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**Ken DeGiglio
on tackling
reconciliation
issues through
a digital-first
approach**

Day one agenda inside



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1Source: reconciliations and transaction breaks a thing of the past?

EquiLend CIO Ken DeGiglio explores how the firm's upcoming 1Source system will support market participants in tackling reconciliation issues through a digital-first approach

Price breaks, orphan breaks and rate breaks are among the most common securities lending reconciliation issues which occur several times, on a daily basis, across any number of trades. With EquiLend 1Source, we aim to eliminate them all.

In 2021, we assembled a Digital Transformation Working Group, consisting of several agent lenders and broker-dealers. These group members identified the elimination of the antiquated reconciliation process as the top priority to be solved by a new, digital-first approach to transaction and lifecycle management. A third-party consultancy — commissioned by the working group to assess the cost of these top-three breaks and other reconciliation problems — determined that the cost to the industry totalled approximately US\$100 million per year. From this, EquiLend 1Source was born.

EquiLend 1Source is a distributed ledger-based system that ensures all transaction information and subsequent lifecycle event information remains in sync for both counterparties in a contract at all times. With a single source of truth for all contract data across the trade lifecycle, the need for reconciliations simply goes away. Lifecycle events produce a multitude of breaks that demand reconciliation — this includes price differences, rate adjustments, orphan breaks, in addition to mid-processed dividends, overfunded collateral, and settlement errors.

In addition, the effort to reconcile breaks is managed by operations and traders with considerable labour required to resolve complex breaks. Fines and fees incurred due to contract breaks, which may remain unreconciled for days and even weeks, contribute further time and monetary costs. Now, the underlying technology is available to eradicate these issues completely.

This is not another distributed-ledger technology (DLT) solution for name's sake alone. Our Working Group was tasked not with finding a use for DLT, but with identifying the largest pain points that could be solved through digital transformation. It is not the first wave of digital transformation in our industry, nor the first time EquiLend has worked together with the wider market to develop an improved model for securities lending.

An example is the industry-wide adoption of EquiLend NGT, a trading platform in our market through which more than US\$2.4 trillion in notional is transacted monthly. NGT revolutionised the securities finance sector with pre-matching, unique trade identifiers, post-trade connectivity and SSI pairing, with more recent developments including real-time data integration and hard-to-borrow functionality with the Competitive Bid screen.

EquiLend 1Source is a complete reimagination of the transaction flow which will be equally as transformative — it will do for the trade lifecycle what NGT has done for execution.

Rendering moot, the current inefficient, expensive reconciliation process, using EquiLend 1Source will ensure both sides of a transaction match at every point of the contract lifecycle. All contract records will be held on the ledger as a unique record and all transaction events will update immediately for both parties, eliminating those problematic price, orphan, rate and other breaks. Our use of smart contracts — rules on which conditions for actions



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can be defined — on DLT additionally smooths the pathway to an efficient, mutualised workflow. Trades will flow through the EquiLend 1Source system and smart contracts will serve to automate further lifecycle actions.

EquiLend 1Source is built on Digital Asset's Canton Network, a DLT "network of networks" upon which dozens of the largest corporations on the planet have connected their systems. This will result in unparalleled interoperability — a favourite feature across the EquiLend tech stack — and synergistic opportunities across the finance sector and beyond.

Participants have engaged in a pilot and are actively integrating to EquiLend 1Source prior to the full system roll out next year.

T+1 and 1Source

The benefits of monetary and time cost savings are obvious. However, EquiLend 1Source also supports even larger-scale industry changes such as the move to shorter settlement cycles. Scheduled for late May 2024 in the US and Canada, Mexico is also looking to move to the same reduced settlement schedule. The efficiency gained in

maintaining perfect contract records throughout the lifecycle with EquiLend 1Source means that T+1, and even T+0, become significantly less burdensome. With no breaks to threaten settlement, trades can be agreed and executed, and pricing, terms and other events will be updated immediately, on any timeline, no matter how short.

Risk management and sector-wide efficiencies

Removing reconciliation as a breakpoint is a primary benefit of EquiLend 1Source, but there are ancillary benefits too. Firstly, firms benefit from an assurance that contracts are always correct, allowing for accurate daily accruals and accurate accounting. Billing becomes a non-contentious issue because accruals are always right on this centralised ledger.

In ensuring the accuracy of contracts across the lifecycle, this DLT technology also enables efficient regulatory reporting as contract details are accurate, on one single ledger, supporting reporting under existing and future regulation such as SEC 10c-1.

Furthermore, through EquiLend's connectivity to the Canton Network, 1Source is positioned for the future, with the ability to connect to DLTs in other market segments. Interoperability, global connectivity and accuracy are guaranteed at every stage. The simplicity is revolutionary and the applications are long ranging from day one.

The working group members who conceived 1Source in their identification of reconciliation as their biggest challenge have also been the biggest advocates of the project, dedicating time and effort to develop a proof of concept, execute a successful pilot programme and embark on the final phase of development prior to the 2024 go-live. Test trades have already moved through EquiLend 1Source and flowed through the trade lifecycle without issue.

The benefits of EquiLend 1Source extend to all of those covered here. However, in practice, it delivers not only time efficiency, cost reduction and simplicity to the securities finance market, but also carries positive applications for the wider financial ecosystem. With this technology, we are not simply solving problems, we are reimagining the securities lending workflow to remove reconciliation issues at source. We look forward to continuing our mission of working with all securities finance market participants to bring about positive change and efficiency to our industry. ■