

SECURITIES AND EXCHANGE COMMISSION  
(Release No. 34-81871; File No. SR-DTC-2017-018)

October 13, 2017

Self-Regulatory Organizations; The Depository Trust Company; Notice of Filing and Immediate Effectiveness of Proposed Rule Change to Amend the DTC Distributions Guide Relating to Announcements and Tax Treatment of Certain Corporate Action Events and to Amend the DTC Fee Schedule

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (“Act”),<sup>1</sup> and Rule 19b-4 thereunder,<sup>2</sup> notice is hereby given that on October 2, 2017, The Depository Trust Company (“DTC”) filed with the Securities and Exchange Commission (“Commission”) the proposed rule change as described in Items I, II and III below, which Items have been prepared by the clearing agency. DTC filed the proposed rule change pursuant to Section 19(b)(3)(A) of the Act<sup>3</sup> and Rules 19b-4(f)(2) and (f)(4) thereunder.<sup>4</sup> The Commission is publishing this notice to solicit comments on the proposed rule change from interested persons.

I. Clearing Agency’s Statement of the Terms of Substance of the Proposed Rule Change

The proposed rule change<sup>5</sup> would (i) revise the Distributions Guide to (A) enhance the DTC Announcements feature (“Announcements”) within the DTC

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<sup>1</sup> 15 U.S.C. 78s(b)(1).

<sup>2</sup> 17 CFR 240.19b-4.

<sup>3</sup> 15 U.S.C. 78s(b)(3)(A).

<sup>4</sup> 17 CFR 240.19b-4(f)(2) and (f)(4).

<sup>5</sup> Each capitalized term not otherwise defined herein has its respective meaning as set forth in the Rules, By-Laws and Organization Certificate of DTC (the “DTC Rules”), available at <http://www.dtcc.com/legal/rules-and-procedures.aspx> and the DTC Distributions Service Guide (“Distributions Guide”), available at

Distributions Service (“Distributions Service”)<sup>6</sup> by adding new corporate action events that do not involve the payment of funds or distribution of Securities through DTC, but which may result in a taxable event for holders (“Tax Event”), as a type of distribution covered by Announcements (“Distribution Event”)<sup>7</sup> and (B) make technical and conforming changes relating to U.S. tax withholding and information reporting performed by DTC with respect to Tax Events; and (ii) add a fee relating to the announcement of Tax Events (“New Fee”) to the DTC Fee Schedule (“Fee Schedule”),<sup>8</sup> as discussed below.

II. Clearing Agency’s Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

In its filing with the Commission, the clearing agency included statements concerning the purpose of and basis for the proposed rule change and discussed any comments it received on the proposed rule change. The text of these statements may be examined at the places specified in Item IV below. The clearing agency has prepared summaries, set forth in sections A, B, and C below, of the most significant aspects of such statements.

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<http://www.dtcc.com/~media/Files/Downloads/legal/service-guides/Service%20Guide%20Distributions.pdf>.

<sup>6</sup> The Distributions Service includes DTC’s announcement, collection, allocation and reporting of dividend, interest and certain principal payments on behalf of Participants holding Securities at DTC. See Distributions Guide, supra note 1 at 9.

<sup>7</sup> Distribution Events covered by Announcements include cash dividends, interest, principal, capital gains, sale of rights on American depository receipts, return of capital, dividend with option, stock splits, stock dividends, automatic dividend reinvestments, spinoffs, rights distributions, pay in kind, and liquidation. Distributions Guide, supra note 1 at 12.

<sup>8</sup> Available at <http://www.dtcc.com/~media/Files/Downloads/legal/fee-guides/dtcfeeguide.pdf?la=en>.

(A) Clearing Agency’s Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

1. Purpose

The proposed rule change would (i) revise the Distributions Guide to (A) enhance Announcements by adding Tax Events as a Distribution Event and (B) make technical and conforming changes relating to U.S. tax withholding and information reporting performed by DTC with respect to Tax Events; and (ii) add the New Fee to the Fee Schedule, as discussed below.

A. Distributions Service Announcements Feature

The Distributions Service includes the announcement, collection, allocation and reporting by DTC, on behalf of its Participants, of dividend, interest and principal payments for Eligible Securities held by Participants at DTC. This centralized processing provides efficiency for Participants for their receipt of (i) payment information and (ii) payments on Distribution Events, from multiple issuers and agents.<sup>9</sup> In this regard, Announcements provides Participants with information pertaining to their record date (“Record Date”)<sup>10</sup> positions for Distribution Events.<sup>11</sup> This information facilitates Participants’ ability to reconcile their records with DTC before the payable date (“Payable Date”).<sup>12</sup>

B. Internal Revenue Code Section 305(c)

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<sup>9</sup> See Distributions Guide, supra note 5 at 9.

<sup>10</sup> The Record Date is the date set by an issuer of a security by which an investor must own the security in order to be eligible to receive an upcoming distribution.

<sup>11</sup> See Distributions Guide, supra note 5 at 11-13.

<sup>12</sup> The Payable Date is a date established by an issuer on which a distribution to holders will be paid by the issuer.

Section 305(c) of the Internal Revenue Code<sup>13</sup> (“Section 305(c)”) states that holders of convertible securities may be deemed to have received a dividend because of a corporate action on common stock into which the convertible security may be converted.<sup>14</sup>

In the most frequent scenario relevant to Distribution Events, an issuer that pays a cash dividend to its shareholders may trigger an increase to the conversion rate (“Convertible Rate Adjustment”)<sup>15</sup> on a convertible debt Security. Under Section 305(c), this Convertible Rate Adjustment is considered as a deemed distribution.<sup>16</sup> This deemed distribution under Section 305(c)<sup>17</sup> may be subject to tax reporting by Participants, and if the convertible debt Securities are held by non-U.S. persons, the appropriate tax withholding.

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<sup>13</sup> 26 U.S.C. 305(c).

<sup>14</sup> Under Section 305(c), a change in the conversion ratio or conversion price or a similar transaction is treated "as a distribution [by the issuer] with respect to any shareholder whose proportionate interest in the earnings and profits or assets of the corporation is increased by such change." Id.

<sup>15</sup> Such a convertible debt Security provides for a Conversion Rate Adjustment so that the conversion rate is changed if a distribution is made on the issuer's common stock. Generally, the primary purpose of a Convertible Rate Adjustment is to prevent the holder of a convertible debt Security from being diluted upon a distribution to the shareholders by adjusting the conversion rate on the stock to increase the number of shares that the debt holder can obtain in a conversion of the bond to shares of the issuer.

<sup>16</sup> Such a distribution based on dividend payments made to common shareholders will be considered to be deemed distribution to bondholders even before the bondholders convert the debt to equity.

<sup>17</sup> Supra note 14.

In April 2016, the U.S. Treasury released proposed regulations to provide guidance to financial institutions regarding their withholding and reporting obligations.<sup>18</sup> The regulations also require issuers of convertible securities to provide the amount and the timing of deemed distributions under Section 305(c) to the holders of convertible securities, i.e., DTC. Despite this reporting requirement, holders may not be directly informed of changes that have occurred in the instrument's conversion ratio or the amount of the resulting "deemed" distribution that may result in a tax withholding obligation for them. A lack of information relating to these deemed distributions and other Tax Events may affect Participants' ability to comply with applicable Federal tax withholding requirements and applicable DTC Rules requirements relating to the use of DTC services.<sup>19</sup>

#### C. Proposed Enhancement to Announcements Feature

Pursuant to the proposed rule change, in order to facilitate Participants' ability to comply with the requirements described above, DTC would revise the Distributions Guide to allow it to source information on Section 305(c) deemed distributions and other Tax Events for Securities on Deposit at DTC directly from issuers, and then provide the Tax Event information to Participants. DTC would distribute the Tax Event information for a deemed distribution in the same standardized manner that DTC uses to announce distributions. In this regard, DTC would revise the text of the Distributions Guide to (i)

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<sup>18</sup> IRS-2016-0016-0001. 81 FR 21795 (April 13, 2016) (REG-133673-15).

<sup>19</sup> In connection with their use of DTC's services, Participants must comply with all applicable laws, including, but not limited to all applicable laws relating to taxation. See Rule 2, Section 8, supra note 5.

add Tax Events as a Distribution Event covered by the functionality described in the Distributions Guide and (ii) add a new section titled “Tax Event Announcements” to (a) describe and define Tax Events and Tax Event Announcements and (b) describe the systemic data fields (“Fields”) that DTC would use to provide relevant Tax Event information for a Security to Participants, including: (1) “Event Type” to be shown as “Tax Event,” (2) “Sub Event Type,” which would be used to classify the type of Tax Event, (3) Payable Date, (4) Record Date, (5) “Cash Rate,” to provide the amount of the deemed distribution, and (6) “Comments,” which would be used to provide any other pertinent information regarding the Tax Event.

D. Proposed New Fee

Pursuant to the Fee Schedule, DTC charges fees to Participants for the processing of corporate action events. Fees are established to offset the cost of processing all aspects of the applicable corporate action event, including the announcement processing, the actual processing of payments, and book-entries associated with the corporate action. Pursuant to the proposed rule change, the Fee Schedule would be revised so that a Participant that holds Securities subject to a Tax Event would be charged flat fee of \$40 per announcement. The proposed New Fee would align DTC’s revenue with costs for retrieving Tax Event information from issuers and announcing that information to Participants, as proposed. The New Fee would be added to the Fee Schedule underneath the heading for U.S. Tax Withholding, which is a feature of the Distributions Service, for reference purposes so that it would be located on the Fee Schedule in the same place as other fees charged for tax-related processing performed by DTC.

E. Processing of Tax Withholding and Information Reporting

DTC performs adjustments for entitlement and allocation activity that is outside of traditional pay date allocations. This includes activity tracking for stock loans, repos, and due bill fail tracking.<sup>20</sup> With respect to tax treatment of such adjustments, currently the text of the Distributions Guide refers to DTC's performance of U.S. tax withholding and information reporting for credit adjustments that occur with respect to Participant positions in their DTC accounts.<sup>21</sup> The proposed rule change would modify the applicable text with respect to the tax treatment described within the Due Bill Fail Tracking System, Stock Loan Income Tracking System and Repurchase Agreement (REPO) Tracking System subsections of the Adjustments Section of the Distributions Guide, to state that such withholding and reporting would also be performed related to Tax Events.

F. Implementation Timeframe

The proposed rule change would be implemented on October 2, 2017.

2. Statutory Basis

DTC believes that the proposed rule change is consistent with the requirements of the Act, and the rules and regulations thereunder applicable to DTC, in particular Sections 17A(b)(3)(D)<sup>22</sup> and 17A(b)(3)(F)<sup>23</sup> of the Act.

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<sup>20</sup> See Distributions Guide, supra note 5 at 32.

<sup>21</sup> Id. at 34, 36, and 37

<sup>22</sup> 15 U.S.C. 78q-1(b)(3)(D).

<sup>23</sup> 15 U.S.C. 78q-1(b)(3)(F).

Section 17A(b)(3)(D) of the Act<sup>24</sup> requires that the rules of the clearing agency provide for the equitable allocation of reasonable dues, fees, and other charges among its participants. DTC believes that the proposed New Fee would be equitably allocated among Participants because each Participant holding Securities subject to Tax Events would be charged the same New Fee amount per Announcement. DTC believes that the proposed New Fee would be reasonable because it would allow DTC to align its revenue with its costs of providing important Tax Event information through Announcements to Participants, which information is needed by them to facilitate their compliance with applicable tax withholding obligations, as described above. Therefore, DTC believes that the proposed rule change is consistent with Section 17A(b)(3)(D) of the Act, cited above.

Section 17A(b)(3)(F) of the Act<sup>25</sup> requires, inter alia, that the rules of the clearing agency be designed to promote the prompt and accurate clearance and settlement of securities transactions.<sup>26</sup> As described above, the proposed rule change would enhance the Distributions Service to include the distribution of Announcements for Tax Events to Participants. As described above, by providing for the distribution of Tax Event information to Participants, the proposed rule change would facilitate Participants' ability to comply with their Federal tax withholding obligations. This would further facilitate Participant's ability to continue to maintain Eligible Securities subject to Tax Events on Deposit at DTC and make use of DTC's book-entry transfer and settlement services with respect to those Securities, in accordance with DTC Rules requirements relating to the

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<sup>24</sup> Supra note 22.

<sup>25</sup> Supra note 23.

<sup>26</sup> 15 U.S.C. 78q-1(b)(3)(F).



use of DTC services by Participants.<sup>27</sup> Therefore, by facilitating Participant's ability to continue to use DTC's book-entry transfer and settlement services at DTC with respect to Eligible Securities that are subject to Tax Events, the proposed rule change would promote the prompt and accurate clearance and settlement of securities transactions, consistent with the requirements of the Act, in particular Section 17A(b)(3)(F) of the Act, cited above.

Section 17A(b)(3)(F) of the Act<sup>28</sup> requires, inter alia, that the rules of the clearing agency be designed to promote the prompt and accurate clearance and settlement of securities transactions.<sup>29</sup> As described above, the proposed rule change would enhance the Distributions Service to include the distribution of Announcements for Tax Events to Participants. As described above, by providing for the distribution of Tax Event information to Participants, the proposed rule change would facilitate Participants' ability to comply with their Federal tax withholding obligations. This would further facilitate Participant's ability to continue to maintain Eligible Securities subject to Tax Events on Deposit at DTC and make use of DTC's book-entry transfer and settlement services with respect to those Securities. Therefore, by facilitating Participant's ability use DTC's book-entry transfer and settlement services at DTC with respect to Eligible Securities that are subject to Tax Events, the proposed rule change would promote the prompt and accurate clearance and settlement of securities transactions, consistent with the requirements of the Act, in particular Section 17A(b)(3)(F) of the Act, cited above.

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<sup>27</sup> See supra note 19.

<sup>28</sup> Supra note 23.

<sup>29</sup> 15 U.S.C. 78q-1(b)(3)(F).

(B) Clearing Agency's Statement on Burden on Competition

DTC does not believe that the proposed rule change proposing to amend the Distributions Guide to provide for the announcement of Tax Events would have any impact, or impose any burden, on competition, because the information that would be provided to Participants in this regard is necessary for Participants to receive in order to be able to accurately perform tax accounting for their positions held at DTC, and maintain compliance with their tax withholding requirements, as described above. The addition of the New Fee could have an impact on competition because only those Participants that hold Securities subject to Tax Events would be charged the New Fee. To the extent the proposed rule change to add the New Fee to the Fee Schedule would provide for a burden on competition, DTC believes it would be necessary and appropriate under the Act because the New Fee is required to cover the cost of providing the Tax Event information to Participants, which information is necessary for Participants to receive in order to facilitate their compliance with their tax withholding obligations.

(C) Clearing Agency's Statement on Comments on the Proposed Rule Change Received from Members, Participants, or Others

DTC has not received or solicited any written comments relating to this proposal. DTC will notify the Commission of any written comments received by DTC.

III. Date of Effectiveness of the Proposed Rule Change, and Timing for Commission Action

The foregoing rule change has become effective pursuant to Section 19(b)(3)(A) of the Act<sup>30</sup> and paragraph (f) of Rule 19b-4 thereunder.<sup>31</sup> At any time within 60 days of the filing of the proposed rule change, the Commission summarily may temporarily suspend such rule change if it appears to the Commission that such action is necessary or appropriate in the public interest, for the protection of investors, or otherwise in furtherance of the purposes of the Act.

IV. Solicitation of Comments

Interested persons are invited to submit written data, views and arguments concerning the foregoing, including whether the proposed rule change is consistent with the Act. Comments may be submitted by any of the following methods:

Electronic Comments:

- Use the Commission's Internet comment form (<http://www.sec.gov/rules/sro.shtml>); or
- Send an e-mail to [rule-comments@sec.gov](mailto:rule-comments@sec.gov). Please include File Number SR-DTC-2017-018 on the subject line.

Paper Comments:

- Send paper comments in triplicate to Secretary, Securities and Exchange Commission, 100 F Street, NE, Washington, DC 20549.

All submissions should refer to File Number SR-DTC-2017-018. This file number should be included on the subject line if e-mail is used. To help the Commission process

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<sup>30</sup> 15 U.S.C. 78s(b)(3)(A).

<sup>31</sup> 17 CFR 240.19b-4(f).

and review your comments more efficiently, please use only one method. The Commission will post all comments on the Commission's Internet website (<http://www.sec.gov/rules/sro.shtml>). Copies of the submission, all subsequent amendments, all written statements with respect to the proposed rule change that are filed with the Commission, and all written communications relating to the proposed rule change between the Commission and any person, other than those that may be withheld from the public in accordance with the provisions of 5 U.S.C. 552, will be available for website viewing and printing in the Commission's Public Reference Room, 100 F Street, NE, Washington, DC 20549 on official business days between the hours of 10:00 a.m. and 3:00 p.m. Copies of the filing also will be available for inspection and copying at the principal office of DTC and on DTCC's website (<http://dtcc.com/legal/sec-rule-filings.aspx>). All comments received will be posted without change; the Commission does not edit personal identifying information from submissions. You should submit only information that you wish to make available publicly. All submissions should refer to File Number SR-DTC-2017-018 and should be submitted on or before [insert date 21 days from publication in the Federal Register].

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.<sup>32</sup>

Eduardo A. Aleman  
Assistant Secretary

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<sup>32</sup> 17 CFR 200.30-3(a)(12).