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# Fund Administration

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## Post-Trade

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## Proxy Process

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## HKMA supports Hong Kong-China funds agreement

The Hong Kong Monetary Authority (HKMA) has welcomed a mutual recognition funds agreement between Hong Kong and China, announced by the Securities and Futures Commission and the China Securities Regulatory Commission.

The agreement means the client base of Hong Kong-domiciled funds will expand to include mainland China investors, while mainland funds will be available to global investors through a mutual recognition arrangement.

The move is designed to help facilitate Hong Kong's development in to a fully functional Asian asset servicing centre, and to improve links between Hong Kong and China in terms of both infrastructure and regulatory cooperation.

HKMA chief executive Norman Chan said: "For the implementation of mutual recognition of funds, the HKMA is working closely with relevant institutions on the mainland to establish an efficient fund processing platform to provide an automatic channel for cross border transactions and cash settlement. I look forward to seeing the successful implementation of the arrangement."

## Collateral is a new currency

Collateral mobility and pricing of assets are the biggest challenges for effectively managing collateral, according to a Euroclear survey.

The issues of collateral mobility and pricing were each highlighted as challenges by 35 percent of respondents, while lack of standards and dispute resolution also ranked highly, each highlighted by 25 percent of respondents.

A drive for standardisation was attributed to more focus on collateral resourcing and optimisation, but 30 percent of respondents said they still do not have an optimisation strategy in place.

Lack of automation was also identified as a challenge by 20 percent of respondents, as was regulatory change. A majority of 70 percent also considered collateral transformation to be high on their agenda.

The survey suggested that the implementation of the European Markets Infrastructure Regulation (EMIR) could have a heavy impact on collateral management function, with 65 percent of firms agreeing with this.

Jo Van de Velde, managing director and head of product management at Euroclear, said: "Many industry experts argue that collateral has become a new currency, as firms look to shore-up credit exposures from a variety of different activities while grappling with increased balance sheet pressures."

Virginie O'Shea, a senior analyst at Aite Group, added: "Regulatory reform is a driving force behind firms' current re-evaluation of their collateral management capabilities. EMIR is heightening the need for a more proactive approach to collateral, on a more frequent basis."

"Assets must be quickly identified and seamlessly transported to where they are required. This is a significant challenge, given the internal and external inefficiencies that must be overcome, and something that they are unlikely to be able to tackle on their own."

## AIFMD burden hurting European investment

Fund managers are passing up European investment opportunities in a bid to avoid the Alternative Investment Fund Managers Directive (AIFMD), according to a panel of speakers at the Guernsey Funds Forum 2015.

Tim Hames, director general of the British Private Equity and Venture Capital Association (BVCA), said Base Erosion and Profit Shifting (BEPS) provided a challenge to the future success of private equity in Europe.

"If we create a world, whether by accident or design, via the Organisation for Economic Co-operation Development (OECD) BEPS process, in which it becomes so gruesome in terms of tax treatment for investors to get involved in European private equity, then they are not going to do so, even if the returns are alpha, alpha, alpha."

He added that this is because it would be adding to the demands already being exacted on the industry by AIFMD.

Hames said that there should be one question asked: "Will this action make Europe a less or more attractive place to outside investors and observers?"

Karen Sands, head of finance at Hermes GPE, answered: "I think delivering European private equity with commingled vehicles becomes even more complex, particularly if you are marketing to investors outside of Europe."

"They are put off by AIFMD and certainly some of the discussions that we've had have been around single investor funds."

James Gee of Weil Gotshal and Manges added that AIFMD had proved more onerous for those onshore rather than third countries such as Guernsey, which was able to offer access to the EU through national private placement regimes.

Robert Mellor, tax partner at PwC, argued that Guernsey's advantage was in having a dual regulatory regime, one that is AIFMD compliant, and another free from the requirements of AIFMD.

## Renminbi number one in APAC

Renminbi is now the most active currency in the Asia Pacific region in terms of trades with China and Hong Kong, according to SWIFT's RMB tracker.

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Value in weight of the RMB used for payments exchange between the Asia Pacific and China and Hong Kong increased by 327 percent between April 2012 and April 2015.

In this time, payments of this type made in RMB increased from 7 percent of all transactions to 31 percent.

It is now the most popular currency used to do business between the Asia Pacific and China, compared to the fifth most popular in 2012.

This growth has been attributed to an increase of RMB use in Asian countries when directly trading with Hong Kong and China.

In the last three years, a majority of Asian countries have moved from being low users conducting less than 10 percent of trades in RMB, to medium users conducting between 10 and 50 percent of trades in RMB. Six countries are considered high users of RMB.

Michael Moon, SWIFT's head of payments in the Asia Pacific region, said: "The Asia Pacific is clearly paving the way forward when it comes to RMB adoption."

He added: "Big trading partners like Singapore, Taiwan and South Korea have adopted the RMB for the majority of their payments with Greater China."

RMB has also retained its place as the fifth most active currency for global payments, accounting for just over 2 percent of payments worldwide.

## Small World FS reaches £10 billion transactions

Small World FS has reached the milestone of £10 billion in transactions processed since its launch in 2006.

The business now operates the third largest payout network in the world, reaching 250,000 locations across 188 countries.

The firm has recently experienced rapid expansion with the extension of its digital services into 14 sending markets, as well as inking deals with the MTN Group and Nations Trust Bank.

Nick Day, CEO of Small World FS, commented: "This milestone is evidence that our local approach to international payments is one that resonates with our customers around the world."

## Deutsche Börse builds relationships in China

Deutsche Börse has teamed up with the Shanghai Stock Exchange and the China Financial Futures Exchange to launch a joint initiative, known as the China Europe International Exchange.

The partnership intends to develop financial instruments based on Chinese underlyings, and to market them to international investors.

Products will be offered in renminbi, thereby promoting the internationalisation of the currency.

The initial scope of the project will cover cash markets products for market launch.

The exchange is scheduled to begin market operations in Q4 2015.

Zhang Shenfeng, chairman of China Financial Futures Exchange, said: "The establishment of the RMB asset trading platform in Frankfurt by Shanghai Stock Exchange, China Financial Futures Exchange and Deutsche Börse is a milestone for Chinese exchanges and the capital market in general."

The move comes as a reaction to the rapid growth in use of the RMB worldwide, and its internationalisation as a strategy to open China's economy and financial industry. Deutsche Börse and the Shanghai Stock Exchange will each hold a 40 percent stake, and China Financial Futures Exchange will hold the remaining 20 percent.

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## Summer in the City

That's right, it's summer in the City and it's hot, hot, hot! Not just the weather—don't forget that the nights start to draw in soon—but the jobs market, too. While supply, in terms of the number of folks looking for opportunities, still currently outstrips opportunities available, there is a vibrancy in the market of a level which has not been seen for several years.

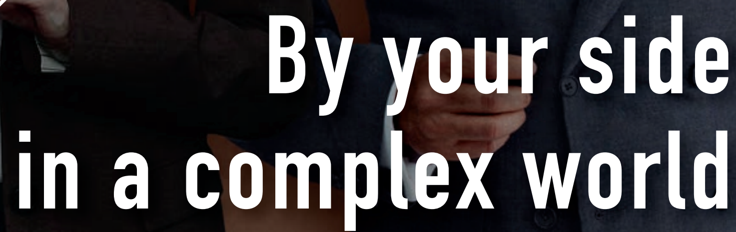
This is a reflection of improving economic conditions, an air of continued optimism coupled with a return of confidence in the near term (18 months or so), at least. Both the sell side and buy side are strong and a 'jobs merry-go-round' is in place with significant backfilling taking place. Sales are taking centre stage: there's still no substitute for having a demonstrable ability to raise revenue to get a hiring firm or manager over-excited. Sales roles currently available range from traditional, common-or-garden long-only product asset manager salespeople to middle-office outsourcing experts to alternatives specialists. In fact, the only roles that aren't available at present are 'classic' care-and-maintenance relationship managers. These have been either 'squeezed' upwards to be sales people, business developers or client executives (depending on the firm), or downwards to be account managers or client services executives. Whether this jobs rally will end at the start of summer, which is usual, or perhaps power through, which has been known, we'll only find out in a month or two.

There are a couple of events threatening to rain on certain people's parades, though. At least two major banks are considering relocating their head offices, which, while not necessarily material in terms of the transfer of job numbers, could be deemed to be the thin end of the wedge in the decline of London as a financial centre. EU referendum uncertainty might well also start to ramp up in the coming months, with a 'Brexit', perhaps added to an imminent 'Grexit', creating even more uncertainty. This, in turn, leads to a reluctance to invest and a potential stalling, or even reversal, of the positive momentum being seen now.

On the subject of heat, many heads of compliance, risk and regulation will also be feeling the heat following several significant fines for transgressing basic securities safekeeping rules. I should stress that this is absolutely no cause for schadenfreude from either competitors on the sell side or clients on the buy side. Issues such as this can cause a knee-jerk reaction and result in even more regulation being foisted upon the industry, as well as increased costs to be cascaded down to the end consumer, ie, you and me, with no discernable improvement in asset safety, job satisfaction or industry reputation.

The best cause of action I'd suggest would be not to gloat, but instead issue an immediate mea culpa if you are at fault and then demonstrably self-police to prevent recurrence. If you haven't—yet—been caught, then now is a perfect time to start checking and double-checking procedures, processes and documentation. It is far better to put your own house in order than be obliged to do it by someone with little or no real understanding of our industry.

**Paul Chapman, managing director, HornbyChapman Ltd**



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# To Singapore and beyond

## SWIFT's Fabian Vandenreydt reveals some of the discussions, themes and meetings delegates can look forward to at Sibos 2015 in glitzy Singapore

At the Sands Expo and Convention Centre, Marina Bay Sands in Singapore from 12 to 15 October, Sibos will bring together key figures from financial institutions, market infrastructures, and technology vendors to showcase the latest strategies that will help shape the future of the industry. Hosted by SWIFT, the event enables delegates to explore issues related to regulation, transparency and new payment platforms, among other industry-driven challenges.

### What are the overall themes of the sessions focused on securities at Sibos 2015?

Regulation tops the list, with transparency and reducing risk as two key areas that are having a significant impact on the securities landscape. We have five panel sessions spanning four key areas where we aim to address challenges and opportunities around account segregations, clearing and settlement, reporting obligations and shareholder identification.

We will also be running different workshops and sessions in collaboration with the Compliance, Corporates and Market Infrastructure forums as there are mutual challenges to be discussed across these areas. For example, one of the joint sessions we have in the Market Infrastructure Forum takes a look at securities market infrastructure innovation, particularly how we can bring 'real-time' to securities.

The industry is making great strides on the payments side. It will be interesting to discuss this topic more broadly and see what the securities industry can learn from that success, and how these innovative new technologies can be applied to the securities space.

### Why focus on these particular themes within regulation?

For a very long time we have been discussing potential regulations, their implications and what they meant to be a financial institution in the 'new normal'. Today, we have moved well beyond the theoretical discussions to the practical implementation of regulations with a very strong focus on transparency and reducing risk.

In the securities space, transparency seems to be more of a priority than operational efficiency. We are seeing a shift in focus from shortening settlement cycles and creating a more automated and efficient back office, towards institutions managing transparency challenges. This is such a broad challenge that we need to discuss what financial institutions need to do to ensure a proper balance between low risk and greater proficiency.

Compliance is another area that led us to focus on transparency and risk reduction. With increased use of financial sanctions globally, and regulatory pressure to maintain strong sanctions compliance capabilities, the spotlight has fallen on the securities industry. Regulators are concerned about the lack of transparency in securities intermediation, and the difficulty in establishing the beneficial ownership within securities transactions chains due to the use of omnibus accounts or nominee structures within different legal national frameworks. This poses a growing challenge for securities firms across the world, particularly those engaged in the cross-border business.

### What is the focus for SWIFT at Sibos this year?

At our exhibition stand this year, SWIFT will target key business areas including: financial crime compliance, business intelligence, reference data, and services and connectivity. Over the past year, we've expanded our capabilities in these areas and have some new products to unveil and features to highlight. Our focus at Sibos will be on fostering the discussion around transparency and reducing risk as main drivers for the industry. Throughout the week, open panels will debate on various themes such as transaction reporting obligations, shareholder identification, outsourcing risks and opportunities, collateral management and also, as mentioned before, account segregation and portability.

### Will Sibos 2015's location in Singapore be reflected in the conference agenda?

Yes, most definitely. On the Thursday, Sibos will feature an Association of Southeast Asian Nations (ASEAN) day, which will be fully dedicated to topics of importance to the ASEAN community. Also, Piyush Gupta, CEO and director of DBS Group, one of the leading financial services groups in Asia, will deliver the opening plenary address.

Developments in Asia will be an important subject, reflecting the shift from west to east. There are many key drivers supporting this growth. Asia's key cities are becoming more open markets and as a result, more banks and securities firms are looking to attract more business from that region. It is a two-way street. The local market infrastructures want to be more global, and the global banks want to support that growth.

Singapore is a great location for Sibos. It is a vibrant city-state in the heart of Asia. Singapore is the world's fourth biggest financial centre, as well as the fourth largest foreign-exchange trading centre after London, New York City, and Tokyo. The World Bank has rated Singapore the easiest place in the world to do business, and lists it as the top logistics hub.

From a business perspective, this gives SWIFT and many of the other delegates and exhibitors at Sibos the opportunity to engage with several key and potential customers in person, which can be challenging when many are based in other parts of the world.

We have a fantastic programme and will have a great line up of speakers and attendees from across the spectrum—banking, securities, corporates, and compliance.

We are very excited for Sibos 2015 and look forward to welcoming the more than 7,000 delegates that will converge on Singapore in October. **AST**

**Fabian Vandenreydt**
Head of markets management, Innotribe and the SWIFT Institute
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# T2S: making waves in liquidity management

## Edwin De Pauw of Euroclear on accessing and managing liquidity

With the start date for the European Central Bank's (ECB) Target2-Securities (T2S) settlement platform almost upon us, an important issue for market participants is how to optimise intra-day liquidity in the new European landscape. This is driven partly by new regulations, including Basel III and the European Market Infrastructure Regulation, that introduce additional capital charges for credit and liquidity consumption as well as the need for high quality collateral.

At the same time, new opportunities in T2S for firms to more efficiently manage their liquidity in Europe are gaining increased attention. For one, T2S effectively creates a new, central bank money liquidity environment.

Today, most international firms leverage a single commercial bank money liquidity pool from an agent or an international central securities depository (ICSD). In T2S, firms that wish to do so will also have the opportunity to settle their European domestic activity out of a single central bank money cash account, reducing the cost of funding.

The extent to which a shift will take place in Europe towards the use of central bank money liquidity for intra-day financing, however, will only be known after T2S is fully rolled out. What is certain is that there are ways for firms to reduce liquidity costs in both the ICSD and CSD environments while maintaining or even strengthening their access to immediate and guaranteed liquidity

Firms will need to make decisions about which environment best suits their needs, or whether they can adopt an approach that utilises the best of both worlds.

### Reducing intra-day liquidity costs

In the new T2S environment, market participants are looking for efficient intra-day and end-of-day cash management in order to reduce their credit consumption for settlement. Access to sufficient liquidity funding sources is vital to allow them to support their, and their clients', business under any market conditions.

By centralising activity in either an ICSD or CSD, the cash pooling and netting effect that can be achieved across all T2S markets will reduce credit usage and significantly increase funding opportunities. Furthermore, firms will be able to take advantage of an auto-collateralisation functionality, whereby collateral is automatically posted with the central bank to cover intra-day settlement needs across all T2S CSDs.

Cash and securities deadlines will also be optimised in T2S, enabling cash to be transferred back into the ECB's Target2 cash system as late as possible, or collateral moved between the CSD and ICSD environments.

While efficient funding support is key to liquidity management, other elements that contribute to reducing liquidity costs include high levels of settlement efficiency, access to a broad range of counterparties, instruments and central counterparties (CCPs), and real-time reporting/forecasting facilities.

### Optimising financing

From a liquidity perspective, the choice of whether to centralise post-trade activity in a CSD connected to T2S, or in an ICSD, will depend on various factors individual to each firm, such as where its counterparties are, where they can access credit and liquidity in the most cost-effective way, and how much of its activity in T2S-eligible securities is funded by liquidity from a more global activity (in euro or non-euro).

When deciding on their network strategy, however, firms not only need to consider where to hold their assets to meet their short-term liquidity needs in the most efficient way, but also asset servicing and financing.

Indeed, collateral mobilisation on a global basis is a top priority for financial institutions as regulations require them to post more collateral to finance and support their activity. In T2S, firms will be able to pool collateral either by consolidating assets in the same location where they have their settlement activity, or by using a collateral management service provider that moves the inventory of assets where it is needed for financing purposes.

The use of collateral optimisation and transformation services will then enable firms to convert the quality of collateral for onward re-use, for example, for CCP margin calls, to meet regulatory requirements and reduce their liquidity costs.

### Connecting both worlds

To access liquidity and reduce the cost of managing it, firms may be looking for a reduced number of providers through which they can pool cash for all markets, access bespoke liquidity management services and receive real-time consolidated reporting for their European and non-European activity.

In addition, collateral management services that are efficiently interconnected with T2S, such as those offered through Euroclear's Collateral Highway in both the ICSD and CSD environments, will enable firms to smoothly transfer collateral for activities both in commercial and central bank money and between their business in Europe and globally.

It is important in T2S for firms to be able to easily access financing opportunities with both domestic and international counterparties. Given Euroclear's position as an open-market infrastructure that straddles both the ICSD and CSD worlds, it will ensure seamless interoperability between the two environments so that clients can strike a balance that's right for them between running either a single, global financing book or multiple financing books, while at the same time minimising their liquidity costs. AST

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# Utility boom

## SmartStream is breaking boundaries with its TLM Transaction Fees Invoice Management solution, according to Severine Melis-Cooper

STEPHANIE PALMER REPORTS

### Credit Suisse's fees and expense management solution was acquired by SmartStream in December. What developments have you made to it since then?

One of the main functionalities we have added is around listed derivatives—futures and options. We have added a full fee calculation model that covers all fee types such as brokerage, exchange and clearing fees across all asset classes, and we developed a framework for systematic interfacing with electric settlement platforms, as well as launching new managed services.

This fee offering is not just going to be software, but an operated services desk that surrounds technological capacity. We have operational teams based in India, London and Bristol, which manage processes, but also, because the service deals with listed derivatives, we have a rate maintenance service that provides the rate cards from all of the key global markets and creates a kind of data service.

We are also developing more capacity from a billing perspective. Before we made the acquisition our main position was around brokerage—historically, that is where we started. Now we have the capability to process payables and receivables, and our platform will be built around helping our end clients to bill their end clients.

### How do the new technology and your existing systems complement each other?

We launched our TLM Transaction Fees Invoice Management (TLM TFIM) service three years ago, and our original positioning with this was in the back office. From our client base we identified reconciliation processes in the fees space that were broken, particularly in the brokerage fees space. Our clients were finding they had huge backlogs and inefficiencies with manual processes. We tried to help them with processing invoices and gaining control—adding calculation capabilities.

The Credit Suisse Fees and Expense Management solution started in a very different state, in the front office. It was built to help control fees, but it lowered the number of relationships with brokers and focused on optimising trading venues. Our two products were really approaching the same problem from two different angles. Their technology had elements that our back-office offering didn't have, or didn't really develop to the same extent, so our strategy was to combine the two strengths.

We have ended up with a platform that is very strong in volume capacity, which can tackle both front- and back-office needs, but that can also apply to different groups, such as finance and network managers.

### Have you seen an increase in demand for efficient transaction and expense management? Why?

The increase in demand has been overwhelming. The market almost didn't exist when we first looked at it, and there were obviously problems with a lack of standardisation. When we first started talking about it with industry players, everyone was of the same opinion that something needed to be done to address the issues, but because none of the earlier initiatives had worked, there were doubts about our solution.

Now, not only have we had interest from our existing clients, but also from firms we have never worked with before. Companies are coming to us with the hope of outsourcing inefficient back-office processes.

Many investment banks are implementing cost-saving programmes. They have too many providers and too many trading venues, they don't really know how much they're spending and they have bad allocation capacity. Now, they want to optimise and lower their costs.

It's more important than ever for banks to control their costs, and that is a big driver. They can't afford to neglect these specific areas any more. Of course, regulators are on their backs as well, but I would say that cost is the main driver.

It is also only recently that there has been a viable solution in the market. We are offering an interesting alternative and we have demonstrated that it is a utility type of offering and that every market participant can benefit from it. Suddenly, even the sceptics are now seeing that it is possible.

### How important is automation, and the adoption of new technologies, in this area of the back office?

It has been very important. We are moving away from a world of random checks on a few invoices per month, to a world where asset managers have control over each transaction, invoice and payment. With proper treatment of exceptions and better dispute management, along with a rationalised number of providers, we have ended up with a huge improvement on the traditional solutions.

In the past there has been a tendency to consider payment fees as secondary, almost as a by-product of trading activities. The amounts were considered less significant and there was not much effort to understand the scale of the problem, but banks can save tens of million of pounds, and that's not something they can afford to neglect.

It has become enforced because banks want to be more efficient, but it's also a regulatory enforcement, as regulators are looking far more closely at what controls banks have put in place in all areas of business. Transaction management was left in the dark ages, and it's only now that banks are considering an alternative.

### Is this reflective of a shift in the servicing space in general?

Absolutely. Five years ago, 'utility' was a buzzword—everybody was talking about it but nobody knew really what it was about. Now it is a reality in all back-office areas. Standardisation, centralisation, common platforms and common processes all make total sense. Reference data, fees and billing, know-your-customer and collateral management are some of the key areas where utilities make sense and will be compelling for the market. There is a massive move towards utility in the back office and I sincerely believe that this is the only way to provide tighter controls and lower operational costs significantly. AST

**Severine Melis-Cooper**
Global head of TLM transaction fees management and billing solutions
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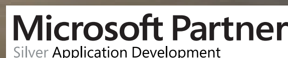

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# Targeting infrastructure

## Harmonising the proxy process will demand a robust data infrastructure. And the good news is, it already exists, according to Broadridge's Patricia Rosch

### With significant market changes, custodians must make operational adaptations to support new standards. The first phase of Target2-Securities will be implemented soon—what other issues are market participants facing?

It's important to remember that capital markets around the world have always, and will always, evolve. Target2-Securities (T2S) is a significant market change. But in addition, new regulations, a more rigorous approach to corporate governance and the sheer volume of market activity are creating challenges and opportunities for participants. Those who are able to adapt their operations quickly and efficiently will be able to capitalise on opportunity.

### Where do you see opportunities for those agile businesses?

In the EU, with its many jurisdictions, it's imperative to have systems and processes in place to support both domestic and foreign investment. T2S harmonises the trading environment with collateral management, but we also have to harmonise other associated asset servicing functions, such as proxy voting. That demands a complex data infrastructure to ensure transparency, accuracy, and local market compliance.

No one can afford to reinvent the wheel. Working from a large-scale global proxy management platform and tailoring solutions for local markets allows us to drive operational performance in global capital markets.

In North America, we transformed the proxy process by harmonising practices, reducing risk and optimising cost efficiency for more than 1,100 custodian bank and broker clients. We are now working with participants, including custodians and central securities depositories in the EU region, to support T2S and provide local market solutions that meet market and client needs. That's our competitive advantage, and it lets us pass economies on to our clients.

### What does increased market activity mean for participants?

Year after year, we're seeing volume increases in meetings, ballots and cross-border shares voted. In 2014, across 114 markets with cross-border activity, there was a 20 percent increase in the number of meetings held by corporate issuers, a 26 percent increase in ballots voted, and a 53 percent increase in the number of shares voted by institutions. This volume and complexity really underscores the importance of robust, reliable proxy management in the securities lifecycle.

### What steps are being taken to ensure the proxy management process is not only efficient and accurate, but that it supports increasingly rigorous governance standards?

In markets around the world, we see how evolving regulations and technology innovation go hand in hand. Often, the implementation of new rules relies on changes to the supporting data infrastructure.

In North America, the implementation of the notice and access rules is a good example of that. In that case, the rules necessitated a significant infrastructure change to support electronic delivery of proxy materials and an investor preference communication model.

Japan is another good example, but in this market the technological innovation came first, and set a new standard for governance. We launched Investor Communications Japan (ICJ), a joint venture between Broadridge and the Tokyo Stock Exchange, in 2005.

The impact has been transformative, with more than 550 Japanese share-issuing companies now using the electronic proxy-voting platform.

ICJ has greatly improved the flow and transparency of information to shareholders and back to issuers. We've reduced the time it takes to deliver materials from weeks to days, giving investors more time to conduct research ahead of company meetings.

The process also provides assurances to all participants that votes cast, by both Japanese and global investors, reach the shareholder meeting in a timely and accurate manner, and that they are cast at the meeting as directed by shareholders.

Recognising the benefits of the ICJ platform to the market, the Japanese Exchange Group will be implementing The Corporate Governance Code, which will become effective this month. Under the new guidelines, Japanese issuers are required to "comply or explain" regarding e-voting participation. The code points to the significant number of institutional and foreign shareholders in Japanese companies as the underlying reason for the guidance.

### Is this exclusive to the Japanese market, or are you seeing the same kind of evolution elsewhere?

We're seeing more interest in electronic voting and end-to-end vote confirmation solutions across EU and Asian markets.

We have strong participation today, and it's growing. More and more global custodians are asking to participate because they're recognising the benefits to their clients.

We're making further system enhancements to support even greater transparency in vote reporting. Global custodians are asking for more reporting in response to requests from investors, particularly in terms of confirmation that votes have been passed down the chain of intermediaries and cast at the meeting.

### What end-to-end vote confirmation projects are in place for this year?

This year, end-to-end vote confirmation programmes are being conducted in Spain, the Netherlands, Taiwan, the US and Canada. **AST**

**Patricia Rosch**
President, international investor communication solutions
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# Survival of the efficient-est

## When it comes to an evolving back-office, operational efficiency is key. Confluence's Todd Moyer explores the options for asset managers

STEPHANIE PALMER REPORTS

### According to a Confluence survey, asset managers are moving toward a more consolidated back office. How much of this is driven by regulation?

This is very much being driven by regulatory changes and the proliferation of new technologies and data sources that the industry must now manage to remain compliant. Our most recent Confluence survey, which was conducted in 2014, gave us deep insight into the views of a good cross-section of the global asset management industry. Almost half of the respondents, 48 percent, told us that managing the reporting requirements in the current regulatory environment is their firm's top goal over the next two years.

One of the interesting things we found was that, as firms have adopted new single-point technology systems to meet new regulatory requirements, their operational efficiency is decreasing and business costs and risks are going up. Firms are now beginning to rationalise a lot of those processes to achieve a more efficient back-office operating model.

Of the survey respondents we spoke with last year, 78 percent use multiple third-party solutions to support their back-office operations—and many find they're using multiple solutions to solve one reporting challenge. Since 2008 there has been a period of problem solving and only now are firms beginning to rationalise their approach.

### How have new technologies and automation affected the back office?

The financial services industry has had concerns over manual processes for quite a while, and the problem hasn't been solved yet. It has been apparent that there's a desire to move away from things like spreadsheets. But concern over manual processes in the back office appears to be growing—94 percent of survey respondents last year said they were concerned that manual processes would impact their ability to reduce reporting risk. In 2010 this number was 85 percent.

The primary difference between 2010 and now is that firms must manage and report on a considerably larger amount of data. That is a primary driver in the push for consolidation and increased process automation. Of the survey respondents, 76 percent told us that consolidating back-office technology would improve operational efficiency, 55 percent said it would streamline the reporting process and 48 percent said it would reduce operational costs.

Firms are looking for a consolidated, single source solution for managing their regulatory data. They are also looking to achieve this at a lower cost point. There's a growing sense of urgency to improve back-office data management processes, which is a part of the business that has historically been neglected.

> "Asset managers need to think holistically about how they manage their back-office technology and data"

### Do you anticipate any knock-on effects, positive or negative?

We have seen a significant increase in the number of vendors offering single-point solutions. One of the challenges firms will have to face short-term is how to simplify their back-office technology, which has become much more fragmented. They can do that by identifying solutions providers that address a much broader set of technology needs. Firms will need to start asking how a new technology solution can extend in to other areas of the business and tie in to overall data management strategy.

At the moment firms are dealing with too many vendors and third-party applications that solve similar needs. By consolidating technology and data sources, firms will be able to develop a golden copy of their data that can be validated once and reused in multiple instances and for multiple reports. That type of change in back-office data management will create immediate value for the firm.

### Are you seeing an increase or decrease in outsourcing?

Over the last six months in particular we have seen firms looking to outsource more of their data management processes as they drive to consolidate their back-office technology. We are seeing a significant shift in the way that firms view the back office. There is a growing willingness to move those business processes and data to a shared services model. More customers are actively approaching us, looking to take the cost out of some of these processes and find a single solution provider to meet their needs across the spectrum.

This move towards an outsourced model will help drive operational efficiency without diminishing performance.

### What should asset managers be doing in order to stay on top of regulatory reporting requirements?

Asset managers need to think holistically about how they manage their back-office technology and data. For the last several years we have been talking about the flood of new regulatory reporting requirements and the data management challenges those rules have created.

I don't believe there are any asset managers who wouldn't like to reduce the number of vendors they work with. The current regulatory environment has arguably led to greater stability in the market, but it has also contributed to the fragmentation of the asset manager back office. We have had three or four years of firms reacting to regulatory mandates by plugging holes in their data management processes.

Now there has been a bit of a slowdown, and firms have had time to step back and evaluate where they are. A lot of firms are using this time to improve operating efficiency so that they are better prepared to address the next round of regulations in a more systematic way. **AST**

**Todd Moyer**
Executive vice president of global business development
Confluence

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# Do the math

## It's just another regulatory equation to figure out, but, says Fundsquare's Paolo Brignardello, the trick to Solvency II is to do your homework

Whether talking to insurers or asset managers, one thing we want to do is provide reassurance. Solvency II may seem onerous but we believe it is possible to overcome some of its most challenging aspects.

At Fundsquare we are keen to make sure that our positive message doesn't instil complacency. The evidence is that many in the industry aren't as prepared as they ought to be at this stage, with just over six months to go before the new rules come into play, and there seems to be a distinct difference in the level of preparedness between asset managers and insurers.

### Re-read the question

Asset managers seem to have embraced Solvency II more enthusiastically than their insurer partners, which may seem unusual considering the regulations aren't aimed primarily at them. However, when the business case is made that Solvency II is a once-in-a-lifetime opportunity to overhaul how fund managers deal with one of their biggest client bases, initiative becomes clear.

For fund managers, there are few client groups more important than insurers. Europe's fund management companies oversee almost €17 trillion in assets, and the total assets for the European insurance industry stands at about €8.4 trillion, representing almost half the investment industry. Even if some of this money is overseen internally at insurance businesses and invested into securities directly, that still leaves a huge amount of insurance assets in the care of the fund management industry. It's also a growing sector—that €8.4 trillion is almost 55 percent higher than the €5.4 trillion invested by insurers a decade earlier.

Given the significant increase in the burden of regulatory and administrative work insurers are facing as a result of Solvency II, it does not seem controversial to say that many will try and consolidate the number of asset managers they deal with. The likely outcome of this is that there will be fewer, but more valuable, insurance fund contracts up for grabs.

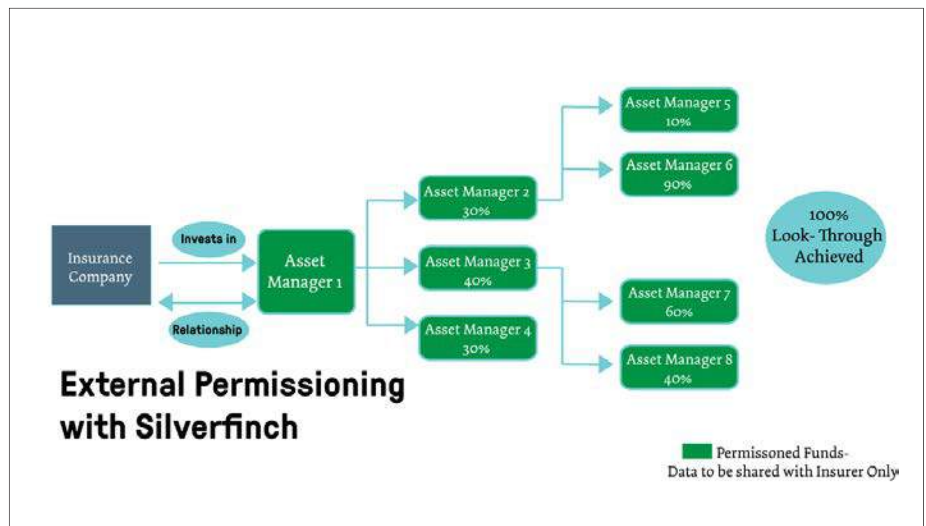
Importantly, from a business planning perspective, the number of insurance funds up for tender is expected to increase markedly in coming months as insurers restructure their portfolios. Fund managers know that those among them who can best demonstrate they can help insurers with their Solvency II requirements will be the ones most likely to get the lion's share of these new contracts.

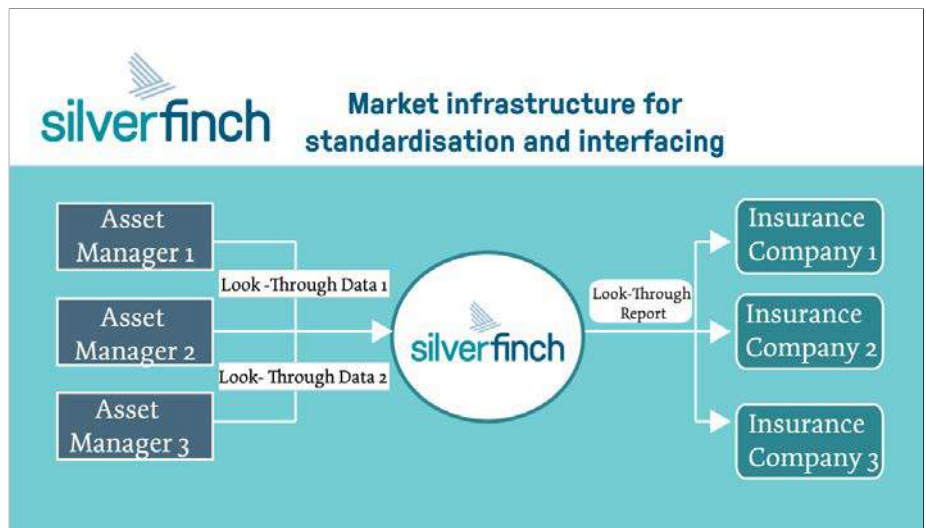
### No cheating

Insurers haven't been so proactive, and we are couching our language here. We have talked to more than 200 companies in the past six months and only about half are taking steps to make sure they are fully compliant with the new rules within the deadline.

Some may be over-confident about what they can achieve in a short time, or are thinking that the regulator will be forgiving when it comes to interpreting the rules on look-through.

Indeed, some insurers have suggested that they won't need to fully outline the underlying holdings in a third-party fund and instead think a breakdown of asset allocation will suffice—it certainly won't.




Another worryingly common response to Solvency II is simple inertia. Some in the insurance industry are finding the prospect of identifying and listing their holdings so onerous that they have delayed taking any action in the hope that someone will come along and fix the problem for them.

Whatever the reasons, firms will need to get their skates on if they intend to meet the requirements of Solvency II. Luckily, while there has been procrastination among many that are the targets of the new rules, other participants have been doing their best to move Solvency II forward.

## Power of three

Asset management companies are among the best businesses in the world in looking after their clients, and Solvency II, in the end, is a client-servicing issue for their insurance customers. The companies realise this, and so do the overall trade organisations. Over the past few years, industry bodies have banded together to introduce the tripartite data model, which outlines the entire range of data that asset managers will need to provide to their insurance clients to meet the Solvency II stipulations.

This set of more than 100 data points has now been adopted as the EU standard. So far so good—the fund industry has determined which data needs to be provided. The problem is that the model doesn't suggest how this data is formatted or, most importantly, how insurance companies can access the information they need. For Fundsquare, this is the biggest problem with Solvency II, which is why Silverfinch has spent the last few years formulating a viable and efficient solution.

## Show your workings

The new Solvency II requirements stipulate that insurers have to be able to understand the risks within their asset books, and that in order to do this they must be able to outline the underlying assets they own. As we have pointed out, many asset managers know how important this client group is, and are therefore prepared to provide details on the holdings within their funds.

However, investing isn't as simple as it used to be. Many insurers are straying from the direct bond holdings and equity funds that have been a staple, and are accessing more exotic assets. Funds-of-funds in particular are attracting investors—43 percent of hedge fund-of-funds managers saw their assets increase in 2014, up from 39 percent in 2013. The increased use of funds-of-funds means that the connection between the insurer and the end investor is becoming ever more complex.

While fund managers are willing to give fund details to their direct clients, when an intermediary is introduced in the form of a competitor—essentially what a fund of funds is—the shutters go down. This is understandable, as asset managers feel they are being asked to share their proprietary investment strategies, effectively the secret sauce of their business, with the competition.

## The solution

Fundsquare understands the needs and concerns of each party and has developed a solution that breaks the logjam. It is based around giving the asset manager control over who sees its data. The insurer who has a direct relationship with a fund-of-funds can of course get the data on the individual fund holdings with relative ease. But the insurer also needs to get details on the holdings of the individual funds within the fund-of-funds.

Fundsquare's Silverfinch solution allows an asset manager to give permission to the insurer to access this information, without ever going through the intermediary or competitor who runs the fund-of-funds. And, because the asset manager is always the gatekeeper, a fund-of-funds competitor can never inadvertently get access to this data.

We want to convey reassurance, and with Silverfinch we believe everyone will be satisfied with our solution. Insurers can access the data they need, the asset management compliance director can be content that the company's data is secure, the asset management client servicing department will be happy that their customers are satisfied, and the regulator knows that its requirements are being met. What could be more reassuring than that? **AST**

**Paolo Brignardello**
Head of product management and marketing
Fundsquare

# In the spotlight

Experts from Pacific Fund Systems and RBC Investor & Treasury Services discuss how automation could be the key to a cleaner back office

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> “Investor protection, and alongside that, increased scrutiny and regulation of the asset management and custody sectors, will remain key themes for the foreseeable future”

**Sébastien Danloy,** head of continental Europe and offshore managing director, **RBC Investor & Treasury Services**

### What can asset managers do to comply with the swathe of regulatory reporting coming in to effect in Europe?

**Keith Parker:** As a general rule, asset managers are not in a position to decide whether or not to comply with regulatory reporting requirements, short of actively avoiding being domiciled in a particular location. The issue is rather how to effectively manage this challenge without losing focus on their core competency—managing assets. We would argue that outsourcing this regulatory burden is likely to be the most sensible strategy. We have clients that are now providing an alternative investment fund managers directive (AIFMD) Annex IV reporting solution to their asset manager clients. The nature of the Annex IV reporting means that a very sizeable percentage of the data that needs to be reported on resides with the administrator. These administrator clients in turn have approached us to assist them through their usage of our fund accounting platform, PFS-PAXUS.

In terms of the regulatory reporting that we have built, a solution for the AIFMD Annex IV reporting undeniably poses the biggest challenge mainly around the fact that it is so cumbersome. There is just so much data that needs to be reported on. That said, we have built what we like to think of as a very easy-to-use and elegant solution for our fund administration clients to deal with this challenge.

**Sébastien Danloy:** Regulatory change continues to proceed at a great pace and as a result, the cost and complexity of regulatory compliance looks set to continue to increase. For example, asset managers will need to examine the impact on their operating models and IT systems, the demands for greater and more detailed reporting, the identification of underlying investors, repapering of contracts, and more. In-house teams, such as legal and compliance, and operations, are under increasing pressure and resources are being consumed away from the core investment management capability of the asset manager.

In this context, outsourcing to service providers can be an effective way for asset managers to tackle compliance with regulation. Asset managers can leverage the shared experience (and mutualised costs) gained from service providers working with multiple clients and across multiple regulations, as well as benefit from the use of developed operational solutions and requirements for areas such as reporting.

Effectively managed regulatory change is a partnership, as both partners must adapt to evolving regulations and challenging market conditions. In many cases the regulations require both parties to work together to determine roles and responsibilities, and may include data collection and reporting requirements or changes to processes.

While there are several large and potentially complex regulations currently having to be worked through, it is difficult to say which regulations pose the biggest challenge as this depends on the profile of each individual asset manager, their level of understanding and preparation, and the support of their service providers.

### How important is the adoption of new technologies in back-office administration?

**Danloy:** Embracing technology is critical to our clients and our ability to serve them—helping them to better manage their processes, improve their operating models, and ensure there are no errors when trades are settled on time, net asset values are calculated, and data is managed. Clients also want the interaction with their service provider to be as seamless and simple as possible, and for access to the data we hold on their behalf to be straightforward and timely.

Asset managers are increasingly required to dedicate more time and resources to managing stricter reporting and accountability requirements as a result of increased regulation and scrutiny. As a result, the profile of middle and back-office functions within asset managers has risen and custodians have responded through services aimed at helping them meet their obligations.

Innovation and increased use of technology can also help businesses to manage operational risk and improve efficiency by reducing human error and standardising processes, for example with straight-through processing.

**Parker:** Back-office administration, by its very nature, is perfectly suited to be automated. It is repetitive, often very complex, data intensive, and has a lot of underlying moving parts. Using technology in the first instance in this environment is crucial if an administrator wants to be both efficient and accurate. An excellent administrator will not only maximise the use of technology but will also constantly seek out new and improved technologies, continually pushing the boundary of what is achievable in terms of automation. Of course, all of this comes at a cost, so this is a crucial part of the overall operational challenge facing an administrator.

> “Back-office administration, by its very nature, is perfectly suited to be automated. It is repetitive, often very complex, data intensive, and has a lot of underlying moving parts”

**Keith Parker,** head of sales and marketing in Europe**, Pacific Fund Systems**

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> There will be much of the same: more regulatory scrutiny and a continued demand for the automation of processes within the funds industry

**Keith Parker,** head of sales and marketing in Europe, **Pacific Fund Systems**

## Are you seeing an increase in real estate investment funds, or in any other asset type? Why is this happening now?

**Danloy:** In terms of assets under administration, RBC Investor & Treasury Services is the largest asset servicing provider in Luxembourg for offshore real estate funds, with a 39 percent market share. In both Luxembourg and Dublin we are seeing a boost from growing institutional investor interest in alternative asset classes, especially real estate, but also private equity and alternative hedge fund strategies.

Alternative investments continue to attract institutional investors. The continuing low rate environment and ongoing depressed yields in traditional asset classes are significant challenges for investors, who, as a result, are increasingly looking at alternatives to achieve the returns they need to meet their liabilities. A report published by Mckinsey & Co in 2014 estimated that three-quarters of investors expect to maintain or increase their investments in alternatives over the next three years.

This trend has been supported by an increase in new or revised vehicles and structures, such as the Investment Limited Partnership in Ireland and the Special Limited Partnership in Luxembourg.

**Parker:** Over the last three years or so we have seen a significant emergence of the automation of private equity fund structures. First, retail and mutual funds were automated, then hedge funds and now private equity funds.

One reason for this is the growth of private equity as an asset class, meaning that there are just that many more of these fund types around.

Private equity asset managers have seen how successful automation has been with retail and hedge funds, and sensibly questioned if this could also be true for the types of funds that they manage. These types of fund structures are now better understood by administrators, for example, which fuels growth in the usage of technology in managing and administering these fund types.

## How do administration requirements differ for real estate and alternative investment funds?

**Danloy:** Alternative funds, including real estate funds, have more complex underlying assets, which lead to different valuation frequency and accounting entries, and different demands fon transaction documentation and support to traditional UCITS funds.

Alternative funds often have more complex multi-jurisdictional structures that need support, and with them transaction and cash-flow monitoring requirements.

The domiciles of Luxembourg and Ireland are both home to exceptionally strong regulatory and service provider infrastructures which are well-

> Alternative funds often have more complex multi-jurisdictional structures that need support, and with them transaction and cash-flow monitoring requirements

**Sébastien Danloy,** head of continental Europe and offshore managing director, **RBC Investor & Treasury Services**

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suited to the greater complexity of handling real estate and other alternative investment funds.

### What trends do you anticipate appearing throughout the rest of 2015, and beyond?

**Parker:** We believe much of the same, in terms of what has transpired over the last few years; more regulatory scrutiny and a continued demand for the automation of processes within the funds industry.

**Danloy:** Investor protection, and alongside that, increased scrutiny and regulation of the asset management and custody sectors, will remain key themes for the foreseeable future. There will be greater demands on fund administration in terms of reporting and transparency for valuation and pricing. Transparency in general is a growing trend, notably concerning taxation, and this is supported by regulatory initiatives.

Another trend is likely to be technology and how it will continue to influence the shape of the industry, from identifying and tackling new distribution models and how they are supported, to how the industry can learn from other sectors in areas such as cyber-security and effectively exploiting 'big data'. AST

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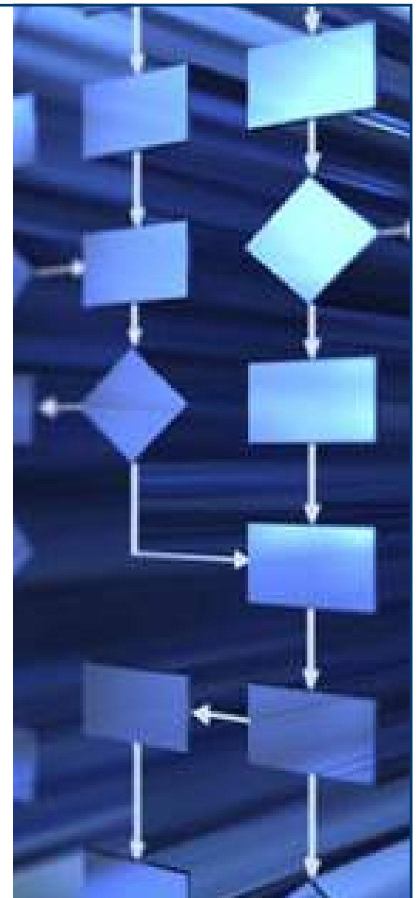

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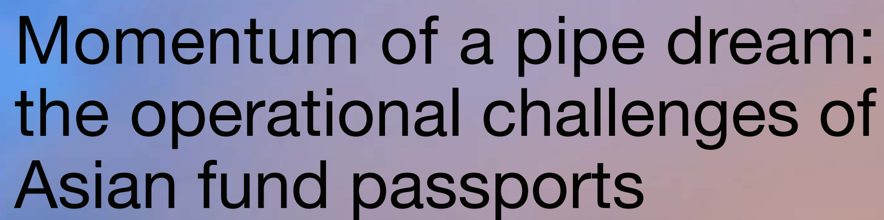

# Momentum of a pipe dream: the operational challenges of Asian fund passports

Asian passport initiatives create a great opportunity for Asia-based fund mangers, but barriers remain, says Sébastien Chaker of Calastone

With rules and operational arrangements currently being developed in earnest, the dawn of the Asian funds passport seems fast upon us. Headlines in the Financial Times have progressed from the rather negative "regional mutual fund passport a 'pipe dream'" in 2011, to the more positive "Asian fund passports gain momentum" in February 2015. But will an Asian funds passport really prove useful for fund managers?

Industry experts, such as Lawrence Au, head of the Asia Pacific at BNP Paribas Securities Services, think it will result in change in Asia, but only if investment companies customise their funds to suit Asian markets. Ernst & Young, one of the 'big four' accounting firms, has erred on the side of caution, advising: "Any firm with regional aspirations in Asia should at least consider its potential response to the proposals."

### Three schemes

The Asia Region Funds Passport (ARFP), backed by the Asia Pacific Economic Cooperation (APEC), was developed in order to provide a "multilaterally agreed framework to facilitate the cross-border marketing of managed funds across participating economies in the Asia region". It is not, however, the only passporting initiative in the area. The Association of Southeast Asian Nations Collective Investment Schemes passport, launched in August 2014 and covering Singapore, Malaysia and Thailand, allows fund managers within those countries to distribute fund products "via a streamlined process" across borders to retail investors.

Yet the initiative that has attracted the most excitement is the imminent launch on 1 July of Hong Kong and China Mutual Recognition of Funds (MRF), not surprisingly because of the potential access to the lucrative Chinese market it represents.

Each of these three competing schemes have the same central goal, to give Asian investors a greater choice of investment and to revamp Asian capital markets in order that they become more integrated and resilient. In essence, each of these schemes aims to emulate the EU's UCITS framework in which funds can operate freely throughout the EU on the basis of a single authorisation from one member state.

### Diverse designs

With only one of the schemes begun so far (at the time of writing, the official commencement of MRF was only just announced on 22 May), there remains scepticism over the launch date of the ARFP, as well as the amount of take-up each will attract. It is unlikely that the programmes will experience overnight the same levels of success currently enjoyed by UCITS products.

The programmes are also hindered by a region that is legislatively and economically divided. The lack of a central governing body, common currency and harmony, given that participation of some countries is dependent on their success in becoming the principle Asian domicile for funds, are all potentially standing in the way of success.

There are also uncertainties as to whether there would be sufficient values in order to attract investors and distributors, as well as concern over whether current operating models would be able to handle a move from pure domestic to regional servicing.

### Strength in numbers

But does this pessimism count for much when we are talking about the fastest growing and most dynamic region in the world?

If the common aim of all three schemes is to better integrate and strengthen Asian capital markets, then it stands to reason that regional authorities will start to put more emphasis on their own schemes rather than continuing to approve UCITS distribution, although slow-downs have been noted in Hong Kong and Taiwan.

In addition, Asian regulators continue to be uncomfortable with the introduction of UCITS III and its more extensive range of derivative investment products. While the lack of a central governing body for each of these schemes remains one of the most difficult hurdles to overcome, the desire to create a competitive product to rival UCITS may actually act as a catalyst in creating a consensus amongst Asian governing bodies.

As with UCITS, Asian funds passports will take time to develop and reach similar maturity and success. The UCITS framework was created in 1985, with the first UCITS Directive implemented in 1988.

It took another five years to see any material flow and more than 15 years for UCITS to become a real success. What's more, there was no single currency at the time of UCITS's creation; even today, several members of the EU do not use the euro, yet UCITS has successfully developed across Europe and even outside of Europe.

In terms of distribution, investors in less mature markets (including Malaysia, Thailand, Indonesia, Vietnam, Philippines and China) have a chance to greatly benefit from access to funds from experienced global and regional fund managers.

If the passporting schemes were to succeed, it would be mandatory for those firms interested in cross-border distribution to have an onshore presence in at least one of the participating markets, as well as strong branding and access to distribution networks across the region.

In terms of operating models, distributors and fund managers alike will need to leverage technology and use service providers with a proven expertise and track record in cross-border fund processing.

### Seamless cross-border distribution

The advent of Asian passport initiatives and the general trends towards globalisation of the mutual fund distribution industry create a great opportunity for Asia-based fund managers to leverage their regional brand to export their fund management expertise and products to a broader investor base.

But equally, cross-border distribution creates a wide range of new operating challenges, which need to be identified and understood in advance in order to unlock any opportunities.

While Asian fund managers still remain mostly domestically focused in terms of fund distribution, UCITS fund providers have nearly 30 years of experience in operating in a cross-border distribution environment.

The most successful firms have set up an efficient and scalable operating model that enables them to smoothly distribute a single-fund range to a number of disparate fund distributors located in more than 50 countries.

Calastone has been helping leading global fund managers in standardising and streamlining their fund transaction interactions with their key distributors globally.

Calastone's community includes more than 800 clients in 23 domiciles processing domestic and cross-border fund transactions over its network.

As a fund messaging network in the key markets actively involved in the Asian fund passporting schemes (Australia, Hong Kong and Singapore), Calastone is ideally placed to support the Asian fund community in building the efficient and secured fund messaging infrastructure required for the successful development of these passports. **AST**

**Sébastian Chaker**
Managing director and head of Asia
Calastone

# For the good of the brand

## Accuracy, availability and consistency of fund data could have a significant impact on asset managers' reputations, says Lee Godfrey of KNEIP

The core business of asset management firms should be to manage and grow their clients' money. The key challenge therefore is to work on achieving the best performance possible over the long term, while managing risk and remaining transparent. Often, however, when discussing products with their buyer community (ie, investors, distributors, platforms and other fund selectors), sales managers often spend too much of this valuable time justifying data inaccuracies and/or reporting discrepancies. The buyer community notice data inconsistencies across data vendors or on asset managers' web sites, which can lead to a loss of confidence in that manager's brand.

### Proactive fund data management

A recent survey by Fund Buyer Focus reveals that the most important element for asset managers' credibility is the accuracy, availability and consistency of reporting and data. If fund data is not actively managed—which of course is time and resource consuming—it can very quickly become outdated and/or inaccurate.

Our detailed analysis shows that the average data consistency across the leading information channels is typically between 50 and 55 percent, and can be lower still. Notably, even companies that manage this data internally or through external service providers still fall within this range of inconsistency.

The effect on the asset manager and their brand can be significant, but is not always visible. We hear from clients when the burden on sales and operations teams is too high and the 'noise' from a dissatisfied buyer community becomes detrimental to growth. However, it is that hidden impact that can be more costly, through potential loss in sales due to a lack of credibility and trust from the market. In addition to these two elements, there is also the risk of sanctions or fines from regulators, and in extreme circumstances, litigation from the buyer community.

Asset managers that proactively manage their data see an increase in accuracy and consistency of their fund data to between 95 and 100 percent. By outsourcing this non-core function, they can also significantly reduce the cost of internal operations, and above all add substantial value through increased sales and improved credibility in the marketplace.

### Quality control

Data quality and infrastructure require investment and focus, but should not be a discussion point between asset managers and their buyer community; it should just work, all the time. The only occasions where one should hear about it is from positive testimonials from buyers. As I recently heard at an awards ceremony, a certain asset manager "always provides clear, consistent and timely data".

Each country where your funds are registered for sale will have specific regulatory requirements, and will require a certain amount of data to be published—from the net asset value to fees to tax to performance information—which all need to be managed proactively. However, channels that are not on asset managers' preferred list of destinations will still acquire and publish their funds' data from whatever source they can.

The problem then becomes that fund buyers may still use these channels when conducting their analyses and making buying decisions. Therefore, asset managers must not only actively monitor the channels that matter most to them, but also the other channels being used by the wider buyer community.

Whereas there are some data point that are more regularly requested than others, many of them will be used by buyers in different ways. Clearly, performance is important, as are fees, however, many other fields can be equally relevant. For cross-border funds, registration countries are essential for buyers to know where each fund may be distributed. Many advisors use tools that will filter on fields, and without this the fund will not even be presented to potential buyers.

### Spot-checking is not enough

We do not sell data, hence there is no conflict of interest. The asset manager is our only client. This allows us to build long-term, mutually beneficial relationships with the data vendor platforms that matter to our clients.

We have invested significant time and resources working with each destination on data formats, scope, and frequency of delivery. We have implemented direct data feeds to all major channels for critical data. Spot-checking data sporadically is simply not enough. Data changes constantly, and this is part of the life of the asset manager. When we identify discrepancies, we follow up on each one to ensure that it is resolved in a timely fashion and report back to both the information channel and the asset manager on the result.

We open more than 500 tickets each month with each of the major information channels and close them within an average of two days. If dialogue is required to discuss conflicts such as fund classification, we broker calls between the portfolio manager and analysts on the channel side, saving sometimes months of email trails to find the right people and get to the heart of an issue. **AST**

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# Security alarm

## As the Czech CSD approaches its fifth birthday, there are still concerns around the safety of securities. CSOB's Marek Začal explores why

It is often overlooked, deemed too small or even uninteresting, but the Czech securities market is not about to stand aside. This year, it will be five years since the market finally introduced its first central securities depository (CSD), but it's not time to celebrate yet. In terms of record keeping and asset safety, questions and concerns still remain, even after such an anniversary.

In 2010, the local CSD came into existence with the typical enthusiasm and related expectations. However, despite the fact that securities—except T-bills—are finally settled under one roof, Czech legislation did not shed much light on the safekeeping side of the matter. After the introduction of so-called 'two-tier registration', one could argue that there is no cause for discussion about segregation and asset safety. Unfortunately, this discussion still persists today, and it seems it will continue.

### When one and one is not always two

There is a two-tier registration of securities held in the local CSD, as defined by the Capital Market Act. Beneficial ownership must be recorded either at the CSD level (tier one), or

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in a sub-custodian's books (tier two). For this purpose, Czech legislation introduced two types of accounts: the owner account and the account of customers.

To clearly distinguish between these, the owner account is defined as one where book-entry securities are registered for the person for whom the account was opened. Additionally, it is deemed that the owner of book-entry securities is the person in whose owner account the securities are registered.

In the account of customers, there will be various registered book-entry securities of many persons who will entrust their securities to one person, in whose name the account of customers has been opened. The person for whom the account of customers has been established is not the owner of book-entry securities registered.

Moreover, the CSD maintains the central register of book-entry securities on both owner accounts and accounts of customers. More importantly, the person who maintains the follow-up register linked to the central register of book-entry securities, ie, the person who holds the account of customers in the CSD, maintains this follow-up register only, and entirely, on owner accounts. Therefore, two-tier registration of securities should be assured.

## Read between the paragraphs

So what is the point? The problem lies in Czech legislation, or rather, in its interpretation.

This is mainly due to the legal definition of an owner account, which states: "It is deemed that the owner of book-entry securities is the person on whose owner account the securities are registered". The word "deem" amounts to a rebuttable presumption that the holder of an owner account is the owner of securities. But there are two different interpretations to this presumption on the market.

The first stream refers to this rebuttable presumption and says that registered ownership of securities may be rebutted, or proven otherwise. This stream claims that it is possible, if needed, to prove that a holder of an owner account is not the beneficial owner of securities held on this account, although this holder is deemed to be the owner by all local authorities and issuers.

The second stream claims that the idea of rebuttable presumption is not to create the nominee concept for the owner account, but to allow corrections of mistakes in ownership registration. For example, omitted changes in ownership records in cases of marriage, inheritance and other similar situations. This stream also stresses that the very existence of statutory nominee accounts, or accounts of customers, proves that an owner's account is not meant by the legislator to be used as a nominee. As we can see, a full nominee concept is not applied simply because the holder of an account of customers in the CSD can only open owner accounts of final beneficiaries in its books.

## Low cost or risk-free?

Some foreign investors still feel that the situation in the Czech Republic is unclear. This is due to the fact that some Czech sub-custodians are of the opinion that it is possible to use an owner account in the CSD as a nominee account, or even that this is an acceptable market practice. The secret as to why this solution became a market practice for some local providers is hidden. To open and fully manage an account of customers, local providers are obliged to implement a particular communication interface, which brings with it costs and time pressures. If you ask your Czech sub-custodian whether it is able to open a true account of customers in the Czech market, its reply will most likely indicate what its attitude to account management really is.

Although some Czech sub-custodians do call it a 'market practice', it can also be said that it is a practice of many foreign banks, which might not be fully informed of all implications. Many foreign banks do use owner accounts as nominee accounts in the Czech CSD. However, there are still two key questions: are these foreign banks aware of the fact that an owner account is not a nominee? And, are they aware of the related risks?

If we consider a foreign bank using an owner account as a nominee for holding the securities of its underlying clients, then clients of this bank are exposed to a risk that their securities may be blocked, if an order for blocking of foreign bank property is released by authorities or an insolvency administrator. This could be, for example, in case of the foreign bank´s insolvency. Considering this indisputable risk, the opinion that it is a market practice to use an owner account as a nominee account is misleading, at best. However, the question remains whether foreign banks are fairly informed by Czech sub-custodians about this risk, or if this risk is trivialised.

## The whisper of a regulator

At a meeting of the Association for Capital Markets held in October last year, the Czech CSD representatives confirmed that the CSD will block owner accounts belonging to foreign banks if instructed to do so by authorities or an insolvency administrator. There is no need to further describe how long it would take to reverse this action, or, in the language of Czech law, to 'prove otherwise' that the actual owner of securities on such an account is different from the named account holder.

Also, the local regulator, the Czech National Bank, has already confirmed that final beneficiaries must be informed on such a risk. What's more, the Czech National Bank supports the second-stream opinion, saying that the statutory owner account is not meant to be used 'as standard' as a nominee account. One could say that this resolution is the end of the story. But this statement from the regulator would not be complete if we did not include one additional remark. It will not be Czech National Bank that would, in the case of a dispute, decide the ownership of any securities. The final word in this matter would be uttered by a court of law, and the Czech National Bank claims that it cannot anticipate a court decision with any certainty.

## Out of sight, out of mind

All in all, it still looks like we do not have a winner. The reason is, perhaps, truly hidden in the last paragraph.

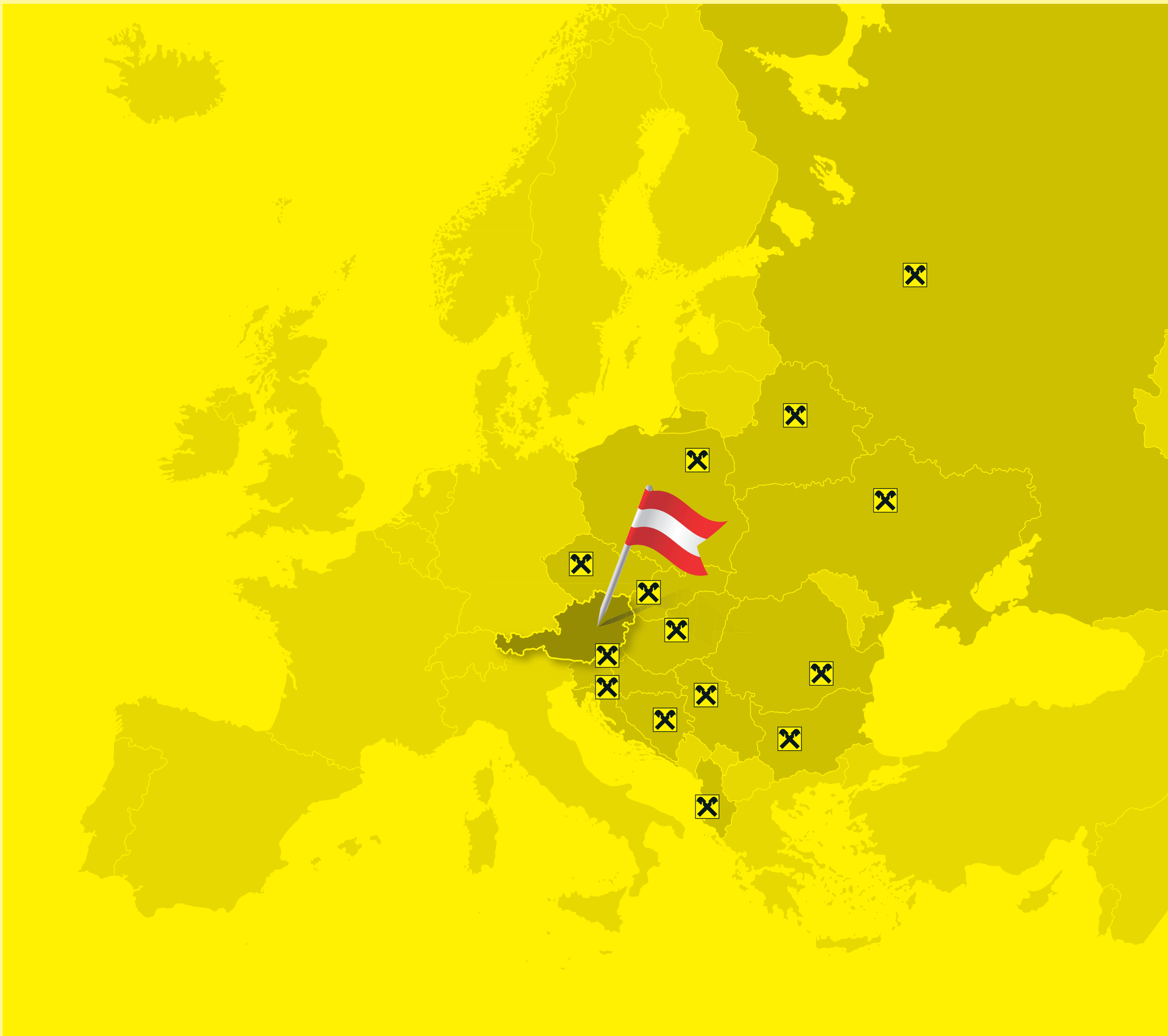
The truth is that the market still lacks any real praxis. Since the establishment of the CSD as there has been no real evidence of a court's decision, and a dispute could prove lengthy. However, one example can be found beyond Czech boundaries. It is not more than a few months since UK regulator the Financial Conduct Authority (FCA) imposed a significant penalty on Barclays Bank, fining it nearly £38 million for failing to properly protect clients' custody assets, worth £16.5 billion.

Because of 'significant weaknesses' in the systems and controls in Barclays's investment banking division between November 2007 and January 2012, clients risked incurring extra costs, lengthy delays or losing their assets if Barclays had become insolvent. In addition to these failings, account naming or incorrect data suggested that the account assets belonged to Barclays, instead of its client.

The Czech market could learn a lesson from this, but the numbers are unrelenting. The fine imposed by the FCA in this case was £38 million. On the other hand, according to the latest statistics from the Czech National Bank, it has imposed record penalties totalling only £500,000 since the beginning of 2015.

Is the cost for keeping assets safe in the Czech Republic really so high? In any case, if usage of a Czech account of customers was more supported and widely practiced, many clients, as well as network managers, might sleep better. **AST**

**Marek Začal**
Custody relationship manager
CSOB



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# The next frontier

## The Romanian market is improving at a gallop, but Andrei Mezdrea of Raiffeisen Bank explains why it still has a way to go if it's to graduate from the frontier

The progress made in aligning the Romanian capital markets with international standards is remarkable.

In a joint effort to obtain reclassification from 'frontier market' to 'emerging market' from Morgan Stanley Capital International (MSCI), market participants and authorities have teamed up. The Romanian government is strongly supporting this initiative, which is aimed at creating greater visibility of Romania but also at attracting a whole new range of investors, namely those who are not currently allowed to invest in frontier markets.

The working group, including the Bucharest Stock Exchange (BSE), the Financial Supervisory Authority, the National Bank of Romania and the Romanian government, identified a list of eight systemic barriers for the creation of the modern capital markets in Romania, and committed itself to removing them.

### Regulatory framework in place

A number of bold initiatives promoted by the authorities and the government during the last two years have qualified Romania as one of the European markets with the fastest progress. Market procedures and infrastructures have been aligned with international standards in various fields:

- Major improvement in corporate governance and shareholders' rights regulations, for example, in the introduction of ex- and pay-dates, general representation for shareholders meetings, and centralisation of income distribution at the local CSD;
- Segregation of trading and settlement infrastructure;
- Reduction of market fees as an incentive for liquidity providers; and
- Reduced fiscal reporting obligations for non-resident investors.

BSE officials estimate that, from a regulatory and infrastructure perspective, the market is already compliant with MSCI requirements as of today. However, we are still missing a consistent pool of well-capitalised companies and we need improvement of the free float and liquidity criteria.

### Opening up for additional trading

Apart from regulatory and functional enhancements, a number of initiatives took place in recent months, underling the market's intention to implement and accept thorough changes that have come along with the application of the MSCI standards, as well as with the intent to boost the capacity to absorb additional volumes.

We have seen market opening for depository receipts (DRs). Following the introduction of global depository receipts (GDRs) in Romania in late 2013 and the successful initial public offerings of natural gas producer Romgaz and the Romanian electrical power distributor Electrica, one of the top five most liquid issuers at the BSE, Fondul Proprietatea, has opted for trading on the Specialist Fund Market of the London Stock Exchange, through GDRs by means of a non-capital raising listing.

There has also been an increase in remote membership at the BSE. In the last year, two brokers from Central and Eastern Europe obtained membership at the BSE, despite the fact that the Romanian market is not rendering the services of a central counterparty (CCP), and that the settlement setup in relation to the local CSD is quite complex. This is a clear indication of confidence in the market's potential.

Finally, there has been development on the bond market. In May 2015, the Bucharest City Hall issued municipal bonds worth €500 million in order to refinance a previous bond issue of €500 million, maturing in June 2015. As they premiere, the bonds are available for settlement through Clearstream.

### An ambitious agenda

The Romanian market has undertaken major steps forward, but a lot of work still lies ahead to enforce further improvements, such as:

- Automation of the operations: A significant part of the operations still implies manual intervention into applications, requiring paper-based or human processing;
- Settlement risk management: the creation of a local CCP will have to be put on the agenda once again. In order to evolve, the market needs to address the settlement risk by creating a CCP.
- New listings: state officials' ambitious statements about further listings and privatisations need to be backed up by a master plan, and relevant milestones will need to follow.
- Increasing the liquidity at BSE: the Romanian market is a buy-and-hold market. The regular turnover is still small compared to the market's potential. In our view, this could have to do with the fact that the numerous regulatory and system changes so far have not yet been entirely internalised by small-medium investors.
- Developing the retail market: financial education is the key for the creation of a pool of domestic long-term investors. They are needed to cushion the effects of movements of the large players and provide solid demand for Romanian instruments.
- Aligning taxes to business realities: Once approved, the amendments to the Fiscal Code planned to become effective as of January 2016 will significantly improve the fiscal treatment of the capital markets investments.

### About Raiffeisen Bank Romania

Raiffeisen Bank Romania is an agent for promoting and realising new setups and projects on the domestic market.

The group securities services Romania business has actively been taking part in the development of the Romanian capital market. At the same time, product and service quality for global clients is key in an increasingly automated and standardised business environment.

Virtually all market developments of the last few years were either initiated or supported by Raiffeisen, including the permission of settlement of municipal bonds via Clearstream; the start of trading of newly issued shares within three days following the capital raising through an IPO; the introduction of DRs on the market; the introduction of over-the-counter turnaround trades; the introduction of a global accounts structure, market making and short selling; and remote broker access to the BSE.

We are confident that, despite the fact that the Romanian market is still small and needs further investments, the improvements of the last few years prove it will remain one of the European markets with the fastest progress, and an example of growth in the region. AST

**Andrei Mezdrea**
Head of GSS Romania
Raiffeisen Bank

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# Post-trade fees: time for a change?

## Robert Scott of Commerzbank considers how the security services, custodial and asset servicing businesses are pricing their offerings, and whether change is needed for the good of clients

Pressure on pricing has been the overriding dynamic of the securities industry for the past decade. When lobbying of the stock exchanges failed to bring down execution costs, the big banks worked together to create alternative trading venues and multilateral trading facilities. The resulting drop in executional pricing and the introduction of true competition and innovation was something to be celebrated.

But in security services, custodial and asset servicing, has the pressure on pricing become too great? In the race to push costs to the floor, are we in real danger of jeopardising the long-term sustainability and stability of an essential and necessary part of the transaction lifecycle?

The services performed by custodians and sub-custodians are critical. If they are not performed correctly, it can cause enormous problems with clients and lead to significant cumulative losses. Moreover, in the new regulatory environment, poorly managed post-trade activity can also create huge drains on capital and collateral efficiency.

So, is it time for a fundamental change in how service providers do business, and how clients are educated as to the real value of the tasks

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executed daily around the world on their behalf? To use an analogy, is it time clients understood the implications of taking their highly-prized Rolex or Cartier watch for servicing in a local budget jeweller?

## Fee compression

The squeeze on margins for service providers has been relentless at a time when providers have had to invest in regulatory compliance, increased transparency and market innovation. Ten years ago, custodians could have expected to levy fees of multiple basis points or more for core custody and safekeeping. Now, pricing rarely begins at more than a basis point (in fact, it's often lower), while transaction fees that used to be in the 10s of euro/US dollars have fallen by 80 percent or more.

Fees used to be negotiated once every two to three years. Clients now routinely want to review them annually or semi-annually. Negotiations are often expected to begin at the very bottom-end of pricing scale regardless of volume, with clients still demanding the highest level of servicing.

Attempting to maintain a profitable business against this backdrop of continuous fee compression and growing costs is, of course, unsustainable. For many custody providers, operating in mature European markets often means having to accept a negative cost-income ratio. So what's the solution?

## Profitability tactics

Banks have used a number of tactics to address the profitability challenge. The first, and most popular, is simply to go for scale and process as much volume as possible, typically going offshore to keep costs ultra-low. The second is to hope that offering custody as a loss leader will bring in other reciprocal business. The third is to accept the status quo and look to other markets such as Asia and Central and Eastern Europe, where pricing hasn't been so sensitive, to help cross-subsidise custody activities closer to home.

But all three tactics have their issues. Processing huge volumes for little return on equity isn't a business model that even the biggest banks want to be seen to rely on now, and clients are often vocal in their dislike of being serviced offshore; client business reciprocity has stubbornly failed to materialise.

Finally, as regulation now demands banks carry a capital charge for non-profitable business, simply cross subsidising loss-incurring European business with profitable business in, say, Asia and Central and Eastern Europe is far more challenging. Plus, it's only a matter of time before the same pressure on fees hits these markets in the same manner.

Put bluntly, allowing custody services to muddle along unprofitably and inefficiently can't last much longer, as many banks have started to realise. We've already seen some major names exit certain business lines, such as clearing, as they look to redefine their business models. Banks are also exiting unprofitable or imbalanced client relationships, forcing smaller and less well-capitalised institutions and intermediaries to look elsewhere for the services they need.

But while banks begin to address unprofitability, they aren't necessarily tackling the underlying problems that are making custody and asset servicing so unviable. In our view, a real sea-change is required over the next three-to-five years in how banks provide post-trade services if the industry is to remain stable, sustainable and deliver the reliability and efficiency that clients require. Here are the key areas that need to be addressed:

**Legacy systems:** most banks are still working with aged systems and platforms that are complex, inefficient and light years from the level of functionality being used in other sectors. A 2014 study showed that the average age of a securities platform in Europe is 18 years or more. That's equivalent to using a Nokia 3310 when the rest of the world is using the iPhone 6.

Overhauling a proprietary global mainframe platform can easily cost €100 million or more. Given that banks have been diverting all of their resources to keep up with regulatory change over the past eight years, that's capital most simply don't have available.

This is largely why we are starting to see some major high profile IT outsourcing announcements. By transferring to third-party platforms rather than changing their own technology, banks are citing cost savings of up to 40 percent, and this outsourcing will be a continuing trend among the big players.

**Lack of fee transparency:** post-trade billing has become overly complex, with hundreds of charge points and lack of clarity on new billing items that were previously bundled, such as corporate actions. The challenge of reconciling bills and invoices is such that most clients now simply look at, and make a comparison between, the headline amounts each month. Effective reconciliation in most cases is pretty much impossible.

Industry standards on certain price components are now sorely needed to ensure transparency, to reduce the administrative burden on clients, and to align with the post-credit crisis ethos of openness and honesty.

**Realistic pricing:** open and honest conversations need to be held with clients as to what is fair but sustainable pricing, taking into account balance sheet and regulatory demands. This is an educational process. If clients want a partner that will be there for the long term, and which isn't going to abruptly pull out of the market under pressure from shareholders, then realism about the risks and costs of doing business is required.

No one has bitten the bullet yet, but we anticipate at some point, banks will look to charge explicitly for services such as intra-day credit, which clients currently expect to be provided for free. There are also some compelling opportunities for banks to charge for other products and services where they can add substantial value—for example, helping clients to navigate regulatory change by providing trade depository reporting services.

The key will be to sit down with clients and ask them what they want and what they are willing to pay for, which is not exactly a revolutionary step, but one that is not being taken right now.

## A new business model

For too long, banks have tried to be all things, in all markets, to all people. The need to manage risk-weighted assets and balance sheet consumption are forcing service providers to abandon that volume approach.

Now, banks need to define their strengths, show where they can add value for particular groups and work out a focused, long-term sustainable business model. This is particularly urgent now that so many other participants, including exchanges, CSDs and CPP, are seeking to encroach on service providers' business to recoup revenues lost on their traditional service offerings. Most of all, banks need to work out how to tackle the burden of sometimes enormous internal overheads and cost allocations, which so often affect the bottom line performance of a service unit.

As regulation starts to settle down and banks have more time and space to think about their future business strategy, I'm hopeful that change will occur. We are already seeing the glimmerings of some exciting disruptive technology that could transform how our business operates, and that needs to be accompanied by some bold innovation in fees and pricing transparency.

In five years, I would hope that the world of post-trade will be very different. If it isn't, the ability of the industry to service the long-term needs of its clients will be severely compromised. **AST**

**Robert Scott**
Head of custody and collateral solutions
Commerzbank

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# The end of grace: more pain on the way

## As grace periods come to an end and legacy systems are found wanting under the weight of regulatory scrutiny, the pressure will grow to come up with sound, persistent solutions that greatly diminish the threat of crippling fines and levies. Simon Shepherd of MYRIAD reports

Recent regulatory enforcement and hefty fines from the UK Financial Conduct Authority (FCA) came with a stark warning from Georgina Philippou, the then acting director of enforcement and market oversight: "[F]irms with responsibility for client assets should take this as a further warning that there is no excuse for failing to safeguard client assets and to ensure their own processes comply with our rules."

The FCA's statement made it extra clear that custody rules require firms to "keep entity-specific records and accounts", because they are required in the event of insolvency. Without them, client assets cannot be safely returned. Additional requirements include the obligation to: conduct entity-specific external reconciliations; maintain an adequate Client Assets Sourcebook (CASS) resolution pack (from 1 October 2012 when the requirement to do so came into force); and submit accurate client money and asset returns (CMAR) (from October 2011 when the requirement to do so came into force).

But in these areas, the fined financial institutions had been found wanting. Specificially, they failed to take the

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necessary steps to prevent the commingling of safe custody assets with firm assets from 13 proprietary accounts; used safe custody assets held in omnibus accounts to settle other clients' transactions without consent; and failed to implement CASS-specific governance arrangements that were sufficient given the nature of the firms' business and their failure to identify and remedy the failings identified.

It was not just the operations area at various banks that had come in for scrutiny. The serious rule breaches had typically not been spotted by the banks' internal compliance teams, either. It is safe to assume that the level of internal communication and information sharing, and the setting of standards internally at many banks, had fallen somewhat short of the FCA's expectations. The issue is whether they continue to do so.

It is clear that many banks have taken steps to correct these shortcomings, however, it is a worthwhile exercise to look at why and how such situations arose in the first place and, more importantly, what lessons can be learned from this episode for all major financial institutions. A key question has to be: to what extent do many interim measures put in place over the last six or seven years, sometimes even longer, continue to meet the ever-more demanding needs of their owners?

Part of this examination must necessarily look at the environment within which all financial institutions, and particularly banks, are working. Inevitably, this means that the regulatory regimes around the world will be part of the discussion. Much of the regulation put in place after the financial crisis is starting to bite and is being extended. The Organisation for Economic Co-operation and Development has come up with the common reporting standard (CRS) modelled on the US Foreign Account Tax Compliance Act (FATCA). Fifty-one early adopter nations signed up to the CRS principles in October 2014 and the first information exchanges will take place by September 2017. CRS has significantly increased the scope and complexity of existing (FATCA) projects. Many tactical solutions are, or will be, unsustainable.

Furthermore the Basel Committee on Banking Supervision's 14 principles for aggregated risk reporting (BCBS239) will progressively affect the industry through 2015 and 2016, and will necessitate radical overhauls of governance and infrastructure, risk aggregation capability, risk reporting, and overall supervisory reviews.

The fact is that a lot of solutions that have been cobbled together since the financial crisis are now coming under intense scrutiny and many of them are being found inadequate. In-house systems that might have been deemed 'robust enough' and put in place as stop-gaps over the past six years lack sufficient depth, breadth, sophistication and persistence to deal with this raft of regulation satisfactorily. Legacy systems that might even be older than this are also suffering from under-investment and can be deemed no longer fit-for-purpose.

All of these concepts—functional capability and persistence, in particular—are key to the definition, design, development and deployment of any solution. Indeed, in-house solutions frequently fail to address all four of adequately, if at all. Part of the problem with in-house solutions is that they are designed, indeed destined, to fail from the outset and it comes down to vision, knowledge and the ability to execute in a timely and cost-effective fashion. 'Robust enough' is typically indicative of not being robust at all in times of stress.

Why would a large bank not maintain segregated accounts as required under the FCA's CASS? The only two reasons must be cost and/or capability. In the past, it must have been cheaper to maintain omnibus accounts anyway, but part of the cost consideration is the supposed difficulty in maintaining and administering segregated accounts.

The mechanics of maintaining segregated accounts are straightforward, if you have the right technology. Building the right technology, in-house, is slow and costly and perpetually 'behind the curve'. The main criteria for assessing any project of this nature—those of being functionally robust, timely and cost-effective—have consistently not been met by in-house projects. Banks need to focus on definition and deployment, not design and development, and the best use of a bank's money is to book-end the technology with saying what they want (requirements) and making sure it 'goes in' properly (implementation). Leave the rest to the experts.

A good example of this would be what needs designing into a system on the back of requirements to open up access to multiple departments, permitting better coordination and collaboration, and reporting and management information systems. Simply declaring that a new nostro database will be built is all well and good, unless it: (i) costs 10 times what is available on the market, (ii) only does 10 percent of what is available on the market; and (iii) takes three years to deliver, when an industry standard can be deployed in six months.

Any shareholder would question the value of doing this, and wonder whether their investment might be better spent elsewhere. The value-for-money argument throws into sharp relief any justification for developing in-house.

And here's the rub: grace periods are running out in the next two-to-three years. The 'robust enough' approach is about to get very expensive. When an FCA fine could have paid for a 1,000-year licence to software that could easily have solved these issues 10 years ago, senior executives need to re-cast their eyes over empire builders and in-house technologists, and rapidly acquaint themselves with what is available in the wider world.

In-house software systems are, by definition, 'legacy' from the outset. They lack a clear upgrade path, they suffer from infrequent release cycles and the absolute cost of ongoing maintenance means they can rapidly fall into disrepair. The job of a chief information or technology officer should be to determine that 'best-of–breed' is the preferred approach, even if it means going externally, and that in-house development really is the last resort.

Investment should be made in definition, deployment and integration, not design and development. The economics of in-house development rarely stack up and the opportunity cost of a slow, relatively expensive development project means that long-term returns remain a pipe-dream.

Irrespective of the cost of maintenance and upgrades, the compliance cost of keeping up with regulation often means starting projects anew, yet the inertia of in-house systems means that fresh change and adaptability are difficult to achieve. The very nature of internally developed systems means they are often standalone, further hindering ongoing development. The resource responsible for the original project has almost certainly left the institution, so continuity and persistence become additional problems.

Reasons given for the development of in-house software systems include operational efficiency, business growth, keeping up with regulatory initiatives and both system consolidation and cost reduction—all of which can be much more readily achieved by buying a purpose-built platform.

Indeed it could be argued that in-house development projects have often actually increased operational risk, rather than reduced it. Given the obvious shortcomings of in-house projects and given the time-to-market deadlines that a series of end-of-grace periods represent, it must make sense for banks to acknowledge that the functionality exists to properly address these issues. This functionality is constantly evolving. What they need to do is to examine what they really want, where it sits and how best to use that functionality within their operations' teams. **AST**

**Simon Shepherd**
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# Europe's quest for transparency

## Guidelines from ESMA will have a profound impact on brokers and their clients. Those looking to make a smooth transition will need to make some important choices, but they also have an opportunity to position themselves for the future. Experts from GBST take a look

For the financial industry, an era is about to end. The European Securities and Markets Authority (ESMA) is expected, later this year, to issue guidance spelling out how the cost of broker-provided or independent financial research should be broken out and charged to clients.

This dry-sounding change may not seem as transformative as some of the landmark measures that have been enacted in the wake of the global financial crisis, but it is, and it has far-reaching consequences for how both the sell side and the buy side do business.

The changes are part of a drive to increase transparency in terms of what banks and brokerages do and how they charge clients. The measure will mark the end of nearly a decade and a half of self-regulation, during which investment banks and their institutional customers were largely left to themselves to come up with a practice commonly known as commission-sharing agreements (CSAs).

Many concede that CSAs have little chance of surviving in their present form, although some industry participants believe that CSAs, with some changes, represent the best approach.

Whatever replaces them will require sell-side

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and buy-side institutions to make significant changes both to their back-office systems and their business practices.

At the moment, broker costs are based on an equity market model that has three components: a charge for execution, an amount for providing research and a small market fee, which is essentially the cost of doing business.

"While there is an element of market charges attached to a commission value, the real issue is trying to dissect any research payment from the cost of execution," says Denis Orrock, CEO of financial software and services provider GBST.

What's more, in following an equity market model, ESMA is raising another issue for the industry. "ESMA now is looking to implement this idea across other asset classes, which means potential unforeseen consequences in the fixed income world," says Shaun Blake, a principal partner at consultancy Sheperdine Sand.

"That's a massive headache for organisations to comprehend at this stage. Research and commission are embedded in the pricing model, so there are fundamental changes on the way."

A major focus in ESMA's efforts is providing investor protection, but this raises yet another issue. The UK Retail Distribution Review sought to bring transparency to retail investors by ensuring commissions were disclosed up-front rather than through murky trail commissions paid by product providers. ESMA is trying to apply similar principles in the Markets in Financial Instruments Directive (MiFID) II to the institutional side, but the level of granularity required will be difficult to administer on both sides, with some vendors currently unable to meet this requirement.

## Rising to the challenge

Once ESMA comes up with a decision on commissions, there will be three key factors market participants will need to consider.

The first factor is what type of technological solution they pursue. Second is whether they can build a robust solution, or whether a vendor can deliver one in time for the ESMA changes due in 2017. Finally, there is the question of future-proofing operations for the inevitable changes in regulation that will follow as processes are bedded in.

"At a technological level, firms should consider taking a holistic approach to codifying agreements between brokers, asset managers and funds," says Nick Clarke, head of products at GBST Capital Markets.

"Market participants will need a system that can log any transaction, and by extension log a transaction against a research account based on a complex set of rules. Whatever the rules that ESMA finally comes up with, if those elements are in place market participants should be able to make the transition relatively painlessly."

Blake says there is an opportunity for a systems provider to act as a central hub, which does all of the filtering, calculations and comparisons and which then connects with clients' payment systems, eliminating a large amount of manual work.

"GBST has extensive experience in middle- and back-office applications and matching around the post-trade space," adds Clarke. "GBST is also versed in dealing with fragmented silo-based systems infrastructure, where current capabilities don't spread across all of those asset classes."

A second but equally important area for market participants will be how ready a brokerage firm or a solutions provider is to address the requirements that ESMA sets. These changes form just one item on a long list of new measures addressing market infrastructure and business practices. Sell-side and buy-side firms have been scrambling for the past few years to keep up with the pace of change, and allocating the time and resource to cope with more adjustments is not always easy.

Finally, there is the future to think about. Experience shows that regulatory measures are rarely set in stone. They are frequently updated and tweaked, with different formulae changing all the time. So firms need to make sure they build or choose a system that can cope with all the change. By outsourcing this function, banks and institutions wouldn't need to worry about keeping on top of the ever-increasing amount of regulatory information.

Clarke says that modern technology allows for research budgets and commission agreements to be codified and continuously adapted as agreements and regulations change, ensuring the cost of compliance is minimised.

ESMA's stated desire to make changes across asset classes highlights the importance of this last factor. As Europe formalises the way that research ideas are priced, having a single central solution that can cope with all the different technical issues could be a critical issue for firms.

Some firms are trying to get ahead of the curve by working with their clients to price research. At the moment, there is no clear holistic answer for the industry.

In the end, European officials are asking themselves a question that sounds simple: how should firms set a price for research? Whatever the answer, the new dynamic for market participants is likely to be anything but simple. **AST**

"These changes form just one item on a long list of new measures addressing market infrastructure and business practices. Sell-side and buy-side firms have been scrambling for the past few years to keep up with the pace of change, and allocating the time and resources to cope with more adjustments is not always easy"

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# Riva Financial Systems: new needs, fresh thinking

## Transfer agents and fund administrators should take note of Riva Financial Systems Limited, an Isle of Man-based software company with a formidable solution

Nestled away in the peaceful surroundings of the Isle of Man is a thriving niche software company that is making a big impression on the asset servicing industry. Riva Financial Systems is a software company that has developed a global transfer agency system capable of supporting multiple countries and investment products on a single platform.

### A systematic approach...

Riva Financial Systems was founded by four industry innovators, each with extensive experience of operations and technology at some of the largest asset managers and fund administrators in Europe. Their vision called upon the creation of a flexible, cost-effective, totally integrated global transfer agency system solution to leverage best-of-class technology and servers, and the flagship product that emerged from this blueprint was Riva Transfer Agent (TA).

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Riva TA comprises a range of features designed to make transfer agency operations more efficient and responsive to both client needs and market changes, by allowing customers to consolidate all of their servicing requirements onto a single platform, substantially reducing costs and increasing operational efficiency.

As a modern service orientated architecture application built using best-of-class technology and servers, we believe Riva's software to be more robust, scalable, flexible and cost-effective than any other single-platform solution.

Suitable for both transfer agent and alternative fund administrator, Riva TA is a highly functional dealing and registration software solution capable of supporting the entire investor record-keeping process across multiple administration centres, investment products and currencies, all on a single platform with a very low total cost of ownership.

It also comprises a range of features designed to make transfer agency operations more efficient, flexible and responsive.

Riva TA offers, among other features, a web enabled front end for ease of servicing, integrated cash management and general ledger advanced functionality, integrated imaging and workflow functionality, enhanced foreign exchange processing, and interface capabilities with an open database architecture.

To fully complete its value proposition, Riva maintains a team of highly skilled business analysts, software quality engineers and developers recruited from within the financial services industry to ensure that design,

**The Riva advantage**

Riva TA is in a class of its own for several reasons:

implementation and support issues are always addressed in the appropriate business context by individuals with the required expertise.

To date, Riva TA has proven successful with customers in all three major European jurisdictions, including the UK, Dublin and Luxembourg, and has been successfully deployed across the entire UK and International transfer agency operations at Franklin Templeton in a project described as being "unprecedented in terms of scale and complexity".

As of March 2015, approximately $280 billion of assets were administered on Riva TA by clients of Riva, across 14 global locations covering Asia, the Middle East, Europe and the US, with deployment and implementations in other jurisdictions already under way.

### Learn more

We understand that when it comes to researching shareholder record-keeping technology solutions, it can be a challenge to clearly differentiate one from another.

Should you wish to learn more about Riva TA, please contact us and we can set up a 'phone an expert' discussion, offering you an informal yet detailed conversation with one of our technical experts about any of Riva TA's features or functions. We would also be happy to arrange an on-site visit, where a Riva representative will visit you to discuss your business needs and determine whether Riva TA is an appropriate solution for you.

To learn more about Riva TA's potential within your organisation, please visit our website www.rivafs.com or alternatively please call us on +44 (1624) 850 140 or email learnmore@rivafs.com

**Ghassan Hakim**
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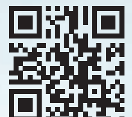

## Industry appointments

LCH.Clearnet Group has appointed **Ali Hackett** to the newly created role of global head of sales and relationship management, based in New York.

Hackett will be responsible for maximising the value, reach and range of the group's existing customer relationships, while pursuing new member and client business opportunities.

She will report to group CEO Suneel Bakhshi, and will be a member of LCH.Clearnet's executive committee.

Previously, Hackett served as an industry advisor with Formation 8, helping portfolio companies to develop client partnerships. She has also served as senior managing director of global client development and sales at CME Group.

Before this she spent nearly 20 years at Citi, serving in various positions of increasing responsibility and finishing as co-head of global prime finance.

Bakhshi commented: "Hackett's experience, expertise and deep knowledge of our industry will further strengthen our global management team. In her new role, she will be integral to ensuring that we maintain a harmonised approach in our relationships with customers."

Hedge funds service provider Enso Financial Analytics has hired **Julian Pittam** as head of Europe, the Middle East and Africa, and **Stephen Caplen** as global COO.

Pittam and Caplen will operate out of Enso's London office and join the company's global executive management team.

Prior to his new role, Pittam served at Data Explorers, now known as Markit Securities Finance, and was responsible for building on the product and client base.

During his seven years at Data Explorers, Pittam established offices in the US and Asia and in 2007 he was named head of sales and marketing. He was also head of institutional marketing for equity and prime finance at Lehman Brothers International in Europe.

Caplen was previously deputy group CFO at ICAP. Before this, he ran ICAP's global IT infrastructure and global business services departments.

Pittam said: "Fast-growing companies with great products and excellent management teams are the most exciting and challenging places to work. I look forward to working with the existing team in Europe as we build our presence."

Caplen added: "Market participants are confronted with extraordinary changes in market conditions that call for exceptional solutions."

"ENSO has successfully brought to market a solution that addresses unprecedented regulatory pressures and the ever-rising cost of capital on dealers' balance sheets. I look forward to working with ENSO as we bring this new model to international markets."

Barclays has appointed **Steve Rickards** as head of offshore funds.

He will lead the creation and implementation of the bank's offshore funds strategy and report directly to Paul Savery, managing director of personal and corporate banking in the Channel Islands.

Rickards has 30 years of experience with Barclays, working in its corporate banking and international finance centres.For the last four years he has been heading up the Guernsey Funds team, providing debt solutions for private equity and working with locally based fund administrators.

Savery said: "Barclays's funds segment has seen some terrific cross-functional success over the past year or so."

"Specifically, the offshore business has worked hand-in-hand with the funds team in London to bring the very best of Barclays to our clients, and [Rickards] has been a real catalyst to driving this relationship from a Guernsey perspective."

**Olivier Grimonpont** is taking over as global head of collateral management services at Euroclear.

Grimonpont, who is currently CEO and regional head of the Asia Pacific in Euroclear's Hong Kong branch, will move to Brussels. He has worked at Euroclear since 1999, having moved to Hong Kong in the summer of 2010 to take on regional duties for the Asia Pacific. **AST**

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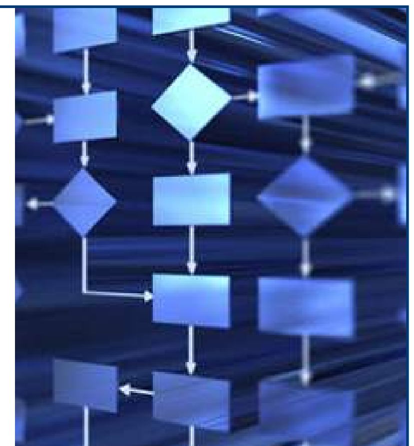

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