ISLA Daily 3

30th Annual Securities Finance and Collateral Management Conference

Thursday, 22nd June

The EquiLend ecosystem

Kevin McNulty reviews the first year of its RegTech Solutions division

Day three agenda inside

Panellists encourage market collaboration to tackle RWA pressures

Market participants need to partner to find solutions to mitigate risk-weighted asset (RWA) pressures across the industry that are derived from Basel IV regulation, according to The Trading Renaissance panel at the ISLA 30 Conference in Lisbon.

The anticipated Basel IV rules have become a much debated topic that panellists expect will have a large impact on market participants in Europe.

The Basel Committee on Banking Supervision (BCBS) redrafted the entirety of the risk-weighted assets (RWA) framework for Basel IV. The regulation presents an increased focus on the standardisation of risk weights and moves away from the European Central Bank (ECB) and Bank of England (BoE) internal model, explained one panellist.

Basel III/ IV regulation is a set of international standards developed by the BCBS, which produced a framework of measures to strengthen the supervision and risk management of banks.

Reviewing Europe and the UK specifically, one panellist indicated that there should be no minimum haircuts for securities financing transactions (SFTs).

This point was also raised within the recently published Prudential Banking Rules: Explanatory Note, which was created by the International Securities Lending Association (ISLA). The paper indicated that minimum haircuts for SFTs under the Basel III reforms could prove challenging for the industry.

The panellist also highlighted that an Output Floor requirement under the UK and Europe regime means that banks will have to recalculate their exposure using the standardised approach, which will have an impact on the market.

For banks under the UK regulation, the RWA for unrated corporates and unrated sovereign and central banks will become "extremely punitive", conference attendees heard, as these entities could be rated with 100 per cent risk weight.

The Basel IV regulation will be implemented through a phased implementation that began on 1 January 2023 and will take five years to come fully into force. It will undoubtedly create further discussions for the industry as market participants work to adopt the redrafted framework.

Settlement efficiency remains point of concern for sec lending industry, says BoE's Pyzer

Settlement rates remain a point of concern for the securities lending industry, delegates heard at ISLA's 30th Annual Conference in Lisbon.

Jon Pyzer, senior adviser at the Bank of England, told the audience that failure rates for the return leg of a securities lending trade are often above 10 per cent and are sometimes close to 20 per cent in times of high trading volumes. "Settlement frameworks for securities lending trades are not functioning as they should be," he observed.

To address this inefficiency, the Bank of England has established a working group to understand the causes of high settlement rates and to look for solutions. The group anticipates that advances in technology offer potential for significant improvements in straight-through processing (STP) rates across the securities finance transaction lifecycle from pre-trade to closure of the return leg.

However, for Pyzer, the challenge is broader than technology adoption and also lies in motivating firms to change their settlement culture as well as to upgrade their workflow.

Twenty years ago, he recalls a fierce commitment across counterparty firms to ensure that a trade did not fail. Subsequently, he suggests that this commitment has diminished and it is important to refocus on eliminating trade fails, particularly in advance of a future move to T+1 settlement in line with the US, Canada and India.

In planning for next-day settlement, an HM Treasury task force has been established to evaluate the case for T+1 and to scope out the requirements for this to be delivered. In earlier times, when securities were delivered physically from one settlement counterparty to another to complete transfer of ownership, there was a case for working with T+3 (or longer) settlement windows. Now that these transfers take place electronically, the case for settling on T+2 is substantially weaker.

These steps to drive improvements in settlement efficiency will be one element of the Bank's forthcoming plans to review and update the Money Markets Code (MMC), planned for 2024.

The existing code has been in place since 2017 and was drafted by the market with the Bank of England standing as facilitator. The Code has four sections, with its overarching principles and ethics followed by chapters on unsecured financing markets, repo and securities lending markets.

As part of the MMC review, working groups have now started to review each of its existing chapters, updating its content and "keeping it fresh".

The MMC is a voluntary code, Pyzer explains, with more than 200 firms on the register that have signed up to the Code. In case of a breach, the Bank has mechanisms to voice its disapproval and to advise that market participants should change their behaviour. The recent case of an EU bank borrowing stock to vote at a company AGM — when Mediobanca borrowed shares in the London market in Trieste-based insurer Generali — provides an example where the Securities Lending Committee made clear its disapproval in the minutes of its quarterly. meeting and the UK Money Markets Subcommittee wrote to all signatories to condemn this practice.

The Bank of England Securities Lending Committee was established in 2017 and is a sub-committee of the Bank's Money Markets Committee, involving participants from across the market to discuss development activity, efficiency and stability in unsecured financing, repo and securities lending.

Membership is drawn from across the industry, embracing buy-side, sell-side and their relevant service intermediaries. Members join by invitation from the Bank.

In the discussion, which was moderated by ISLA's head of legal services Tina Baker, Pyzer emphasised that the work of the Securities Lending Committee aligns with the central function of the Bank of England to ensure monetary and financial stability.

Pyzer highlighted the central role that the Bank had played in restoring financial stability in response to the UK gilts crisis that extended from late September into early October 2022, when he observes that the "gilts market was not in a stable format" and many LDI funds were facing large margin calls on the repo and derivatives positions.

"The Bank announced that we would buy the long end of the gilts market," he says, making a commitment to buy up to £65 million in gilts holdings if required. "Our presence in the market was fundamental in breaking that 'doom loop' and to restoring stability," he concludes. In practice, the BoE bought £19.3 billion in gilts through its temporary asset purchase programme, well below the £65 million threshold that it had announced, and completed its unwind of this tranche of gilts holdings in January 2023.

Securities finance firms face turbulent tax environment

The securities lending industry is navigating a "somewhat tricky" and "slightly turbulent" tax environment with increased scrutiny from tax authorities across Europe, according to the Legal & Tax Initiatives 2022/23 panel at the ISLA 30 Conference in Lisbon.

The panel provided an overview of the tax environment in which the securities lending industry operates and the challenges the industry is facing from a tax perspective.

Tax rules have always existed on securities lending and continue to evolve, one panellist confirmed.

In 2018, tax came into the spotlight when a consortium of investigative journalists in the EU shone a light on the cum-ex scandal. In the same year, the European Parliament estimated that, at that time, approximately €50 billion was lost to aggressive cum-ex countries in Europe.

Following these events, associations including the European Securities and Markets Authority (ESMA) and the European Banking Authority (EBA) launched investigations into such schemes.

Currently, the industry is required to comply with an extensive body of legislation requiring market participants to implement robust tax reference frameworks for identifying, mitigating and reporting potential tax abuses, conference attendees heard.

Some initiatives target aggressive forms of securities lending, for example, anti-CoCo circulars in Germany. Some initiatives are more general in their application, such as the Organisation for Economic Co-operation and Development's (OECD's) Mandatory Disclosure Regime. And some "perfectly sensible" initiatives, a panellist noted, have had unintended consequences for securities lending.

The discussion on tax concluded that tax rules should be clear, intelligible, predictable and certain so market participants can confidently comply with their obligations.

In addition, member states need to strike a balance between promoting business and fair play, tax collection and control of tax abuse to maintain the efficiency of capital markets.

EquiLend and Broadridge collaborate to streamline central clearing of SFTs

EquiLend and Broadridge Financial Solutions have formed an agreement to facilitate straight-through processing (STP) to the National Securities Clearance Corporation's (NSCC) central counterparty for equity securities finance transactions (SFTs).

The offering will allow clients to trade and automatically submit through the Broadridge SFT Submission Service without a large change in operational processes. It will also utilise EquiLend's liquidity sourcing options.

Clients will profit from the capital cost and risk reduction benefits of central clearing through the new offering, according to the two firms.

The Broadridge SFT Submission Service aims to provide the market with the capability to meet the NSCC requirements to match and submit through an approved trade submitter.

EquiLend's 1Source — a distributed ledger technology (DLT)-based single source of truth for SFT lifecycle information — is designed to direct securities lending trades seamlessly to the NSCC for central clearing through Broadridge's Trade Submitter Service.

According to EquiLend, more than 2.2 million global transactions are executed on the technology firm's Next Generation Trading (NGT) platform each month, which translates to more than US$2 trillion in total notional value.

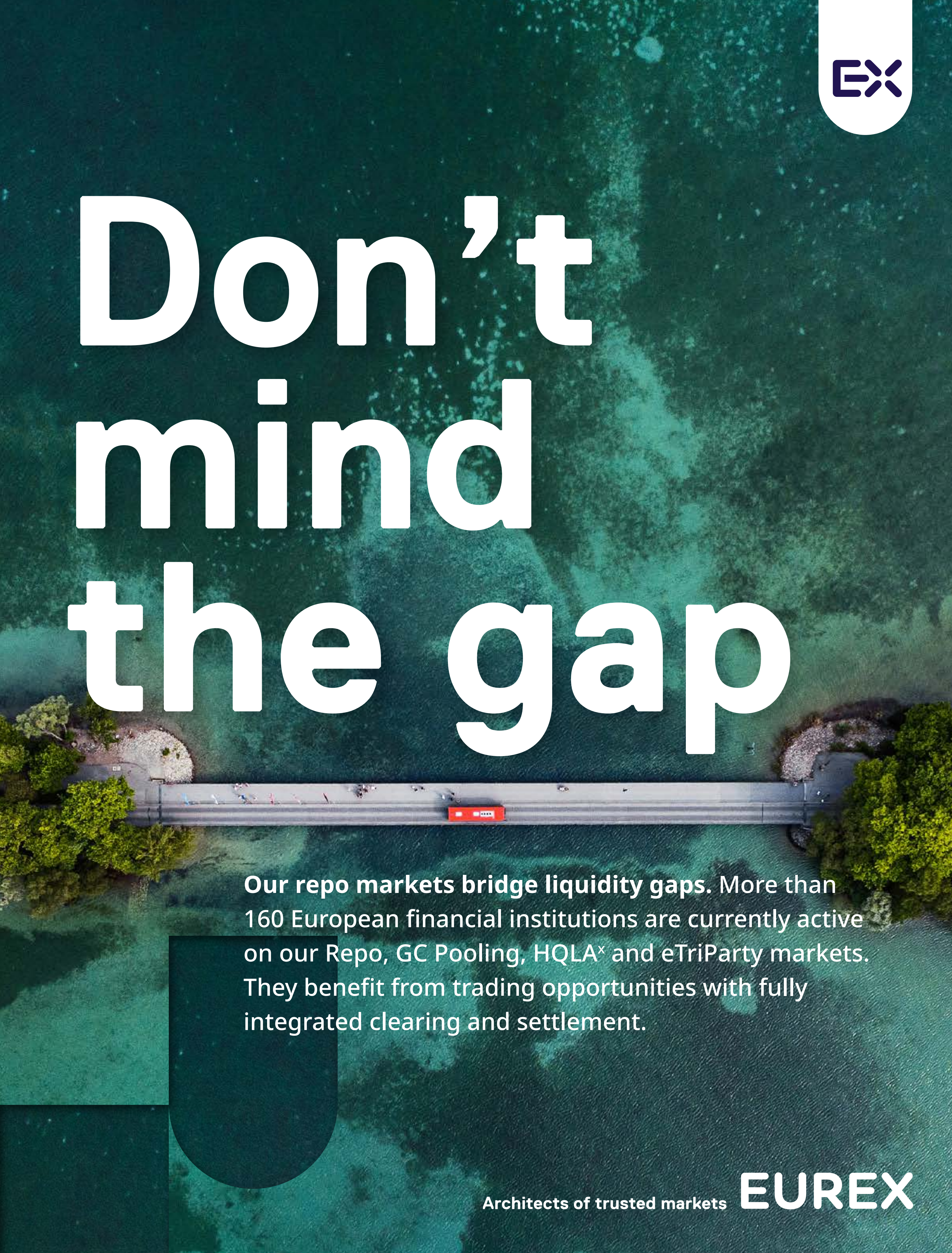
US equities, which are eligible for central clearing with the NSCC, form the largest segment of securities on loan in the global securities finance markets, the firm adds.

Commenting on the announcement, CEO of EquiLend Brian Lamb says: "We are pleased to be working with Broadridge to offer our clients streamlined access to the benefits of central clearing.

"EquiLend is committed to working with our partners in the industry to bring new efficiencies and unprecedented interconnectivity throughout the global securities finance marketplace."

Darren Crowther, head of securities finance services at Broadridge, comments: "We are delighted to be able to offer our joint clients straight-through processing to central clearing via our SFT Submission Service platform.

"Interoperability across our platforms, as well as the entire trade lifecycle event workflow, will enable our clients to benefit from the advantages of the NSCC offering while minimising the time to market due to our out-of-the box connectivity."


Don't mind the gap
Our repo markets bridge liquidity gaps. More than 160 European financial institutions are currently active on our Repo, GC Pooling, HQLA^x and eTriParty markets. They benefit from trading opportunities with fully integrated clearing and settlement.
Architects of trusted markets
EUREX

Kevin McNulty
Head of RegTech Solutions
EquiLend

The EquiLend ecosystem: forming connections through solutions

One year on from the launch of EquiLend's RegTech Solutions, head of the division Kevin McNulty reviews its accomplishments over the past 12 months, the top concerns for market participants and implementing new technology amid mandate changes

EquiLend's RegTech Solutions division has been up and running for one year now. What has been your main focus and accomplishments over the past year?

Although we created the division last year, EquiLend has a long history of providing regulatory solutions for our clients, tracing back to the development of our core Agency Lending Disclosure (ALD) service in the 2000s. Having joined EquiLend at the end of 2021, and having had a few years out of the industry, it was clear that regulatory developments remained a dominant issue for firms. It made sense to create a specialist team to focus on helping clients with their compliance needs. I was delighted to have Iain Mackay, who was previously responsible for our Post-Trade Solutions group, join me to run the division on a day-to-day basis. We have been growing the team ever since with specialists in London and New York.

One of EquiLend's strengths is the ecosystem that we have developed. We connect firms operating in securities finance with each other through a wide variety of our solutions designed to reduce friction, risk and cost. RegTech is an important part of that ecosystem.

What are the biggest concerns for market participants right now and where is the focus for the RegTech division?

One of the first concerns we noticed was the challenge of onboarding new beneficial owners into securities lending programmes. The ALD protocols developed over a decade ago included some basic messaging to help with this, but with the increasing focus and complexity associated with onboarding, the whole process is a major pain point for the industry.

By listening to our clients and understanding their needs, we developed our Onboard+ solution, which incorporates an enhanced version of our ALD offering with a state-of-the-art know-your-client (KYC) and client integration platform. Onboard+ aims to achieve reduced onboarding times for beneficial owners and includes tools which give lenders and borrowers unprecedented insight into the pipeline of new funds coming to market.

Looking ahead, we are focused on the proposed SEC 10c-1 rule, which would require lenders in the US to disclose their transactions and positions to regulators who, in turn, would publish the data in an anonymised form. It is the US version of the Securities Financing Transactions Regulation (SFTR), so to speak, but, as currently proposed, the SEC 10c-1 rule has some material differences to the European regulation. One of these material differences is a requirement to report transactions within 15 minutes of execution. There has been a large amount of pushback from the industry on this point, as well as other features such as reporting lender availability. The market must wait and see what the final rule says, which is expected to be published later this year. We have engaged with the SEC on the proposed rule and are prepared to support clients should it come into force as proposed.

Earlier you mentioned the EquiLend ecosystem. Outside of RegTech, what are some of EquiLend's current priorities across the firm?

The move to a T+1 settlement in the US and Canada is a top priority for our clients. The key to operating successfully in a shortened time frame is to be as efficient and as automated as possible. To that end, we have been busy enhancing our suite of post-trade solutions. Firms that take advantage of these to automate workflows around returns and recalls, exposure monitoring and transaction settlement on a real-time basis should be well placed to manage the change.

"Firms are challenged and have limited bandwidth to implement new technology, but most recognise that maintaining outdated legacy systems is costly"

Of course, being able to trade and cover positions efficiently on our NGT trading platform is also part of the toolkit that firms can take advantage of. NGT trading volumes continue to grow steadily, with 2.5 million transactions executed on NGT in May across more than 110 global firms. We continue to enhance NGT functionality to support the various needs of our large client base. As an example, earlier this year we launched Competitive Bid, a new NGT functionality specifically designed for non-general collateral (GC) trading, which has been popular among clients looking to eliminate time-consuming manual trade executions ahead of the shift to T+1.

We continue to see increasing demand from clients for increased and improved data. Our current focus has been to develop tools and solutions that provide for more real-time data on securities finance markets and to deliver this in ways that support how our clients actually work. New user interfaces, new data points and integration into other solutions such as NGT and Onboard+ are some of the highlights this year.

With a focus on regulatory compliance and shortened settlement cycle in North America, do firms have the bandwidth to implement technology that is not directly impacted by these mandated changes?

Firms are challenged and have limited bandwidth to implement new technology, but most recognise that maintaining outdated legacy systems is costly. Market participants know that to stay competitive with their peers, they need to employ the latest technology. One area where we are helping and where we see strong demand is our EquiLend Spire platform, which is a full end-to-end books and records system. There are a number of advantages of using Spire — it is a fully modular solution, so clients can take the full solution or just the components that they need; the job of maintaining and upgrading the platform is effectively outsourced to EquiLend; and it comes integrated with our full ecosystem of Trading, Post-Trade, Data & Analytics and RegTech Solutions. The demand for Spire has been incredible and is a sign that firms continue to invest in this business.

Digital transformation has been a hot topic among fintech firms. What is EquiLend doing on this front?

Two years ago, we established a Digital Transformation Working Group which included many of the main players in our industry and drew people from business and technology. The first objective of this group was to identify problems that digital technologies would be best placed to solve. Having reviewed a number of industry pain points, they concluded that the elimination of trade reconciliations would be an ideal problem area that could be solved through the deployment of distributed ledger technology (DLT).

Roll on a couple of years and we are in development of our 1Source solution, which is now entering the pilot phase. 1Source will facilitate the creation of a single immutable record on a distributed ledger for every securities finance transaction, completely eliminating the need for firms to reconcile their own representations of the same transaction. Based upon analysis conducted by external consultants, the cost saving for the industry of doing this will be huge. We see 1Source as the platform to support the development of future solutions for the industry, including regulatory reporting. Interoperability is a priority for clients — 1Source will be fully interoperable with the EquiLend ecosystem and is open to connectivity with other technology platforms and solutions.

Brian Ruane
CEO
BNY Mellon

Navigating the market: driving efficiency across clearance and collateral management

Against a backdrop of market uncertainty, Brian Ruane, CEO of BNY Mellon's Clearance and Collateral Management business, explains how the firm is navigating the changing environment for its clients

The year began with increased optimism. Markets were stabilising, inflationary pressures were receding, and the usage of the Federal Reserve Repo facility had begun to fall from its 2022 year-end peak of US$2.55 trillion. In addition, there were early signs of movement from the Federal Reserve Repo facility returning to traditional tripartyand outright purchases of treasury bills and short notes by money market funds.

Despite these positive signs, uncertainty quickly followed — with higher inflation numbers, increased rate volatility, bank failures, geopolitical risk from the war in Ukraine, heightened tensions with China and US debt ceiling negotiations. Therefore, by the start of Q2, the mood had begun to turn from optimism to concern — with businesses now focused on the efficient utilisation of financial resources.

For our clients in the clearance and collateral management business, this has manifested itself in several ways.

Providing financing solutions across the balance sheet

Against an uncertain backdrop, it is becoming increasingly important to enable financing solutions across as much of a firm's balance sheet as possible. In that vein, BNY Mellon has plugged a number of new markets and collateral pools into its platform, including China Stock Connect, Malaysia, Indonesia, Italian national bonds held at Euroclear, and an enhanced pledge product in South Korea.

Another dimension that is becoming key is the ability to access and leverage assets. For example, BNY Mellon's platform is available more than 23 hours a day, and now, following an extensive legal and tax analysis, clients can allocate assets over 'record date' into pledge (non-title transfer) transactions — reducing the liquidity impact over these time periods.

Expand options for clients

In addition to the asset side of the equation, the liability side is also key. For example, where and how can assets be efficiently utilised? The priority for global banks is to provide clients with an ever-expanding suite of options to lend cash and securities. This can create additional revenue streams, while reducing counterparty credit risk and increasing operational efficiency.

With this in mind, BNY Mellon has witnessed growth in Fixed Income Clearing Corporation (FICC) Sponsored General Collateral (GC) (FICC Sponsored GC), BNY Mellon is providing the global market infrastructure for United Nations' Liquidity and Sustainability Facility. Later this year, clients will be able to use the bank's triparty platform to perform intraday repo, to settle the principal leg of securities lending transactions — enabling the loan leg and the collateral leg to allow for delivery-versus-delivery settlement — and to settle pledge transactions against cash whereby both the start and end legs settle cash-versus-securities simultaneously on our platform. BNY Mellon is also having discussions with its clients and central clearing counterparties (CCPs) globally about providing solutions for their collateral obligations.

"The need for efficient allocation of collateral is accelerating, with transparency and optimisation spanning the entire asset and liability equation — across asset classes, business lines and venues — fast becoming a must have"

Optimise, interoperate and innovate

The need for efficient allocation of collateral is accelerating, with transparency and optimisation spanning the entire asset and liability equation — across asset classes, business lines and venues — fast becoming a must have. To meet these needs, banks are increasingly offering collateral optimisation solutions to clients.

BNY Mellon's optimiser, for example, provides eligibility screening and directed allocation solutions, uses client-defined inventory data, customised cost models and security reference data, as well as utilising advanced machine-learning techniques and new technologies to provide a more efficient and configurable way of allocating collateral to solve key business problems. For example, it uses mathematical algorithms to provide options for reducing funding costs associated with liquidity coverage ratio (LCR), net stable funding ratio (NSFR) and comprehensive capital analysis and review (CCAR).

Make it quick, easy and simple

With a number of new and evolving topics demanding attention, the focus has turned to enabling clients to do business quickly, easily and effectively. That is why BNY Mellon has continued to invest in its platforms to provide clients with easy access to its capabilities.

These efforts include a redesigned and modernised user interface known as AccessEdge that has recently been enhanced to incorporate client-informed and workflow-oriented updates, as well as in-application and on-demand training videos. Additionally, the design, function and colour palette has been enhanced to make this an inclusive interface aligned with the Americans with Disabilities Act.

BNY Mellon also continues to enhance RULE, its flexible and intelligent self-service application for the creation and management of collateral schedules for activity on its international platform. For example, in Q3 2023, collateral receivers will have the ability to send exclusions quickly across multiple collateral schedules at the same time, as opposed to an individual basis — an enhancement that is expected to be extremely beneficial, particularly in times of market stress.

Operate through uncertainty

During times of crisis, clients, unsurprisingly, turn their attention to reducing the frictions that they experience in their day-to-day collateral use. It is, therefore, critical that banking partners are not only able to weather the challenging market conditions, but they are able to continue to invest in technology, resilience and cybersecurity to meet the existing and emerging challenges faced by clients.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Publisher: Justin Lawson
justinlawson@securitiesfinancetimes.com
+44 (0) 208 075 0929

Group editor: Bob Currie
bobcurrie@securitiesfinancetimes.com
+44 (0) 208 075 0928

Senior reporter: Carmella Haswell
carmellahaswell@securitiesfinancetimes.com
+44 (0) 208 075 0927

Studio director: Steven Lafferty
design@securitiesfinancetimes.com

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08:30 - 09:15
Breakfast & Registration

09:15 - 09:30
Welcome Remarks

Speaker
Mark Richardson, Head of Trading, Zodia Markets

09:30 - 10:00
Opening Keynote Address

Speaker
Luís Laginha, de Sousa Chair of the Management Board Securities Market Commission (CMVM)

10:00 - 11:00
Digitalisation: Assets, Infrastructure, Regulatory & Legal Frameworks

Efficiencies and structural change that are increasingly being demanded by politicians and regulators in the context of financial services, can only be achieved through the broad adoption of digital technologies. At the same time, the fintech, distributed ledger technology (DLT) and digital asset markets continue to develop rapidly, with institutional interest remaining constant. Amongst other things, this session will review the fast-changing regulatory landscape (including prudential regulation) around digital markets, and the implications for securities lending and financing activity and infrastructure. As new and novel assets, including tokenised securities and cash begin to move into the mainstream, it will also consider legal certainty around issues such as ownership and transferability, so as to allow these markets to scale up and reach their true potential.

Moderator

Johann Palychata, Head of Partnerships and New Platforms for Securities Services BNP Paribas

Speaker

Elliott Drews, European Lead - Product Management, Agency Securities Finance, J.P Morgan

Sophia Le Vesconte, Counsel, Linklaters LLP

Martin Walker, Head of Product, SFCM, Broadridge Financial Solutions

Dina White, General Counsel, Zodia Markets

11:30 - 12:15
DEI: Addressing, Managing, Measuring

At recent events, we have heard from inspiring individuals and some very personal perspectives on Diversity, Equity & Inclusion (DEI) in the securities finance industry. During this session, we are going to focus on where next. How are firms addressing DEI considerations? How do they recruit diverse talent to join the industry? How do they get buy in and engagement within their organisations? We will hear about the benefits it has brought to the business and the practicalities of making positive change, explore the timeframes involved, and finally consider how the industry measures success.

Moderator

Cassie Jones, CFE Managing Director, Head of Securities Finance Client Management, State Street

Speaker

Jemma Finglas, EMEA Head of Asset Financing, Citi

Keren Halperin, Deputy CEO & Chief of Staff, Sharegain

Kyle Kolasingh, Director, Head of Market Services Solutions, RBC Investor & Treasury Services

Marcus Rudler, EMEA Head of Agency Securities Finance Trading, J.P. Morgan

12:15 - 12:35
ESG & the Regulatory & Policy Landscape

This presentation will look primarily at ESG regulatory and policy milestones.

Speaker

Laura Douglas, Senior Associate, Clifford Chance

12:35 - 13:20
Delivering on Sustainability: Where Next?

It has been suggested that ESG assets will reach $53 trillion by 2025, a third of global assets under management. Although the war in Ukraine may have subtly changed some of the sustainability rhetoric, the long term direction of travel remains clear, and the work that ISLA has been leading on in areas such as governance and collateral are vitally important in the context of our markets. This final panel of the conference will touch upon the work already done, against the backdrop of the global policy and regulatory initiatives outlined in the previous presentation, including areas of regulatory clarification needed and the expectations from market participants from across the value chain.

Moderator

Ciara Horigan, Vice President - Regulatory, Industry & Government Affairs, State Street

Speaker

Ross Bowman, Global Head of Agency Securities Lending Client Management, BNP Paribas

Nithya Iyer, Senior Specialist, Sustainable Financial System, UN PRI

Maximilian Kufer, Head of ESG Client Strategy EMEA & Private Markets, Invesco

Donia Rouigueb, Head of Sales, CACEIS

13:20 - 13:35
Closing Remarks by the ISLA Chair

This presentation will look primarily at ESG regulatory and policy milestones.

Speaker

Ina Budh-Raja, EMEA Head of Securities Finance Regulatory Strategy & Industry Affairs and Markets ESG, BNY Mellon

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