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Regulation & Standards

Special Report

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Editor's Letter

Setting the Regulatory Agenda

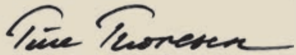
Last year, some market participants commented that financial regulators were the main recruiters of ex-bankers. This might not have been entirely true, but many regulators have indeed added more resources in recent years. There has been growing pressure to review regulatory requirements, impose greater oversight and push for increased transparency—often by enforcing reference data standardization.

In fact, standardization is the one issue all players in the market are trying to solve—and have been trying to solve for the past few decades. But although everyone seems to be talking about the same topic, there is still a long way to go. The market turmoil has now resulted in firms questioning if there is a need for immediate regulatory involvement to improve standardization and reduce the risk associated with poor data, or if regulatory involvement is not the right answer.

Yet, in some aspects, regulators have already tried to enforce data standards. Europe's MiFID includes references to standards, and UK regulator FSA recently fined Barclays Capital for transaction report errors, some of which related to failure to use correct identification for instruments and entities.

Still, while some claim regulators do need to impose the use of specific standards to ensure increased adoption, others suggest standardization should be left to the market. In this *Regulation & Standards Special Report*, which includes comments from industry experts and a news review, we hope to provide readers with an insight into the latest developments in the regulation and standards space.

Yours sincerely,



Tine Thoresen
Editor, *Inside Reference Data*
Email: tine.thoresen@incisivemedia.com
Tel: +44 (0)20 7004 7470

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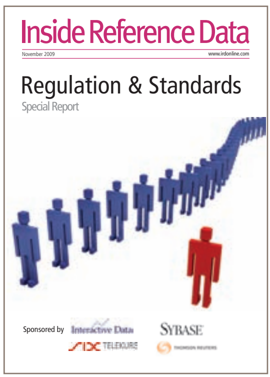

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Incisive Media
Haymarket House, 28-29 Haymarket
London SW1Y 4RX

News Review

SEC Asks For Business Case on XBRL for Corp Actions

WASHINGTON, DC—The Depository Trust & Clearing Corporation (DTCC), Swift, the XBRL consortium and representation from the ISO and industry bodies such as ISITC and SMPG have collectively been asked by US regulator the Securities and Exchange Commission (SEC) to produce a formal business case regarding the benefits of extensible business reporting language (XBRL) usage for corporate actions, spanning issuers, banks, broker dealers, custodians and the investment community, *Inside Reference Data* has learned.

David Blaszkowsky, director, office of interactive disclosure at the SEC in Washington, DC, says: "XBRL is only now becoming a generally known standard, especially due to its recent adoption by the SEC for public company reporting ... It is reasonable for the market to consider it for more purposes."

The industry group aims to present the business case report to the SEC before year end. New York-based Brett Lancaster, vice-president, asset services at DTCC, says this will quantify the cost savings and risk reduction for the industry.

It is hoped that by Q1 2011 every DTCC participant will be able to use ISO 20022 messaging with XBRL as a feed.

The full version of this story appeared in *Inside Reference Data*, September 2009.

Carla Mangado

WG6 CFI Standard Revision to Result in Expanded Coverage and Increased Granularity

LONDON—Proposed changes to the classification of financial instruments (CFI) standard are set to result in improved coverage and increased granularity, but some are concerned the standard is not fit for purpose, *Inside Reference Data* has learned.

ISO Working Group 6, which covers the ISO 10962 CFI standard that helps group securities, has completed a review of the standard, and the final draft international standard will be circulated for voting at the start of October. "The changes cover developments in the securities markets during the past few years," says Zurich-based Nourredine Yous, convener of the group.

The main changes will be the introduction of a new structured product category, restructuring of the referential instruments category, and inclusion of new instruments such as contracts for difference and credit default swaps.

The full version of this story appeared in *Inside Reference Data*, October 2009.

Tine Thoresen

BNP Paribas Securities Services Brings 15022 Messages to Asian Clients

HONG KONG—BNP Paribas Securities Services is set to increase automation in corporate actions messaging for clients in Asia when it launches a new business in the region and brings Swift 15022 messages to the local market, *Inside Reference Data* has learned.

BNP Paribas launched its securities servicing business in Asia in 2007, and is now starting new operations in Hong Kong. The launch involves it bringing its global platform to Asia, and connections with clients will rely heavily on Swift messages. "All the benefits of ISO standards will come through to BNP Paribas Securities Services clients in Asia," says Hong Kong-based Barnaby Nelson, head of business development at BNP Paribas Securities Services in Asia.

In the region, most corporate actions messages are still typically communicated via fax and email. "When we tell local clients what we can do, they are pretty surprised," says Nelson, adding this should be a positive change for the market.

The potential for increased automation and reduced risk of corporate actions processing is now becoming part of the proposition for the custody business. "If I look at the client conversations we've had in the past three months, it is definitely something that raises eyebrows," he says.

The platform is the same as the one the firm uses in Europe. "It is essentially the European discipline we're bringing to Asia," says Nelson.

The full version of this story appeared in *Inside Reference Data*, September 2009.

Tine Thoresen

Swift Releases Tool to Facilitate Standards Implementation

Swift has released its Standards Developer Kit (SDK), aimed at enabling customers to easily implement Swift and ISO standards in an automated way, *Inside Reference Data* has learned.

The tool consists of the MX Repository, the MT/XML Schema Library and MT-MX Translation Reference, an executable reference implementation of Swift's published translation rules.

Event Templates to Aid Corp Actions Data Tagging

The group dealing with the corporate actions issuer investor communications initiative is working on a data tagging tool that will include corporate actions event templates for corporate actions announcements supported by the US market.

The Depository Trust & Clearing Corporation, the ISO and Swift will work together to engage US market participants in this data modelling exercise to review US market events and the event templates. The tool is aimed at helping issuers easily identify the relevant data elements needed for tagging corporate action events.

Virtual Roundtable

Regulation & Standards: The Regulatory Way

Inside Reference Data gathers leading industry professionals to discuss the changing regulatory environment and growing focus on standardization

The current crisis has highlighted the fact that the front office and the back office have not been on the same page when it comes to managing complex instruments and adding volume. What is needed from the regulators to ensure the situation improves?

Amy Harkins, senior vice-president, global corporate events, BNY Mellon Asset Servicing: Regulators are being called on to demand more clarity on financial innovation within the financial markets. The front and back offices within financial institutions will be required to work in tandem with regard to pricing and tracking complex instruments. Many financial institutions were aware of this potential problem pre-crisis and were working on tactical solutions. However, the collapse brought many of the underlying issues to a head. The challenge is to close the gaps through a combination of improved communication and technologies. If the regulators play any role at all, it is in encouraging financial institutions to move forward with the correct internal changes in a timely and cost-effective manner. After all, implementation of new risk control measures is a prerequisite if financial institutions want to retain clients and remain viable in a competitive market environment.

Robert Schork, data administrator, Bayview Financial: I think better definitions of the data that is currently being used will help, but the underlying problem is that there are no data governance processes that enforce communication between the business and IT. The perception is that IT is too slow to react, so the business develops their own silos of information to support their application.

Paul Kennedy, European business manager, reference data, Interactive Data: Innovation in the front office may have proved problematic for the back office, with new, highly complex derivatives and structured products taxing their resources. I believe that firms will have a better understanding that complex instruments need to be framed by good data management, and that front and back offices will work together more efficiently. In terms of regulations, it's important to note that although the authorities have focused on risk, demanding that firms be able to demonstrate that they both control and understand their risk exposure, the regulators will not seek to interfere in companies' business strategies. Their concern is outcomes, as opposed to strategies.

Elliot Noma, senior risk adviser at Asset Alliance and managing director, Garrett Asset Management: Data quality has clearly been an issue in the current crisis. Two aspects are very important. First, the relationship of firms with firms providing external evaluations of instruments and, second, the misuse of data sources within the firm.

In the first case, firms relied on outside sources of information to make investment decisions and evaluate the performance of their positions. One egregious example was the use of rating agencies' expertise, which resulted in flawed evaluations of securities. This led to mistakes in investment decisions from the systematic mispricings of securities. The practice of shopping for better ratings and the agencies' eagerness to satisfy these requests further accentuated this flawed relationship between data providers and users.

The second case is the inability of firms to adequately question the assumptions that they used internally in the evaluation of instruments. These shortcomings were sometimes similar to those of the rating agencies (such as incorrect assumptions on the inevitable appreciation of home prices), but also involves assumptions such as the ability to realize profits on illiquid positions held in portfolios based on faulty assumptions about funding sources (for example, structured investment vehicles) and average daily trading volumes, etc.

The regulators have a role to play in developing a better model for independent evaluations than reliance on the traditional rating agencies. Requiring firms to develop in-house expertise or rely upon other independent evaluators might provide the needed alternative views (with fewer conflicts of interest). Second, regulators should try to be forward looking in their requirements that firms not only consider the traditional risks, such as market, credit and operational risk. Other forms of risk need to be assessed with liquidity risk as a key topic.

Richard Newbury, market development manager, SIX Telekurs: Regulators need to make sure that they employ the right level of oversight—from a process, people and capacity viewpoint—to enforce suitable data standards. Areas where the industry disagrees, for example,

Paul Kennedy, European business manager, reference data, Interactive Data
Tel: + 44 20 7825 8334
www.interactivedata.com

Richard Newbury, market development manager, SIX Telekurs
Tel: +44 20 7550 5179
www.six-telekurs.com

on the intricacies of securities identification, were laid bare during preparations for MiFID. European regulator CESR at one point expected every strike of every option to have an ISIN issued for it. The front office neither knew nor cared what an ISIN was and no-one could really prove a benefit from the investment that would have been needed to issue, process and store so many ISINs.

New regulations and a realization that risk management needs to be all encompassing mean that being able to link market data back to reference data is beginning to receive the attention that it requires. Our market data feed and Valordata Feed [the reference data feed] are compatible with each other and map together seamlessly. We also carry comprehensive cross-reference data to allow those using a different service to connect to either our market or reference data easily.

Regulators are becoming more stringent, as evidenced by a large fine at Barclays recently. The failure to implement the necessary reference data fields meant that transactions from the front office went under-reported. The fine that Barclays received was significant in both amount and in the message that it gave to the industry that regulators expect the rules to be followed.

The other task that a regulator could undertake would be to look at the suitability of systems to support new instrument types that the front office wishes to invest in. Has the front office been able to provide the necessary training to back-office staff? Does the back-office staff understand the impact on operations flows? Have any necessary changes been made to all the systems in a process chain? Does the risk department know that these things are even issues for their firm?

Stuart Grant, EMEA business development manager, financial services, Sybase: The lack of consistency between front and back office is largely down to a combination of a mixture of disparate internal and external data sources, misinterpretation of data descriptions or metadata, and lack of scalability incompatibility of the more quantitative processes used in the front office for functions such as asset valuation. In addition, timing is having a big effect as front- and back-office systems, even middle office, are rarely in sync within a 24-hour period. This leads to inaccuracies and an inability to maintain an agile workflow. For these problems to be resolved, regulators must begin to look more towards standards in data creation, management, interpretation and supply. In particular, firms must either take more responsibility to own the data creation or interpretation process or it needs to be forced upon them. Take ratings as an example. Currently, too many firms extrapolate ratings across to non-rated entities rather than creating their own and linking the data into a entity and company hierarchy. This leads to an inability to truly understand relationships and exposure.

Milton Miyashiro, head of regulatory compliance for evaluations, Thomson Reuters Pricing and Reference Data: Regulators must be vigilant in monitoring the development of innovative products and new markets in the front office. This is important since most new products and new markets are often initiated with little infrastructure support until scale is achieved to justify broader middle-office and back-office resources.

Equally important is regulatory monitoring of infrastructure back-office processing. Market participants and regulators should continue improving the timing and completeness of information between front-office transaction execution and back-office transaction management by imposing stricter internal controls requirements designed to mitigate risk in the information flow.

Emphasis on controls such as:

- properly trained personnel responsible for terms and condition input mapping.
- review and sign off of critical terms and conditions.
- testing policies regarding trade confirmation between front and back office and counterparties.
- testing performance and surveillance procedures.

Controls over the information flow process are designed to eliminate errors in the back office attributable to complex instruments and significant volume. Ensuring data accuracy and completeness is critical for operational functions including accounting, risk management, and portfolio management and reporting.

Faulty reference data is not only a major cost to firms, but increased pressure from regulators is putting further onus on banks to improve data quality. Is this possible without the regulators imposing standardization in the reference data market?

Harkins: It is possible as several large institutions are working together to find more efficient and standardized ways to manage accurate reference data. There has been a consistent industry-wide effort to improve and follow best practices. Regulatory pressure obviously plays a role in encouraging harmonization and accuracy. However, the onus still remains within individual firms. To remain competitive, firms need to provide complete reference data for their clients based upon what is available in the market-place. Thus, the main incentive for improving reference data is the pressure from revenue-based clients and the regulatory bodies.

Schork: Forced regulations for reference data, on the whole, will not work. Even in one company, there are several versions of the same reference data. How can you hope to integrate them with government regulated reference data? The reason reference data is faulty is because someone assumed

Stuart Grant, EMEA business development manager, financial services, Sybase
Tel: +44 20 7648 5361
www.sybase.com

it meant something it didn't. Fix that first, then we can talk about integration.

Kennedy: From our experience, faulty reference data is not the primary concern. Rather, the issue tends to be incomplete or untimely data and confusion about identifiers, which can vary but still describe the same data. There has been a degree of standardization in the industry, but as ISO 15022 has demonstrated, even the broadest standard cannot cover the vast array of complex data generated by the financial industry. Standardization should not be viewed as a one-stop solution—a multi-source approach would be more realistic, with firms pulling their data from a variety of sources and cross-checking any anomalies.

Noma: The issue is the correct use of the data. Part of that is knowing the limitations on the data, so one can determine the assumptions behind its use and manage the portfolio appropriately. Regulation can only go so far on this since the reference data has its nuances for each market, with standards always lagging behind the changes in the market. Regulators should not over-specify the standardization of the reference data market, but should focus on supporting best practices in use of the data and encourage corporate responsibility in use of the information (for example, compensation rules).

Newbury: This is difficult to answer. Standards are great. SIX Telekurs delivers data in industry standard formats and holds data in ISO standard formats. However, complying with standards can also risk hampering growth. What happens when a piece of data is needed that doesn't fit the standard? We have seen that the ISO 15022 format for corporate actions has been evolving for years. A firm's ability to do business would be impacted if it depended on changes to reference data when a single change may take a number of months to be made.

There are two projects on the table at the moment—one by the European Central Bank and one by the National Institute of Finance in the US—which seek to build centralized data repositories. This risks adding an additional layer of cost and confusion to the market and, again, would risk hampering business.

What may work better would be identifying a "skinny set" of data—the basics that are needed on an asset class by asset class basis—and formulating a regulation that forces issuers to always make this skinny set of data available in a standard format. A second part of such a regulation should be to force all issuers to make their issue notices and terms sheets available to anybody who requests them. Currently, for example, some bond issuers will not make their terms sheets available to all data vendors. In trading, this kind of transparency (for quotes and transactions) is enforced through MiFID in the EU and through the data access rule under RegNMS in the US. Neither the skinny set of data, nor the equal access to data rules should require a centralized data repository at a central bank—that is just another interface for a bank to implement as well as creating a potential single point of failure in the processing chain hampered by delays in adding attributes to the standard data set.

The third part of this imaginary regulation would be the mandatory use of this skinny data set—throughout all the banks systems. Regulators then would need to be given the responsibility to verify and certify the use of the data throughout systems in a bank—the verification being the responsibility of the regulator rather than the acceptance of a certificate from the bank.

Grant: Without standardization, firms will essentially split into one of two camps. Those who do not tackle the issue as they don't see the true benefit or see it as too big a problem to resolve and those who see the value in taking stock of their data issues and resolving them in order for them to meet their overall business objectives, provide transparency and have a clear view of their estate. Now, more than ever, reference data is the key foundation to data management within financial markets. An inability to succeed at this level could be more costly than just the operational overhead.

Miyashiro: Standardization in the reference data market is a daunting task but optimally where all market participants would like to be. Basel II advanced approaches for bank risk-based capital and operational risk measurements are reliant upon data accuracy and completeness. Disparate data systems and platforms from technology migrations and merger/acquisitions at banks often pose significant challenges from a standardization perspective.

A major hurdle lies with regulator coordination of the various financial market participants such as banks, insurance companies, mutual funds, public corporations, pension funds, etc.

For standardization to gain traction, regulators from every market constituency need to form a consensus regarding operational best practices. This consensus is necessary to establish common data requirements for all market participants. While it might be possible for industry to forge standardization, it will probably take regulatory influence to ensure compliance and enforcement.

One additional obstacle to standardization is the large number of private transactions (for example, SEC Rule 144A) limiting information access to non investors. Regulators may be forced to re-evaluate private transaction information reporting as more investors turn to data repositories for terms and conditions, corporate actions, legal entity/counterparty and pricing.

Since many governments own stakes in financial institutions, they could be seen as regulating their own interests. In what ways will this new situation affect the regulatory environment?

Milton Miyashiro, head of regulatory compliance for evaluations, Thomson Reuters Pricing and Reference Data
Tel: +1 646 822 3472
www.thomsonreuters.com

Harkins: As stated in the previous question, since in this situation the governments maintain stakes in the financial institutions it is in their best interest to have the best data that is available in the market-place. So with this in mind, it would appear that the needs of the regulatory bodies would benefit other clients within in the same local environment.

Schork: I actually see a relaxation of regulation in order to promote higher profits and thus higher taxes. Of course, this will lead to bigger disasters down the road.

Kennedy: We've observed that although many governments have now taken stakes in financial institutions, they've implemented a "church and state" approach, keeping their new acquisitions at arm's length and managing them through independent stakeholder organizations. Currently, political and popular pressure is focusing on the regulation of compensation for certain financial institution employees. However, the impact on the regulators has been minimal so far and the key issue for them remains risk management and managing exposure.

Noma: Codifying and encouraging best practices would be one way in which governments can institutionalize better uses of reference data and improve the quality of the data. Governments can also use its stakes to move the markets toward a greater degree of transparency for better price discovery, especially in the fixed-income market.

Newbury: Governments around the world are handling their new interests at arm's length and most have been clear that the situation where they own large chunks of banks is not one they want to maintain forever. Given the crisis the world has just endured, it would seem to me to be dangerous for any government to attempt to accept a lighter touch in regulation than is necessary to prevent a recurrence of the situation.

Having said that governments are perfectly entitled to protect national interests. The Alternative Investment Fund Manager (AIFM) directive from the EU is one such case in point. The UK is resisting the proposed directive as London is home to about 450 hedge funds, or about 80% of the European total.

Estimates are that the hedge funds industry in the UK employs around 10,000 professionals directly, and 30,000 others indirectly, including service providers such as lawyers and accountants. Now, since hedge fund failures were not a feature of the financial crisis, it seems that the focus may be a little skewed. Transparency of hedge funds is clearly an issue for investors and asset managers as well as regulators, but the non-global nature of the proposed regulation provides a loophole for fund managers to move abroad and avoid regulation. A move away from the UK would endanger up to 40,000 jobs and the UK government clearly would wish to avoid that situation.

Charlie McCreevy, the European commissioner responsible for internal market and services, has announced that MiFID will be reviewed from the end of 2009. This extends transparency into fixed-income trading and into structured products. Although the UK is also Europe's biggest capital market, the structure of the regulation is likely to be such that the loopholes evident in the AIFM Directive will not exist for MiFID.

Grant: We're already seeing the political environment make an impact on the way regulation is conducted. Many governments see the central banks as key to regulating within their borders, after all it is the central banks that have the consistent track record of involvement and collaboration across borders in times of struggle. As the credit crunch and subsequent recession fades away, this focus is likely to lessen and the model will return to the normal approach of regulatory bodies having less input and control coming from governments.

Miyashiro: Establishing clear lines of regulatory jurisdiction and promoting coordination are critical in this environment for financial institutions. In this current crisis, we've witnessed governmental and regulatory authority and power asserted under extreme circumstances. As evidenced at the recent G-20 summit in Pittsburgh, government and regulatory coordination are essential to mitigating systemic risk in the global financial markets.

Arguably, conflicts of interest will pervade the current market-place until the governmental intervention is removed. Until then, it is important for regulators to establish clear distinctions in order to preserve independence and objectivity including:

- Managing their own financial interests (for example, US Treasury, Federal Reserve and FDIC).
- Promoting rules to protect investors and the financial system (for example, naked short selling).
- Determining appropriate monetary policy (for example, central banks).
- Coordinating among regulators items such as capital adequacy, executive compensation and repayment of government stakes.

At the heart of this question lies the need for data transparency in order for central banks and regulators to properly monitor the objectives listed above. The regulatory environment will change as the demand for more complete and timely information weighs on the market-place.

There has been a growing focus on XBRL data tagging initiatives that help identify content and improve automation. What impact do you expect XBRL to have on future data quality? Is there room for the industry to introduce further XBRL initiatives without regulatory interference?

Harkins: XBRL, like other technology initiatives, should improve data quality. In

Robert Schork, Bayview Financial

its simplest form, XBRL allows institutions and agents to communicate in information in an automated and standardized way. This should avoid confusion while allowing disparate systems to integrate and interpret the same data. There are two catalysts for future introduction of XBRL initiatives. The first is use by regulatory and government agencies worldwide. The second is organic within the market-place. As increasing numbers of financial institutions use XBRL for their reporting purposes, it will put pressure on other firms to do the same so that they can accurately exchange financial data.

Schork: XBRL is a start, but that is where they leave it. They never integrate or share it with other applications. What is needed is a registry to store and share that definition and usage information. The best way to do this is via a metadata repository. Unfortunately most corporations think that this approach is too costly, and it is, unless you create your own. But again, those skills are not easy to find.

Kennedy: Specifically designed for financial reporting, XBRL has allowed companies to produce reports and documents that can be manipulated and analyzed by computers. The financial industry has kept a watchful eye on the development and implementation of XBRL and many companies will be curious to see if it can be applied to different types of data. However, because of its design and specific function, XBRL may never prove to be a universal panacea. For the moment, regulation around XBRL varies greatly from country to country, with the US and China leading the pack, while the UK and some continental European countries implement it on a more relaxed timetable or by only making adoption of XBRL voluntary.

Noma: XBRL would be one way to move the fixed-income market toward greater transparency.

Newbury: XBRL tagging is a great standard. It is great for extracting data and giving an open standard for issuers to use. It is not a panacea though. Standards can only work to improve data quality and so long as the tools for turning a document into an XBRL document are well implemented then the quality of data being reported should be high. It will still fall to experienced data vendors to ensure that data from different sources, although in the same format, is consistent and complete. There is nothing that forces an issuer to fill all the necessary fields. I referred to earlier when talking about a "skinny set" of reference data which should be mandated as a standard set of data. For example, a key field in the issuance of a share is the nominal value. Imagine that one issuer includes the data with an XBRL tag but another doesn't. The standard works for delivery but not fully for content.

Should XBRL be mandated by a regulator? No. Although it is an open standard, mandating a format for data delivery to any single standard without mandating the amount of content that constitutes a record is not useful. It is a great step forward though for consumers of data that issuers use a standard at all. A recent corporate action announcement ran to more than 500 pages. While necessary legally, only around 10 of the fields were useful for corporate actions processing. Being able to extract those fields without wading through so many pages clearly represents an improvement for anyone in the industry.

As an industry how can we push for XBRL to be adopted? Again, we can look at ISO 15022, where take-up is estimated to be at around 22%. The bodies involved in evolving that format have created forums and interpretation grids. Data vendors and software houses have held events and marketed to customers. All this over the last 10 years or so. And we remain at 22%. We can only use the same methods to influence issuers without regulatory mandates and possibly with the same amount of success over the same number of years. Is that a defeatist view? Well, we need to find out what the incentive to an issuer to adopt XBRL reporting would be. Until that can be found and a clear ROI proven, then regulation that suggests the use of standards—but probably multiple standards—would probably be the only way to make significant inroads.

Grant: XML standards in general are good at structuring data and providing an easy mechanism to move data between originator and consumer. The issue with this approach is that there are standards for small subsections of the data that firms rely on to power their business and they're not necessarily easily integrated which is needed for a firm to operate smoothly. In addition, standards such as XBRL do not control the data creation phase, just tagging. Therefore, if the data is constructed incorrectly and assumed to be valid on receipt then the problem still exists, it's just likely to get from point A to point B much quicker, and take up more space!

Miyashiro: We see XBRL as providing a tremendous opportunity to increase reference data quality integrity. The following benefits are well noted, though they are not without implementation challenges: enhanced loading speed; no human interruption; cost savings; and scalable to other business processes.

There is room for the industry to further XBRL initiatives without regulatory interference especially as they relate to the development of taxonomies. But regulatory influence is important in mandating roadmap goals for implementation, which often can be met with resistance to change.

For XBRL benefits to be fully realized, this will require the commitment of regulators, preparers and users working in concert for a long-term benefit.

What specific areas affecting data management do you expect regulators to focus on going forward?

Harkins: It ultimately depends upon what areas regulators see as potential problems. There will be a number of cases based on last year's crisis that will be looked at to determine where new regulation will yield the best results. The obvious answer would be in valuing and reporting illiquid assets.

Organizations need to continue to be ready for a business environment where there is stronger regulation in all areas of data management, interpretation and reporting.

Schork: Data quality has been mentioned already. I think they have finally got to address the definitions and integration. The volume of data is going to explode in coming years and data management needs the tools to support that or find a way around it.

Kennedy: I believe the key future challenge that regulators have identified for the financial industry will be liquidity risk management, which requires companies to manage their operational, market and credit risk. Firms need to prove that they understand their risk exposure and perform the necessary stress tests to ensure their risk management procedures are robust. In order to fully test the variety of possible outcomes, high-quality reference data is required. We've recently seen increased interest in our business entity and corporate actions data services, as customers seek to shore up their counterparty and instrument reference data, and maintain an accurate assessment of their risk profile.

Newbury: SIX Telekurs manages a database of 5.3 million instruments and understands the difficulties of maintaining the data in all of those records. We employ hundreds of data staff around the world to do just that. It is unlikely that a regulator will have that type of budget so it is important that alongside well-trained regulatory staff, they use robust and responsive consultation processes that allow them to instead leverage industry experience. Recent consultation papers from the FSA in the UK have specified which credit ratings should be used and which data vendor should be used. Clearly, the papers were written by someone who did not understand what they were trying to regulate or didn't understand that regulators should not be mandating virtual monopolies.

We would expect that regulators will concentrate more on enforcing the regulations that are already in place and doing so in a more vigorous way, while expanding their oversight incrementally.

Regulators will look to enhance transparency of trading through things like the extensions of MiFID, and will make sure that banks have greater capital cushions and new liquidity standards. This is done in the name of consumer protection, but also to protect wider society from failures in the future. The idea of a living will seems to be taking hold, where a bank has clear unwinding policies in place in case of failure. But these latter ideas seem to be like fitting airbags to limit the effects of a car crash.

Getting down to the nuts and bolts of what needs to be done—really looking at data flows within banks, questioning why a bank has 14 different security masters—will not be done at this point.

Reference data standards are being looked at, but the regulators may need to co-opt industry professionals to help them wade through the intricacies of data management and help them to successfully regulate or enforce regulation.

I rarely agree with the BBC's business

editor, Robert Peston, but something written in his blog on October 6 makes sense. He said: "It's very much like safety on the railways. We need to decide the maximum price we're prepared to pay to avoid crashes. And we should recognize that the cost of eliminating all risk of crashes is prohibitive."

I can agree with that. The fear I have, though, is that the regulators are concentrating on building buffers without even realizing in fact that certain components in the motor and the braking system need to be looked at. If they fail to do that, then the buffers will certainly be tested again.

Grant: I would like to see regulators focus more on data creation, transparency and metadata management aspects as these are key to determining how data is interpreted and acted upon either further down the workflow within a firm or by consumers in the market. If a firm has a concrete method for creating data that is standardized and visible, it can be used across the workflow, allowing data to flow much more easily, in a more timely way and, importantly, with confidence. The cost saving achieved on the operational overhead associated with today's data processing and validation functions would be significant. More importantly, though, this transparency in the market itself would provide investing firms with far more insight into the products they hold on their books, and their constituents and terms and conditions, allowing firms to more easily monitor their investment process against policy and provide confidence back to their customers. This transparency would in turn prevent overly complex and potentially misleading products from making their way into the market, allowing a much more stable platform for consistent growth with less risk. A focus from the regulators in making sure this is adhered to throughout the organization is likely to be needed for the larger firms due to the complex nature of their structure and legacy systems. It is imperative that these changes are made to prevent future failures in the financial system, resulting from a lack of transparency in data and products across a firm's workflow.

Elliott Noma, Asset Alliance and Garrett Asset Management

Miyashiro: We expect regulators to focus much of their attention on outputs and outcomes generated from models. As evidenced by current risk-sensitive initiatives such as Basel II for banks and Solvency II for insurance companies, data management is the foundation for which all calculations are derived. Managing the volume of current and historical data will be critical for regulators in evaluating risks such as "too big to fail" and the creation of "bubbles" in our global financial system.

Data management will also be extremely important, based on current initiatives to provide more transparency through post-trade reporting. Regulators will need effective plans to handle the volume of data through the collection, analysis and dissemination process.

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In the midst of focusing on managing risk and growing their business, firms must follow processes to remain compliant with a variety of regulations, standards and directives. Firms will also need to meet new demands from regulators to address the issues identified in liquidity risk management practices, not least in the application of stress testing under extreme liquidity events and in the adequacy of contingency planning. Risk-weighted capital requirements proposed under Basel II have also posed a series of challenges for financial institutions.

The need to meet regulatory risk requirements is driving an increased demand for a wide range of high-quality, continuously available financial information, especially in the areas of reference data and valuation. Near-time, high-quality reference data —including corporate actions data—is also required to help support trading operations and keep clients up to date.

By prioritizing reference data management, institutions can get a more complete understanding of the underlying dynamics of financial instruments streaming through their applications and databases and, as a result, determine their risk exposure more effectively.

Previously disparate data sets held across an organization now need to be managed holistically. The ability to access multiple data silos—and integrate relevant data to create a holistic approach to risk—has become essential.

Additional scenario and stress testing to factor in extreme market and credit events has become a critical activity for risk departments, allowing them to understand the risk parameters of instruments being traded by their organization. High-quality reference data is required to fully test the variety of possible outcomes.

Detailed entity linkage information, which connects families of securities and helps institutions understand the relationships of the securities to the corporate structure of the issuer, is vital to maintaining compliance with regulations that require institutions to assess their exposure to a given firm, industry or market sector.

Challenges to acquiring and maintaining up-to-date entity data include disparate sources, a lack of standards and manual collection of the data. In the absence of a global identification standard, unique identification of entities continues to be an issue for the industry. There is a recognized need for a unique identifier on a global basis. XML-based data tagging initiatives may well change the way firms identify content and help to improve automation, but adoption of the standard so far varies greatly from country to country.

The current economic and regulatory

Near-Time, High-Quality Data

environment has led to a strong focus on valuation practices, portfolio risk management and transparency in the valuation process. Accordingly, financial institutions are determined to better understand the components of the valuation process, including the underlying market data, model selection and calibration strategies.

The ability to create and transact in highly complex financial instruments, specifically tailored to individual portfolios, coincides with increasing complexity from a valuation perspective. Internal risk management teams require independent valuations for complex instruments such as OTC derivatives and structured products to obtain a clear understanding of portfolio risk: an independent valuation based on market conventions offers an estimate of what a buyer in the market-place would pay for a complex financial instrument in a current sale.

Institutions must work across departmental silos, integrating disparate internal and external data sources, filtering external data according to internal rules and definitions to eliminate irrelevant data. This is especially valuable when effective, predictive modelling requires good quality data to determine, for example, internal loss projections.

A wide range of areas must be addressed: from organizational security—how information is acquired, classified and used within an organization—to using trusted data sources across. There is a need to integrate data content, technology and service levels into a coherent package. New capabilities, functionality and capacity are needed—there's no point improving the supply of data if it can't be made operational to the enterprise. But these benefits come at a cost—legacy systems and operations should be re-visited and tuned to support the broader enterprise, including regulatory reporting.

Interactive Data is known for its deep understanding of data and the processes involved as that data flows through the enterprise. Working with its customers to help address their needs, Interactive Data seeks to incorporate the effects of increased regulatory requirements into services designed to help clients manage and enhance their data assets. Data providers such as Interactive Data are raising the level of service across a broad front to meet the needs of today's powerful risk management applications.

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Paul Kennedy is European business manager, reference data, Interactive Data
www.interactivedata.com

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Reference Data Management:

Financial crises are inevitably followed by new or enhanced regulatory regimes. The Securities and Exchange Commission (SEC) came to life in the aftermath of the Great Depression, Bretton Woods institutions were created after World War II, and more recently, the Enron scandal led to Sarbanes-Oxley. Today, we have seen the emergence of a new forum, the G20 leaders' summit. Although the G20 organization was launched in 1999, it has only been since the Washington summit in late 2008 that heads of states decided to step in. Developed countries had to finance recovery plans through increasing debt levels, and it seems clear today to economists that we'd better not have to deal with another important crisis in the near future. In that context, the current financial regulatory landscape is changing rather rapidly with one clear drive: to find the right balance between tighter regulations and sustainable growth.

Existing regulations are being revamped, and we sometimes hear about Basel III or MiFID II; Ucits IV is well under way already. Some new regulations are also being established to supervise the so-called systemically important actors, meaning alternative investment funds and credit rating agencies. On the accounting side, we are progressing towards a unified set of standards with regards to fair value measurement. We feel the one thing those initiatives have in common is a call for advanced reference data management within financial institutions, and thus a drive for improved standards that favor data exchange and understanding.

Looking at Basel II, one of the current debates is to find a better correlation between capital requirements and risk exposures. Banks should therefore improve their risk management systems to achieve "firm-wide risk oversight." This means two elements are essential. First, the quality of information that feeds risk management systems; second, the capability for banks to process that information. When a global bank operates in multiple locations, with investment activities in Europe, America and Asia, the task of coming up with an overall view and understanding of risk is enormous. Banks need to build upon state-of-the-art data management in that context.

To help financial institutions dealing with reference data, the idea of centralized data utilities is emerging. Whether those initiatives will eventually lead to something tangible remains to be seen. We know that handling a multi-million financial instrument global reference database requires hefty investments, and not only short-term investment, as well as highly specialized staff across all asset classes. Bottom line, any centralized data utility would probably be able to cater only for basic data elements,

Going Back to Basics!

whereas the lifecycle of a financial instrument is complex. Actually, we also notice an opposite trend, reference data is no longer a purely tactical issue, but is becoming rather strategic, an area not seen as a mere cost center anymore, but instead can play an important role in a bank's value chain and competitive advantage.

Two other areas require our attention in the forthcoming months: fair value and hedge funds. On the fair value side, we are seeing a harmonization in accounting rules, and there will be a dedicated International Financial Reporting Standard issued on fair value measurement. In principle, we are going towards a three-level hierarchy to measure fair value, starting with use of market data, up to unobservable market inputs and mathematical models. Once the framework has been agreed upon, this can translate into data vendors' offer, with added focus on liquidity indicators, price sources types for instance.

On both sides of the Atlantic, regulators are considering the registration of alternative investment fund managers, with a view to imposing stricter governance guidelines and reporting requirements upon them. Although this is not yet finalized, we will most likely notice an increased information flow on those types of assets in the coming months. It will be necessary on our side to adapt our systems so that our customers can receive additional meaningful information when required.

Of course, other areas of regulation, such as credit rating agencies or OTC derivative transaction reporting, are also evolving at the moment. Fair value measurement though is a good example where political drive and joint efforts from regulators can lead to shared standards. It is easier for the use of data standards to develop when the legal environment is standardized too.

We are currently running a series of road shows in 17 cities around the world to help our user community navigate the flow of regulations! It is proving to be a great opportunity to share ideas with our customers and business partners from different markets and banking activities. One thing emerges from those events: in a fast-moving regulatory landscape, reference data systems will have to improve in flexibility, scalability and data quality. In this context, we will continue to offer fully encoded quality reference data and to support data standards, where they make economic sense, so that we can contribute to the sort of return on investment our customers will need to see to be able to make those improvements.

David Lecompte is market development manager at SIX Telekurs.
www.six-telekurs.com

Q&A

The Future of Tagging

Inside Reference Data speaks to David Blaszkowsky, the SEC's director, office of interactive disclosure, about the future development of data tagging standard XBRL and the regulatory involvement

David Blaszkowsky

Have standards such as XBRL become more important in today's market?
Standards make it easier for regulators and market participants alike to know what they have got. When we can't see what we've got it's a barrier to making better investment—and regulatory—decisions.

As a former Supreme Court Justice Louis Brandeis said, "transparency is the best of disinfectants." Improved transparency improves the quality of information as the user experiences it.

The SEC has already mandated the use of XBRL for company filings. Are there more areas you see that the standard could be used for?
It is very exciting to see trade organizations, companies and individuals proposing, developing and using new taxonomies on their own initiative to address important domains of investor-relevant information like social responsibility and governance. The future of XBRL should be as much in the hands of the market as the regulators.

This summer, 500 companies in the US started filing in XBRL format. What has the feedback been so far?
We have been reviewing the filings, and we're very pleased they show good faith and efforts, and high quality. We are finding many opportunities for improvement and we have begun to communicate back to the market in the form of SEC interpretations, FAQs and other public media.

Have you seen any interest from other countries?
We are talking to each other to share experiences. A lot of countries are looking at our implementation because of its scale and complexity. We are the first to require footnote tagging, for example, which is considered by many to be a particular challenge, but many folks were worried even about basic tagging, which, in the end, is proving routine. This will make it easier for other countries to proceed—and I think they may [proceed]—with more comprehensive programs.

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Incisive Media, Haymarket House, 28-29 Haymarket, London SW1Y 4RX