

Operations up close

Ben Roberts catches up with Rupert Perry, director at Pirum Systems, to discuss the move towards billing automation, contract compare and ISLA's best practice paper.

1. Last year ISLA finalised its best practice paper for billing reporting. Does this support Pirum's promotion of automated standards in the post trade space?

It does. ISLA's best practices sub group includes some of the operations profes-

sionals who are most active in pushing the whole industry forward towards using processes that provide both more efficient processing and greater control. The most recent best practice paper essentially sets out a standardised data format for securities lending bills which permits the bills to be more easily transmitted electronically between par-

ticipants and thus handled / reconciled automatically. When bills are reconciled automatically, they are processed more efficiently and this facilitates timely settlement of the bills.

2. What near term effect might best practice standards have on the market?

The best practice standards are aspirational in that they provide an agreed "best practice" for the topic in question. Whilst not everyone is able to operate in full compliance with all of the best practices today, the papers give good 'ammunition' to operations people – and indeed the management – to make the case for upgrading the systems that

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are processing their securities lending and borrowing, so that they do operate in accordance with best practice in future. The idea is that over time the whole industry's operational processes will converge on best practice, ultimately providing more efficient and controlled processing for everyone, with fewer exceptions to be handled / investigated by hand.

3. What are the key discrepancies between counterparties that have spurred the need for common standards?

Differences in positions (i.e. disagree-



Rupert Perry

ments over exactly how many shares have been lent) are probably the most important discrepancy, as although genuine positional differences are rare, they are potentially extremely expensive.

Recently, we helped a borrower and lender resolve a positional difference where a borrower attempted to return

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shares which the lender did not believe they had on loan with them.

It turned out that the lender had mistakenly booked a previous return by another borrower to the trade in question, which explained why the lender did not think the shares were still on loan.

In other words, the lender had no record of the shares on loan to the first borrower, whilst they thought they had shares on loan to the second Borrower, when in fact they had already returned them.

Automated contract compare was the key tool which enabled us to quickly identify what really happened in this case. Regular use of automated contract compare is probably ISLA's most important best practice recommendation.

This is because effective use of contract compare every day ensures your positions are correct, which is fundamental to calculating counterparty exposure correctly. Accurate positions are also the foundation to the smooth operation of all other downstream processes (e.g. billing, mark to market, returns, corporate actions etc.), as any positional differences will otherwise cause exceptions in each of these areas, requiring more manual intervention to deal with them.

Another example would be something like the mark to market best practice.

You have to choose when prices on stocks are taken – whether, for example, it is the price at close of markets yesterday or today.

This is an issue commonly encountered in Europe when deciding what prices are appropriate to be used for valuing Asian securities. ISLA's mark to market best practice standard says it is today's close of business price that should be used for Asian securities.

It's important to have a common standard, as otherwise both parties will try to mark their positions to differing prices and this inevitably causes more exceptions which require manual investigation when the two parties try to agree the mark that will actually be processed.

4. Might clarity around standards and transparency improve regulator's understanding and view of securities lending?

Regulators want participants to operate in a controlled environment where they know and manage their exposures correctly. If you run your business in compliance with ISLA's best practice recommendations this undoubtedly helps demonstrate to them that operational risk is being properly controlled.

Having accurate records around open contracts is particularly important when it comes to, for example, understanding your full exposure to Lehman Brothers at the time of the bank's collapse.

5. How far is the industry towards automation?

It generally depends on the size of the firm and whether they are using a vendor package or an in-house developed solution for their books and records.

Market participants using vendor packages often find it easier to adopt industry automation, as the vendor will often develop the necessary file extracts and imports just once for all customers.

Those who are using in-house solutions (especially the older and more mature ones) often find it harder to use

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the available industry automation, as they have to develop the required data feeds themselves.

All other things being equal, generally the larger players use more industry automation than the smaller players. However, when that number of open loans is very small, it is possible to get by without using much automation, but it has to be put in place to allow volumes to rise.

One interesting development that we've seen is that some securities lending firms are assessing counterparties along the lines of the standard of their automation. It's a relationship-based business of course, but equally if a bank knows that their counterparty has automation for post trade systems such as billing and contract compare it is going to be a lot more attractive to do business with – particularly as minimising operational risk is top of the agenda right now. ✨