DTCC | *Important Notice*
The Depository Trust Company

B #:	1348-14
Date:	July 7, 2014
To:	All Clients
Category:	Settlement
From:	Settlement Product Management
Attention:	Managing Directors/Vice Presidents/Managers
Subject:	Settlement Matching – Phase 3 Client Considerations

Since officially announcing the Settlement Matching initiative in November, 2012, DTC has worked closely with the industry to design an implementation plan that strikes a balance between mitigating implementation risk, improving intraday settlement finality and removing risks inherent with reclaims. On the night of July 10, 2014, subject to SEC approval, at approximately 5:00 p.m., DTC will begin its implementation of Phase 3 by reducing its receiver authorized delivery (RAD) default limits to $100,000 for Deliver Orders and $0 for Payment Orders. These new limits will be effective for any non-ID receives[1], including those staged for night cycle processing on July 10 that are due to settle on July 11.

The impact to your firm's RAD volumes depends on the RAD limits used by your firm. Clients are advised to review their current RAD limits to determine whether changes are needed. Below are some guidelines to consider:

- If your firm uses DTC's default limits and you want to continue with this practice, no changes are required. DTC will begin to apply receives in excess of the new limits to receiver authorization.
- If your firm uses DTC's default limits and you want your RAD limits to remain at their current levels ($7,500,000 for deliver orders and $500,000 for payment orders), you will need to establish global limits for these amounts. This option will keep your firm's RAD volumes at their present levels.
- If your firm has defined their own RAD limits (global or bilateral) and you want DTC to continue to route receives to RAD based on these limits, no action is required. This option will keep your firm's RAD volumes at their present levels.

It is important to note that regardless of the limits used by your firm, reclaims above DTC's default RAD limits will no longer override DTC's risk management controls and will be subject to the receiver's RAD approval.

The remainder of this notice highlights some "Day 1" considerations for **managing potential RAD volume increases and managing inventory for higher priority deliveries**. Clients are advised to consider the impact of potential increases to their RAD volumes and take appropriate measures to ensure the timely intraday authorizations of receives in order to promote system wide throughput levels. Clients should also consider the impact that receiver authorization may have on their current recycle logic as the receiver approval requirement in RAD may remove a deliverer's ability to control the order in which their pending deliveries are attempted for settlement.

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[1] DTC's threshold for Omgeo's affirmed Institutional Delivery (IMS Transaction type of "MITS") receives will not be lowered until phase 4 which is currently targeted for Q1 2015.
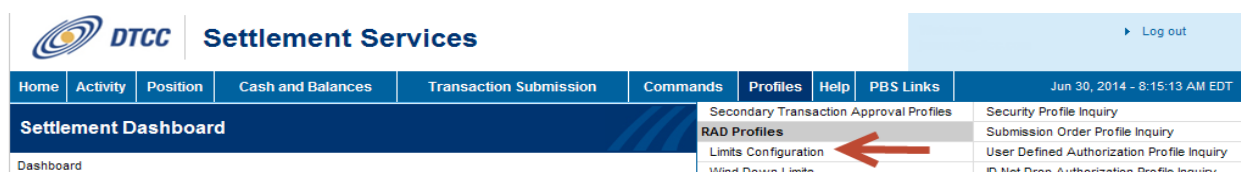
Managing Potential RAD Volume Increases:

DTC has strongly recommended RAD automation as industry best practice in advance of the phase 3 implementation, but recognizes that RAD automation is not a viable solution for all and that many clients will elect to manage increased RAD volumes by maintaining their own RAD limits, providing manual updates or a combination of the two. Clients experiencing difficulty with managing increased RAD volumes as DTC's RAD limits are lowered should consider the following as processing options.
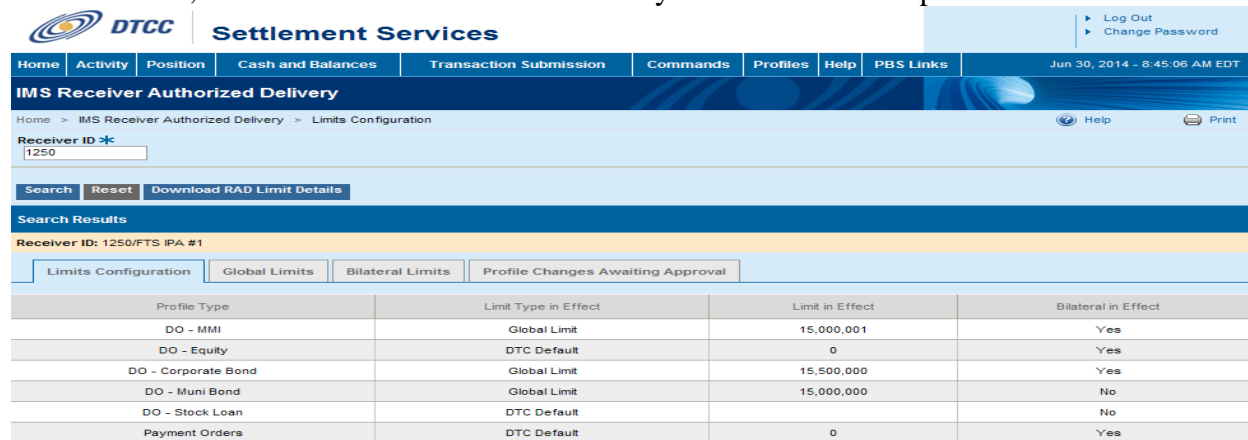
Create your own RAD Limits:

- Bilateral and Global Limits: Client defined RAD limits may be set on a global or bilateral level. Global limits allow the receiver to set a single value that is applied across all deliverers. Global limits are often used by clients to control their RAD volumes as only receives in excess of these global limits are subjected to receiver authorization. Bilateral limits allow the receiver to set a single value that is applied to a specific deliverer. Bilateral limits are often used for clients with transactions between related accounts. Both limit types, global and bilateral, may be used in conjunction with each other allowing for more flexibility and greater control over which transactions get routed to your RAD. Clients may set their limits to a level below DTC's current RAD default limit at any time, but are reminded that DTC will not apply those limits until they become greater than DTC's default limits.
- Stock Lending Profile: Stock lending arrangements are typically agreed upon the same morning as the transaction occurs and carry an extremely low reclaim rate. Because of this, and at the request of the industry, DTC created RAD limits specific to stock lending. Clients may create bilateral and/or global RAD stock lending limits. Applicable reason codes include 10, 20, 220, 230, 260, 270, 280, 290, 600, 610, 630, 640, 704 and 706. Creating limits specific to your stock lending activity is recommended for those clients that are not interested in subjecting their previously agreed upon stock lending activity under a certain settlement value to RAD.

Clients may view or modify existing RAD profiles or create new RAD profiles in the Settlement Web. The functionality is located under the profile tab of the navigation bar and can be accessed by selecting the "Limits Configuration" option from the drop down.

Once selected, clients will be able view and modify their current RAD profiles.

Profile Type	Limit Type in Effect	Limit in Effect	Bilateral in Effect
DO – MMI	Global Limit	15,000,001	Yes
DO – Equity	DTC Default	0	Yes
DO – Corporate Bond	Global Limit	15,500,000	Yes
DO – Muni Bond	Global Limit	15,000,000	No
DO – Stock Loan	DTC Default		No
Payment Orders	DTC Default	0	Yes

It is important to note that profile changes require secondary approval prior to becoming active, but once approved they become effective immediately. Clients may find an intraday adjustment to their RAD profiles useful if they find themselves with greater than expected RAD volumes. The changes to the profile limits are not retroactive, but they will be leveraged to determine whether future receives are routed to your RAD.

Manual Processing Enhancements:
DTC has made several key changes to its RAD processing to assist manual users with processing additional RAD volumes. Below is a list of these key enhancements:

- Allowing for earlier RAD updates: Prior to this initiative, the earliest clients were able to manually process RAD updates for their NDO receives was approximately 9:00 p.m. on S-1. DTC has since expanded its processing windows to allow clients additional time to manage increased RAD volumes and now accepts manual updates as early as 5:00 p.m. on S-1. DTC strongly recommends that clients take advantage of the additional processing time to approve receives as early as possible and in advance of the start of DTC's night cycle. Earlier updates will greatly help maintain settlement throughput levels, reduce costs in some cases and allow clients to address NDO receives separately, and in advance of, day cycle RAD processing.
- Processing multiple updates per submission: There are two "Display Types" within RAD from which updates may be submitted - "List" and "Grid".
  - The list display type has been modified to allow for multiple approvals, cancels and/or reversal updates per submission. Clients may submit updates for as many as 20 transactions per submission.
  - The grid display type allows clients to isolated applicable RAD items via the search engine then submit either a bulk approval or bulk reversal; bulk cancellations are not allowed. Clients may submit updates for as many as 2,000 transactions per submission by selecting the "CMD" button once records have been isolated.

List View:

Grid View:

- Providing increased transparency: DTC now provides an option to view the comments linked to a RAD transaction. Clients selecting the "Activity w/Comments Lens" option in either the list or grid display type will be able to see the comments linked to the RAD item "up front" as opposed having to select each individual item before seeing the comments.

Managing Inventory for Higher Priority Deliveries:

Historically DTC has leveraged a deliverer - based settlement model allowing most deliveries to be processed against receiver accounts without prior receiver notification. This process is changing as DTC continues to subject more, and eventually all, valued deliveries to receiver approval prior to settlement (Settlement Matching). While Matching will effectively eliminate risks inherent with reclaims and improve intraday finality for DTC settlement, it may mean less control for deliverers over their inventory, specifically recycling deliveries.

DTC continually recycles pending deliveries throughout the day. The order in which these pending deliveries are attempted depends upon which of the three recycle order logic options your firm has chosen. Clients may select;

1. DTC's default recycle order: Recycles deliveries in a prescribed order based on transaction type and settlement value.
2. First-In-First-Out: (FIFO) processing recycles deliveries in the order received by the client.
3. IMS Recycle Order Profile: Clients are allowed to create a profile in DTC's Inventory Management Service (IMS) that supersedes DTC's default order in favor of the client defined order.

DTC's default order recycle logic and FIFO processing are not changing and will continue to be supported. However, it is important to note that **DTC's default order recycle logic or clients FIFO instructions do not consider RAD transactions when assigning a priority and, with Settlement Matching, all receives will be subjected to receiver approval in RAD prior to settlement.** It is this approval requirement in RAD that may remove a deliverer's control over the recycling order, i.e., transactions awaiting approval in RAD are not submitted for further processing until approved by the receiver and therefore not considered in the recycle algorithms.

To illustrate the point, assume broker ABC, who uses DTC's default logic, has two deliveries for 100 shares of the same CUSIP but does not currently have sufficient position to complete either of the deliveries. Delivery #1 is a higher priority to broker ABC than Delivery #2 and both deliveries are awaiting RAD approval from the receiver. If the receiving broker for Delivery #2 approves the receive in RAD before the receiving broker for Delivery #1 provides their approval, broker ABC will run the risk of completing Delivery #2 (the lower priority) prior to Delivery #1 (the higher priority) should position become available intraday. DTC urges clients who continue to leverage DTC's default logic or FIFO processing to consider the potential impact of optimizing their deliveries going to RAD before settlement.

Clients wanting to maintain control over the order that recycled transactions are attempted in DTC's settlement system should strongly consider establishing an IMS Recycle Order Profile. In addition to allowing clients to define their own recycle order (or even mirror that of DTC's existing recycle order) IMS profiles **WILL** consider RAD transactions before assigning a recycling priority. This means that in the example above, DTC would have maintained broker ABC's priority for Delivery #1 and reserved the intraday shares received for broker ABC's higher priority delivery until such time when;

1. The receiving broker for Delivery #1 approved the receive from RAD
2. Broker ABC elevated Delivery #2 to a higher priority by releasing it from the IMS logic
3. The daily IMS "release time" when DTC systemically releases all recycling transactions from the client defined IMS logic and attempts to maximize inventory and complete all possible deliveries.

Clients are encouraged to apply the simple example above to scenarios where multiple deliveries exist for the same CUSIP and the order of completion is important. Special Considerations should be given to areas like syndicate processing or fail management. Recycling priorities within IMS may be customized on varying levels, including;

- Asset Class: Define for an individual asset class (Equity, Corporate Bond, Municipal Bond or Money Market Instrument) or across all asset classes.
- Activity Code: Prioritize by activity code, e.g., process my IPO deliveries (activity code 47, 48 or 49) before my "regular" deliver orders (activity code 26), and process my CNS delivery orders first or last.
- Transaction Type: Assign the return of an erroneously processed receive ("reclaims") prior to a new deliver order.
- Sort Order: Further granularity is available by selecting your desired sort order, e.g., largest quantity first, highest settlement value first or oldest settlement date first.

DTC's charges $0.04 per transaction processed that override DTC's existing default order, i.e., DTC will not charge the fee if the IMS recycle priority is the same as DTC's default order priority. Clients interested in receiving additional information about controlling the order their deliveries recycle and eventually complete should contact their RM or the Client Account Representative Team at 212-855-4270, option 2 or rmsupport@dtcc.com.