

CASS 7

Best Practice



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CASS Overview

In recent years, CASS Audits have shifted towards a more control-based approach from the substantive, sample testing methods. This is perceived by most as proactive, as it challenges the suitability of a firm's key controls underpinning the operational processes. Where a control has failed in the past and given rise to a CASS breach, or through rigorous testing found to be weak and inefficient, remediation action must then be taken to enhance the existing control framework. This is particularly true when an FCA regulated firm holds money on behalf of clients as client money and must therefore comply with the client money rules in chapter 7 of the FCA handbook.

Perhaps the purest form of a control is a reconciliation - an "after the event" control which flushes out instances of reconciliation breaks whereby either the firm has made a mistake or there has been a third-party error. Regardless of the party at fault, the firm is responsible for the resolution of the break to ultimately ensure their internal records and accounts for client money are in-line with client money physically held in client money bank accounts.

Firms often overlook the obvious question relating to client money reconciliation processes, whether it is the internal client money reconciliation comparing individual client specific records to client bank account specific records, or the external client money reconciliation comparing client bank account specific records to third party client bank account specific records:

“What do the results of our reconciliations tell us?”

Due to the manual nature of many reconciliations, firms often do not have the time or resource to investigate the root cause of recurring breaks to rectify the issue at source. Furthermore, as a business grows, legacy issues are carried forward and eventually form part of a business as usual process within regulatory reconciliations.

Every reconciliation exception is potentially an issue in the event of firm failure. As a result, the FCA expects firms to demonstrate that their key controls are operating effectively and affording underlying clients an acceptable level of protection. The reconciliation aspect of the CASS rules must therefore be at the forefront of a firm's priorities.





AutoRek Overview

AutoRek is a financial controls, regulatory reporting and data management platform.

It is a powerful data management tool which encompasses integrity and validation of data, automated reconciliations, workflow and case management, and timely, meaningful management information.

AutoRek streamlines the amalgamation and consolidation of data from disparate systems, together with providing the necessary transparency, good governance and robust audit trails to meet challenging reporting requirements.

Over the years, the AutoRek CASS reconciliation and reporting requirements have been significantly enhanced to meet the industry demand.

AutoRek's best practice solution for client money has already been implemented within many large Asset Managers. This solution has developed in conjunction with the following four fundamental client money concepts:

- **Identification**
- **Segregation**
- **Protection**
- **Payment**

This paper assumes a firm uses the normal approach to client money segregation; offers contractual settlement to clients; uses the individual client balance method to derive the client money requirement; may hold client money on a multi-currency pooled basis and maintains internal cashbooks of client monies held at various credit institutions.



CASS 7 – Client Money Rules

At an elementary level, the client money rules state a firm must maintain complete and accurate books and records. In doing so, the firm should then be capable of distinguishing, as at any point in time, the client money held for one client from the client money held for any other client, or from its own money. This is particularly important when client money is held on a pooled basis, rather than in client money designated accounts as an overdrawn client balance on the firm's books and records can indicate a cleared funds issue.

The daily internal client money reconciliation comparing the client-specific records to the client money cashbooks acts as a secondary control, to ensure the amount of client money the firm should be holding for all clients is aligned with the amount of client money actually held on the internal books and records.

The external client money reconciliation then recycles the same cashbook data, acting as the internal comparable source to the client money records and accounts of those held at the various banking institutions.

Some of the common issues and challenges arising with internal and external client money reconciliations in a manual environment are:

- **Risk issues – increased number of dependencies when sourcing data from various and disparate systems;**
- **Completeness of data – no validation of data being sourced for underlying reconciliations;**
- **Break ageing – the correct business age is not applied to reconciliation exceptions;**
- **Break treatment – incorrect CASS treatment of open exceptions;**
- **Foreign exchange application – incorrect FX rates applied to daily reconciliations;**
- **Manual error – incorrect journal postings for client money top ups;**
- **Little or no audit trail – no obvious workflow or governance arrangements;**
- **Record retention – difficulty adhering to the CASS record retention requirements, and;**
- **Inaccurate or no management information – often out-dated once finalised.**

The AutoRek solution is designed to deliver an automated client money reconciliation environment whilst also addressing many of these pitfalls encountered in the industry.

Internal Rec



External Rec



010011
101001
000100

Data Entry

AutoRek can ingest data in various formats, ranging from Flat Text files to SWIFT messages and Json messages. The capability to load various data forms has grown significantly over the years, to meet the demands of new and existing clients. As AutoRek grows, so does the list of data feeds which are used. Below is the list of data feeds which AutoRek is compatible with.

- **SQL Server**
- **Flat Text File**
- **Excel File**
- **Xml File**
- **XPath**
- **Structured Text File**
- **SWIFT Text**
- **Regex**
- **Reconciliation**
- **Json**
- **OleDb**
- **Odbc**

Typically for client money on the external reconciliation, AutoRek consumes files from the general ledger or accounting platform which represent the close of business balances and/or transactions for all client money cashbooks. On the banking side, there would be an expectation to receive prior day close of business balances and transactions from each of the banking institutions holding client money.

AutoRek works with existing data and therefore there is no requirement to amend your existing data feed formats. At the data entry phase, AutoRek allows the end user to create a mapping, which removes the uniqueness of the files being received from different banking institutions and internal source systems, whilst still retaining the original source of the data. As firms scale up, undertake mergers and acquisitions or perhaps place client money with a credit institution for the first time, this feature allows new feeds to be easily introduced into the existing mapping.

The AutoRek scheduling functionality is the mechanism by which data is lifted directly from the client internal directory and fed into AutoRek. A schedule works by setting a frequency and a specific time to commence the schedule. In the case of client money, clients generally set the schedule frequency to daily and use the file watcher trigger to initiate the schedule. As and when the raw data files become available for consumption these are passed through to AutoRek. In the cases of non-receipts of files, alerts can be configured to notify accountable users and the event log of the data feed will provide the full audit trail of the file consumption success.

Scheduling is controllable by the client, making intra-day reconciliations also attainable based on the desired frequency. Consumption of intra-day banking feeds can provide visibility of potential shortfalls in the client money pool or client money diversification risk.

Validation

The completeness of data is always a question asked during a CASS Audit:

“How do you know you have a complete set of data?”

The AutoRek solution has been tailored to meet this specific requirement and enables users to prove the integrity of all data feeding the downstream, regulatory reconciliations.

Validation reconciliations take the opening and closing balance per client, cashbook and client money bank accounts per credit institution and compare these to every transaction from the same period to ensure any shift in the balance can be attributed to the net movement of the transactions. Upon, successful matching in the validation reconciliations, items are then routed to the final reconciliations.

Enrichment

Any enrichment of data in AutoRek is entirely rules driven. Any new rule created will require different levels of review and sign off before being commissioned in a live environment. Where a rule has been created and utilised in a live environment, it can never be deleted and can only be decommissioned. This provides complete auditability on the purpose, impact and owner of the rule.

In a multi-currency trading environment, there will always be the requirement to deliver a close of business foreign exchange rate files into AutoRek. In order to establish the legal entity reportable currency equivalent of any balance or transaction, AutoRek utilises an explosion rule which returns the FX rate for the source balance or transaction from the FX rate file. Upon retrieval of the FX rate, a calculation rule establishes the base currency equivalent of any balance or transaction held in AutoRek.

The use of Payment Service Providers (PSPs) has become increasingly common in the client money space. Client money is often first visible in the immediate segregation client money bank account in the form of a bulk credit from a PSP such as PayPal, and with it, a client level breakdown is provided by the PSP for the constituent parts of the bulk credit. The explosion rule functionality in AutoRek is heavily utilised in scenarios such as this, as it allows the disaggregation of the bulk credit into the most granular level to expedite the allocation to client portfolios.

On the internal client money reconciliation, the individual client balance method (to establish the basis of the client money requirement) is achieved by enriching the raw client balance file to treat any overdrawn client balances as zero. The actual client position is not lost - the visibility of the true overdrawn internal client balance is retained in AutoRek, but the calculation allows the enrichment of the balance in accordance with CASS 7.16.16 (R).

Rules relating to explosions and calculations would typically form part of the same schedule executed to deliver the data feeds into AutoRek in the first instance. The sequential order of events is visible on every schedule and lays out the natural order of events expected to occur throughout the automated process. This provides auditors with a centralised view of the different processes undertaken in AutoRek to reconcile client money.

Matching & Labelling

Upon successful delivery of the raw data files (required in the reconciliation) and their necessary enrichment, the data within the comparable sources of the reconciliation are visible to the end user. The match rule configuration screen provides the opportunity to create match rules which then have a direct and automatic impact on the desired reconciliations.

In relation to the external client money reconciliation where matching is undertaken between cashbook and client money bank transactions, this functionality is extremely powerful. When the match rules are included as part of the daily schedule, most of the cashbook to bank matching is undertaken automatically by AutoRek prior to any user involvement. Any records automatically matched by a business rule are enriched with a record of the business rule used to enforce the match.

Matching rules can be designed to match records at different levels:

- **1 to 1**
- **1 to Many**
- **Many to 1**
- **Many to Many**

Matching is generally undertaken across two comparable sources, such as the cashbook and the bank. However, contra match rules allow matching across the same source which can prove very useful for cases where there have been reversals or cancellations.

Depending on the role permissions of the user, automatically matched items can be rolled back to an unmatched state for further investigation. There may be a requirement to do this if a live match rule is operating incorrectly.

Any residual exceptions not matched within the reconciliation will be automatically labelled with “to be investigated”, therefore prompting the user to establish the root cause of the break. As an aid for any further manual matching, the suggest match function exists to present the end user with potential matches based on characteristics of transactions.

Labelling rules in AutoRek allow for the automatic allocation of labels to items which remain unmatched on the reconciliations. The labels are entirely configurable and can be setup to mirror the operational structure of the business and/or the underlying break reason. Depending on the client and auditor view of external reconciliation items, clients will typically utilise the label field to categorise exceptions as CASS specific labels such as those captured within CASS 7:16.25 (R):

- **Unallocated client money;**
- **Unidentified client money;**
- **Uncleared payments (inbound);**
- **Uncleared payments (outbound – discharge of fiduciary duty), or;**
- **Client money ring-fenced in relation to custody asset shortfalls.**

Where this auditor view is adopted, explosion rule functionality is again used to enrich each CASS labelled exception with the appropriate treatment to the client money resource and requirement and posted back to the internal client money reconciliation.

The secondary label field in AutoRek is known as the sub label field. This is often used to allocate an exception to a user or department of users to manage the resolution of the break, providing immediate sight of ownership.

Notes can be manually added to any matched or unmatched item in any reconciliation. The details of the note, user who applied the note and date on which the note was added will be held against the transaction throughout.

Each exception within a reconciliation is aged in business days using the working days calendar extended function in AutoRek. Where an exception is carried from one reconciliation into the subsequent scheduled reconciliation, the age of the exception is recalculated using the current date offset against the value date of the transactions.

Calendar date ageing is also a feature within AutoRek. This allows Client Money and Asset Return reportable items to be apportioned into the correct ageing buckets at month end.



i Reporting and Management Information

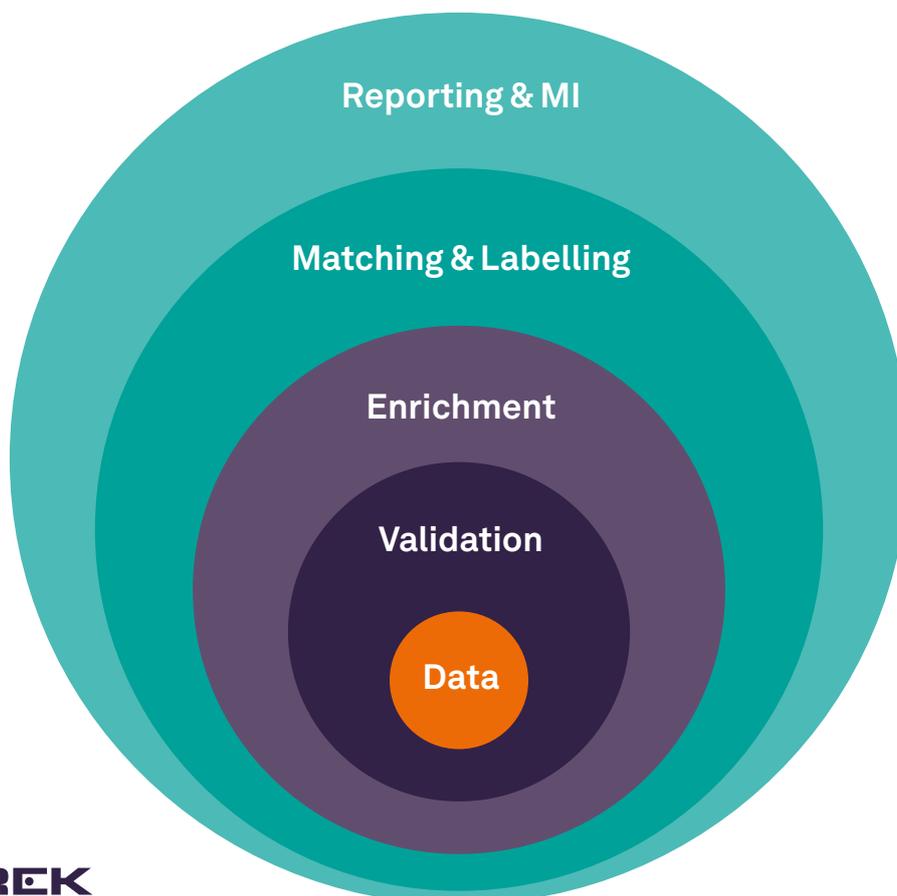
The end point of the solution is the production of the daily calculation. This is driven off the internal client money reconciliation ultimately comparing the client money requirement and client money resource, the bulk of which will be derived from client balances and cashbook balances, respectively. This gives an aggregated view of each of the inputs required to demonstrate alignment between the requirement and resource. Should a discrepancy arise between the two, AutoRek will generate the top up value and post it back into the internal client money reconciliation, effectively clearing down the reconciliation to zero.

There would still be an expectation the end user would post the client money top up journal to the general ledger and facilitate the movement of funds to or from the client money bank account by close of business. However, to prevent mis-posting of the journal to the general ledger, the existing AutoRek export functionality delivers the top up journal in a format required for direct upload to the general ledger.

In AutoRek, management information is best displayed through the front-end dashboards. In addition to provide a real time view into the current status of the underlying reconciliations, they can also provide:

- **Client money diversification current view and trending;**
- **Volume and value of exceptions per department;**
- **Volume and value of exceptions per break reason code;**
- **Ageing of exceptions;**
- **Match rule performance metrics;**
- **Client count, and;**
- **Client money requirement, resource and top up trending.**

This is not an exhaustive list and metrics can be presented in various tables and chart formats. Dashboards can also be made visible to an individual user or group of users depending on their role(s) within the AutoRek solution, therefore tailoring the content according to the role they undertake within the business.





Sign Off and Record Retention

At each stage in the client money reconciliation solution, workflow functionality can be introduced to ensure the appropriate levels of sign off and governance are applied.

Within AutoRek, we typically see clients using RAG indicator functionality to apply a severity to open exceptions and it is best practice to track the status of a reconciliation according to the volume, value or business age of exceptions.

All client money data stored within AutoRek, is held in line with CASS record retention requirements. A daily snapshot of the final client money calculation is stored in-system, allowing auditors to return to a specific date to review the client money calculation for that day. Each daily calculation and the underlying data is easily accessible allowing the end user to identify the client money due to a specific client at any point in time.



Conclusion

The AutoRek platform for client money reconciliations provides firms the ability to consolidate, enrich and validate all data for completeness and integrity. Furthermore, AutoRek can automatically match, record and label data to provide live metrics on all client money activity.

Arrange an AutoRek Demonstration

To arrange a demonstration or a confidential discussion to explore our methodology and credentials, please contact us:

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