WATSON WHEATLEY

HEDGE FUND
ETD & OTC DERIVATIVES
RECONCILIATION

INTRODUCTION

An established Mayfair based hedge fund with over $20bn AUM that uses Linedata's Global Hedge Portfolio Management System required an automated reconciliation system. The volumes are relatively large for a buy-side firm and multiple instrument classes are traded daily. A full reconciliation at the most granular level was required to tie out any discrepancies with Prime Brokers.

REQUIREMENT

The client needed to reconcile large and increasing volumes of exchange traded derivative trades on a daily basis with its clearers to ensure trading data was accurate, charges were being levied in accordance with agreed commission schedules, and collateral requirements were being correctly applied.

Watson Wheatley's iRecs was identified as the best fit for the company due to its ability to automate derivative trade matching and fully account for all mark to market differences.

iRecs was required to interface with the firm's portfolio management system, Linedata's Global Hedge, and reconcile this against data from ten different clearers who provided data in a range of file shapes and formats.

Data import needed to be completely automated; clearer files were delivered via encrypted FTP on T+1. Volumes ranged between 3,000 and 10,000 trades per day across 60 funds/portfolios containing over 1,000 margin accounts.

A very high level of automated transaction matching was therefore required and clear reporting available regarding breaks. Additionally the system needed to generate output files containing interest payments and other adjustments for direct upload to Global Hedge, and spreadsheets containing corrections to be sent to the clearers.

Finally a reporting capability was required to measure clearer service quality as well as identify and quantify operational risks.

- → $20bn AUM Hedge Fund
- → ETD & OTC Derivations
- → Linedata Global Hedge PMS
- → Trades, Positions, Cash Balances, Total Equity Reconciliation
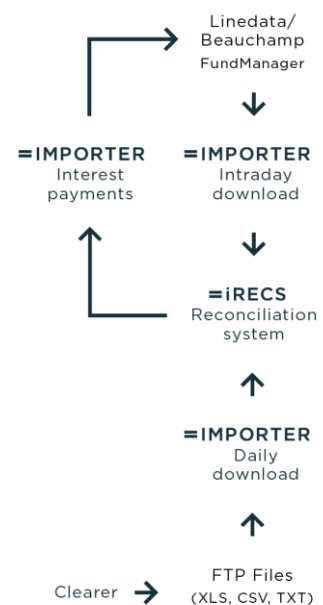
SOLUTION

System installation and configuration was completed in 4 weeks by Watson Wheatley, initially on the client's UAT platform. iRecs was able to interface with Global Hedge via a direct database read which was set to run daily in the early hours of the morning. All previous business date cash balances and positions were retrieved along with new trades, transactions, accounts, securities and identifiers.

Global Hedge was unable to calculate realised P&L from futures trading at the agent account level so cash balances passed to iRecs for matching were inaccurate. iRecs recalculated both the realised and unrealised P&L based on the received trade history, current positions and security prices to create the required margin balance to be used for reconciliation.

Watson Wheatley's Importer software was used to construct import maps to read the files containing the equivalent data from each clearer. The created maps were invoked automatically on receipt of the decrypted files and data was passed directly to the relevant iRecs tables.

All data received by iRecs was automatically validated for continuity of positions (based on underlying trades) and continuity of margin balances (based on underlying cash flows and calculated trade P&L).

iRecs was configured with standard match rules for total equity derivative reconciliation along with bespoke work flows to correctly identify, annotate and route key break items. Bespoke reporting was developed to assist the client quantify the service quality provided by its clearers and to measure the volume and value of breaks by type and to help identify weak operational processes. The reports were delivered through the standard reporting engine delivered with iRecs.

Optimal operating procedures were drawn up with the section head and provided the basis for training users in all aspects of operation of the system.

The system was introduced to production and run alongside the client's manual process for 4 weeks to prove the system, give the users hands-on experience and to tune the match rules and work flows to maximise the automation. Cutover to live was simply a matter of decommissioning the manual process and relying fully on iRecs. Watson Wheatley provided both on-site and remote support to the users throughout for any issues that they encountered.

BENEFITS

The data import process has been highly automated with the use of Importer requiring only occasional manual intervention. Minor and infrequent changes to Importer maps has been required over time to accommodate the availability of new security identifiers and alterations to file layouts imposed by the clearer.

iRecs achieves automated match rates in excess of 99% with over 10,000 trades per day delivering fully annotated breaks to the derivatives team members for remedial action.

Users have been particularly pleased with iRecs' ability to accurately identify securities referenced in the sometimes patchy data provided by the clearer. Importer's flexibility to lookup and compare multiple and partial identifiers proved extremely beneficial particularly for options. Where a referenced security could not be identified, iRecs' repair functionality for trades or positions could be applied by the user, the integrity restored and the audit trail updated with the manual event.

Bespoke reports have been constructed that provide key performance indicators for clearer service quality. These have been used by the client as part of its regular reviews with the clearers. Enhancements made to the process have been able to be quantified, and have had a marked effect of the workload of the derivatives reconciliation team.

A high level of inaccuracy in the charges applied to futures trades across all clearers has been identified. A process has now been established with iRecs to itemise these differences with each clearer on a daily basis by providing accurate difference reports. In one month the charge discrepancy amounted to over $500,000.

iRecs has provided the company with a complete reconciliation of all aspects of its derivative trading. The overriding value of this has been in correcting the inaccurate data of its clearer's with the minimum of resources and in a timely manner.

BEST PRACTICE RECONCILIATION.

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