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Fixing the Reference Data Problem

An industry/government regulated facility to collectively maintain and access reference data is the best way to lower costs, eliminate redundancies and control counterparty risk, writes Allan Grody of Financial Intergroup Holdings.

Today's automated financial markets require data elements of a financial transaction to be accurate throughout a transaction's lifecycle. The ability to externally match and aggregate counterparty information and internally manage financial, operational and risk performance depends on its accuracy. It's the plumbing…identification and reference data, and it is essential to managing financial businesses in the information age.

Recently many vendors, technology companies and financial market utilities have proposed collaborations with different financial institutions to create utilities to collectively maintain and access reference data. The list gets bigger by the week – Smart Stream and Euroclear, Bloomberg, Thomson-Reuters, SWIFT and DTCC. IBM and Golden Source is the newest announced entrant. However, systemic risk and excessive cost would still be built into the industry's infrastructure due to the still unmitigated risk and duplicated costs from:

• the limited availability of budgets to source data from multiple vendors, how many vendors is enough;

• different vendors chosen for each firm or existing infrastructure facility thus embedding a variance in the datasets maintained by each firm and each outsourced facility;

• each firm/facility with different rules for accepting “best of-breed” data;

• duplicated activities and costs for each firm/facility essentially trying to do the same thing;

• regulators and firms still dealing with faulty definitions of aggregated risk for a counterparty whose hierarchies and definitions of business entities are determined separately by each firm/vendor;

• firms still only finding out data faults when they try to send a transaction through its settlement process and it fails to complete;

• the industry still lacking the ability to accommodate STP in any timeframe approximating trade date settlement, let alone real-time settlement;

• regulators still rejecting electronically filed regulatory reports because they couldn’t match incoming data sent electronically from firms to regulators databases; and

• regulators’ accepting electronically filed reports because they did match incoming data from firms, but the regulators’ databases had different meanings (descriptions of business entities, instrument identities, data attributes, etc.) for the matched data elements.

To resolve the disparate, fragmented, redundant and costly state of data management, a Central Counterparty for Data Management (CCDM) should be established to access and match multiple incoming sources of referential data at the pre-trade financial transaction assembly point.

The CCDM is: An industry/government regulated facility operating as an intelligent federated network, acting in one or more capital or contract markets, whose identification and reference data sets are interposed between two trading or settlement parties. The central counterparty guarantees the performance of the underlying transaction’s identifiers and reference data by providing identical

data sets for matching buyer to seller in financial transactions. It also acts as a golden copy of identification and reference data for all manner of unique, unambiguous and universal data sets for purposes of data aggregation of financial transactions for industry and regulatory reporting purposes. [For more information see: Infrastructure Issues in the Financial Services Industry: A Case for a Central Counterparty for Data Management]

The CCDM is proposed as a G-SIFI (Global - Systemically Important Financial Institution) sponsored consortium, established to dispense with the legacy past of technology companies and vendors that are beholding to the silo mindset of financial institutions for sustaining their business model. The largest banks and insurance companies in the world are designated G-SIFIs (there are 39 such entities), so designated by the G20's Financial Stability Board.

The spend on multiple copies of the same technology in different silo businesses, or for different technology suppliers for the same technological end result within the same enterprise has sustained many legacy technology companies far beyond their usefulness. Their usefulness in back-end processes was once innovation and speed to market. Now rapid deployment of point solutions at the business application front end is their value-add. The plumbing in the basement need's a different model to fix.

Wouldn't someone on top (the CEO perhaps) see this excessive silo spend and try to get the plumbing products installed as an enterprise-wide shared product? Not really, because each silo owner runs its own shop, protecting its revenues, and budgeting for its own technology. It has also caused a set of proprietary codes to infest the silos for identifying customers and products, the same customers and products that are identified differently in each business segment and yet again different in other financial institutions. It makes enterprise computing "difficult" to say it using the least pejorative term. It certainly stymies industry-wide undertakings.

Isn't it time for the new category of financial institution, the G-SIFI, to take control of its own destiny, rally around the CCDM model, bid out the construction of it, and tie their fate to the global regulatory initiatives of the Financial Stability Board. It is a truly remarkable attempt by the FSB, a global standards body commissioned by the heads of state of the G20 countries, to try to fix the plumbing of our industry by setting global standards for unique, unambiguous and universal identifiers and their associate reference data. Let's rally around both the CCDM and the FSB's global identification initiatives; ask the data

vendors, technology companies and financial market utilities that are living in the silo legacy past to bid on the project under G-SIFI consortium control; and set a course around tomorrow's technology solutions that are already here today.

We all can recall the captive market and the assumed obsolescence built into US made cars before the Japanese car makers decided to build and sell longer shelf-life cars in the US.

For additional research on this topic see FinancialinterGroup.com.