's middleware application will translate all inputs and outputs to/from UTC and legacy standards. The new output will be available in a real-time Financial Information eXchange (FIX) message or via an MRO data file.

"Customers can subscribe to the type of output they would like to receive and the middleware product will produce it," said William Kapogiannis, DTCC director, Clearance and Settlement/Equities. "The 'middleware layer' will allow marketplaces and participants to transition at will."

## Thumbs up from the industry

"A near-real-time message for equity

transactions will allow firms to reconcile trades faster and more efficiently," said Anthony Principato, managing director, Goldman Sachs Execution & Clearing L.P. "The new streamlined system will also increase our processing efficiencies and allow us to more effectively manage capacity increases in the future. And at a time when risk mitigation is paramount, traders and clients want to have near-immediate confirmation that their trades have been recorded and guaranteed."

NSCC assembled a working group to discuss UTC processes and formats in mid-July. In addition, it recently sent a survey to customers to gain their input on key issues, formats and functionality.

"The goal is to create a new paradigm that meets the needs of the industry, reduces costs and allows for as seamless a transition as possible for our customers," Cosgrove said. "An important step in that process is developing an industry-wide consensus on functionality and formats by the end of summer so firms can begin moving forward with their own development requirements."

## Closing in on real time

The UTC project closely aligns with NSCC's plans to accelerate its trade guarantee, scheduled to take effect later this year, subject to approval by the Securities and Exchange Commission, by creating a near-real-time acknowledgement for firms that the central counterparty guarantee has been applied.

The new guarantee will take effect upon validation for locked-in trades and comparison for non-locked-in trades – as opposed to the current T+1 guarantee, which has a delay of up to two business days before NSCC guarantees a trade. @

# Un-sponsored ADRs Get Tax Relief

by Edward C. Kelleher

The Depository Trust Company (DTC) has expanded its TaxRelief Service™ to provide tax relief benefits for holders of the growing number of un-sponsored American Depositary Receipts (ADRs). The service provides customers billions of dollars in tax benefits each year and was previously available for sponsored ADRs.

ADRs, which allow investors to invest in securities from other countries, are receipts for the shares of a foreign-based company held in custody in the U.S. Whereas a sponsored ADR is created by a depository bank in collaboration with the issuing company, an un-sponsored ADR has no direct involvement with the foreign company and is generally established in response to investor demand.

“The expansion of TaxRelief to un-sponsored ADRs will help standardize the tax-relief process for both un-sponsored and sponsored programs and will bring significant processing efficiencies to the marketplace,” said Patrick Kirby, DTCC managing director, Asset Services.

## Rule change

Until last year, if a depository bank wanted to establish an un-sponsored ADR, the non-U.S. company had to register its securities with the U.S. Securities and Exchange Commission (SEC) or qualify for an SEC exemption, which meant filing detailed documentation with the SEC.

“In October 2008, the SEC amended its rules and simplified the exemption process,” said Nardeo Ganesh, DTCC director, Tax Services. “In effect, these changes removed the involvement of the issuer, which has led to the rapid growth of these instruments.”

The new rules grant exemptions to non-U.S. companies if they:

- Publish their disclosure documents on their website in English.

- Maintain at least 55% of their global trading volume on one or two exchanges outside the U.S., with higher trading volume on one of the exchanges than the total trading volume in the U.S.

- Have no existing reporting obligations to the SEC.

“The changes have prompted the establishment of more than 850 un-sponsored ADRs since last year, which benefits investors who are looking for new opportunities to invest in global securities,” Ganesh said. “It also meant that these customers would seek the same tax relief that DTC gives them with their sponsored ADR investments.”

## ‘At-source’ relief

The TaxRelief Service, offered by DTC’s Global Tax Services, enables customers to secure relief from international withholding taxes. This comes either up front when a non-U.S. income payment is due – called “at-source” relief – or subsequently through accelerated refunds.

“Un-sponsored ADRs are not a new investment vehicle, but with the resurgence of these instruments after the SEC amendment, we knew we needed to do something about tax relief right away,” said Michael Finck, managing director, The Bank of New York Mellon. “So we immediately initiated talks with DTC.”

Finck added, “Many of these ADRs are dividend-paying accounts, so tax relief and a less onerous reclamation process certainly make the product more attractive.”

To establish a process to obtain tax relief, DTC worked with The Bank of New York Mellon and the three other major depository banks – Citi, Deutsche Bank and JPMorgan Chase – along with GlobeTax Services, a firm that helps the depository banks process tax information.

## Multiple parties

“Obtaining tax relief for an un-sponsored ADR is more complicated than the process for a sponsored ADR,” said Ganesh. “With a sponsored ADR, you deal with one depository bank and one local custodian bank, but with un-sponsored ADRs, you can deal with multiple depository banks, as well as many different local custodian banks. It’s necessary to get all those parties



**‘Many of these ADRs are dividend-paying accounts, so tax relief and a less onerous reclamation process certainly make the product more attractive.’**

Michael Finck, managing director,  
The Bank of New York Mellon

on the same page when you process the tax relief.”

Today, DTC offers its TaxRelief Service for more than 152 un-sponsored ADRs in six countries, and the service will be expanded to cover additional countries.

“We’ll continue to work with the depository banks to expand the coverage of TaxRelief in other markets and for non-U.S. investors where appropriate,” said Ganesh. @

# Paying Agents Ace Structured Securities Report Card

by Edward C. Kelleher

The Report Card: the bane of many a student's existence. But at The Depository Trust Company (DTC), the report card is a major initiative helping the industry solve processing problems in structured securities by tracking the performance of the leading paying agents on a monthly basis. The agents are responsible for reporting payments rates to DTC, which determine principal and interest (P&I) payments to beneficial owners.

"Payment data problems in the market for securitized instruments have been responsible for billions of dollars in late payments to hundreds of thousands of investors each year," said Peter Gleeson, DTCC vice president, Asset Services. "These late or inaccurate payments cause additional interest costs, back-office write-offs and significant exception processing costs to broker/dealers and custodian banks."

The report card is changing all that.

## Working with the industry

DTC and an industry-wide task force worked for more than a year to help resolve these problems. In 2008, DTC, with the approval of the Securities and Exchange Commission,



implemented several major initiatives to improve the timeliness of P&I payments, including issuing the report card for the six largest paying agents – The Bank of New York Mellon, Citibank, Deutsche Bank, LaSalle NB, U.S. Bank and Wells Fargo.

"The report card was not a new idea," said Gleeson.

"We had issued reports for the leading agents for several years, but it was for their eyes only; they could see numbers on their own individual performance and how they compared to their peers, but could not identify by name the performance of the other agents."

The task force, including the agents, decided to open the report card to the industry and DTC posted it on its Web page for the first time in March 2008. The result? "Everybody has improved their performance," said Gleeson.

## Introducing Six Sigma

The report card measures the agents' performance on the timely reporting of rate information as well as the accuracy of that information. DTC took the report card a step further and introduced Six Sigma metrics to help measure the performance of each agent and of DTC, in order to provide a comprehensive view of the process.

**The report card is a major initiative helping the industry solve processing problems in structured securities by tracking the performance of the leading paying agents on a monthly basis. It measures the agents' performance on the timely reporting of rate information as well as the accuracy of that information.**

Six Sigma methodology emphasizes a metrics-driven set of quality management tools that strive to deliver world-class performance and reliability. Using industry statistics based on historical data and in accord with the agents, DTC developed Sigma targets for the industry, according to William Scotto, DTCC director, Business Reengineering and Quality.

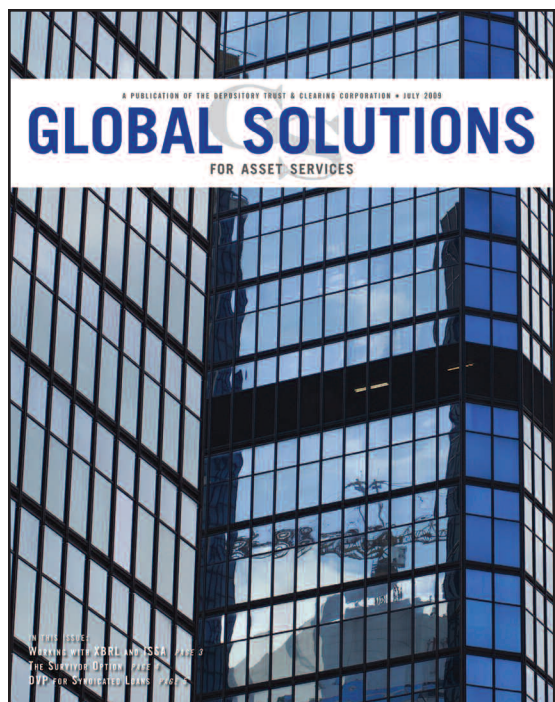
## Surpassing goals

"Working with the agents and using customer-centric metrics, we developed targets for each paying agent," said Scotto. The result was a dramatic improvement on the part of all the agents. "Every agent is surpassing its goals, and the entire structured securities industry is benefiting," Scotto added.

In the past, late or missing rates on "pay date minus one" – paying agents are supposed to submit payment rate information

[continued on page 12]

# Asset Services Introduces New Customer Publication



DTCC has introduced a new customer publication called Global Solutions for Asset Services that will keep clients up to date on the array of products and services offered by the Asset Services group, as well as covering industry-wide events and trends.

“With everything that’s going on in the industry today,” said Patrick Kirby, DTCC managing director, Asset Services, “and with companies looking for new ways to cut costs, reduce risk and boost efficiencies, we

thought it was important to keep our customers informed about a variety of topics important to their businesses, including industry news, regulatory requirements,

strategic initiatives at DTCC, and new products and enhancements developed by the Asset Services group.

“That’s why we decided to publish a single newsletter to reach out to all our Assets Services customers. We hope this publication will become a resource for our clients,” Kirby added.

Global Solutions for Asset Services will be published on a quarterly basis with the first issues distributed in July 2009. If you wish to subscribe, send an email to [assetservices@dtcc.com](mailto:assetservices@dtcc.com). @

## Report Card *Continued from page 11*

one business day prior to the payable date – amounted to 15% of all payable rates. “The goal for 2008 was to reduce this to 12%. But since October 2008, we have cut the average late or missing rate to just over 4%, a full 11 percentage points from the previous rate,” said Gleeson, “with the past two months averaging just over 2%.”

At the same time, the percentage of missing rates on payable date at 3 p.m. dropped by more than 87%, from 1.75% in January 2008 to below 0.22 % in May 2009.

Structured securities are collateralized mortgage obligations (CMOs) and asset-backed securities (ABS) are essentially bonds or notes backed by a pool of mortgage loans for CMOs and loan payments such as credit cards and auto loans for ABS. While new structured securities issues coming to market have dropped substantially since the current economic crisis began, DTC continues to pay out more than \$45 billion a month for an estimated 150,000 P&I payments.

### More metrics for Asset Services

“Based on the success of structured securities, we applied Six Sigma standards to our other business lines in Asset Services and will soon be publishing them on an industry-wide basis as well,” Scotto said.

Metrics and Sigma levels will be published, by agent, underwriter and data provider, for Underwriting, Dividend Announcements, Cash Processing, Redemptions, Reorganization Announcements, Reorganization Processing and Global Corporate Actions. @



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

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@dtcc is published by Corporate Communications and available online at [www.dtcc.com](http://www.dtcc.com) under News Center.

Stuart Z. Goldstein  
Managing Director

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Editor

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Printed by  
DTCC Print Department

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