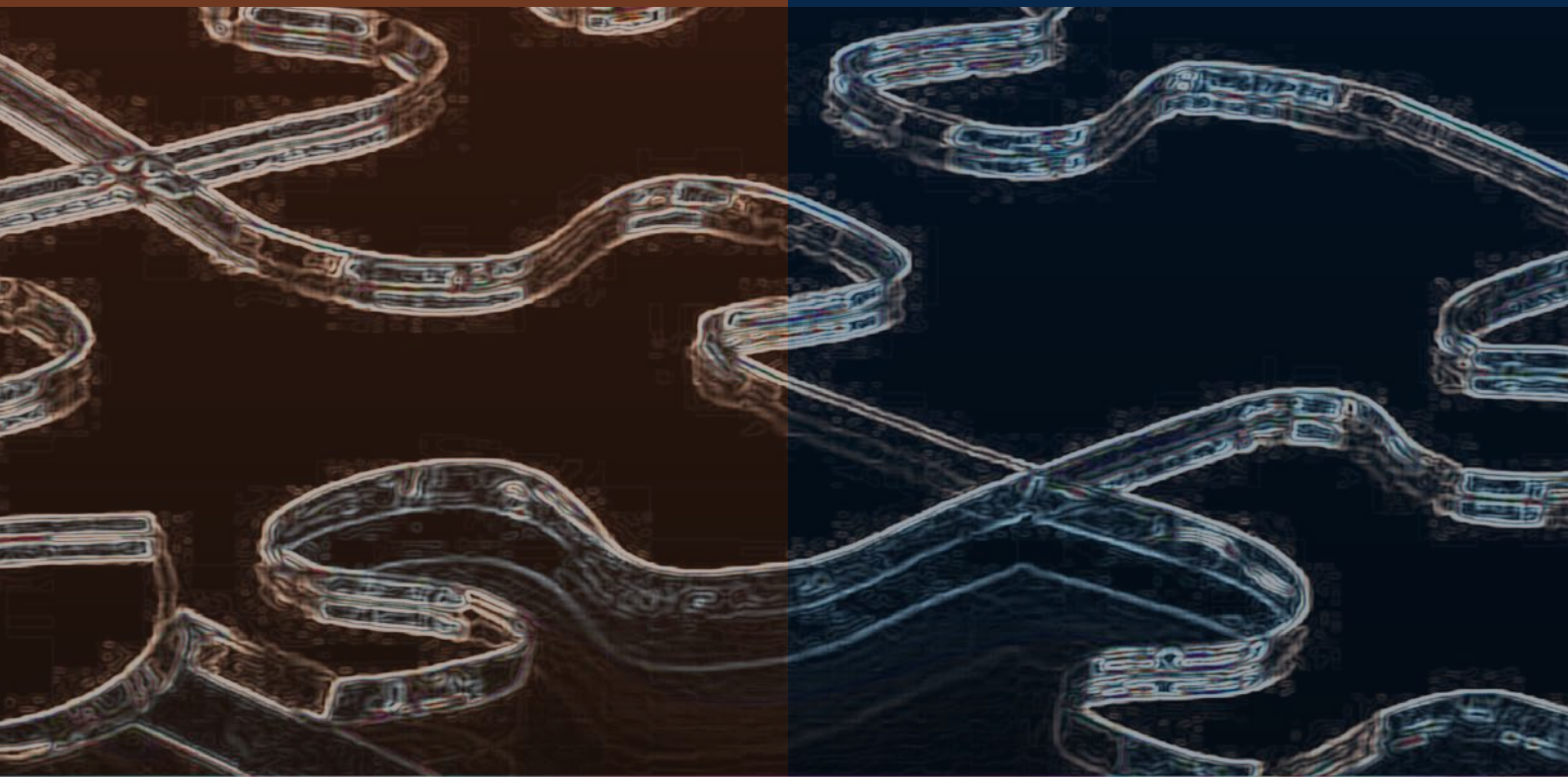


# ENTITY DATA **management**

An **A-TEAM**GROUP Publication  
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## KNOW WHO YOU'RE DEALING WITH?



Entity data management has historically been a rather overlooked area of the reference data landscape, but with the increase focus on managing risk, the industry is finally taking notice. It is now generally agreed to be critical to every financial institution; although the rewards for investment in entity data management appear to be rather small, the consequences for getting it wrong are severe. Settlement, legal, financial, regulatory and reputational risks are all inherent in a failure to properly manage entity data.

Risk mitigation has become the key driver for change in this current economic climate and entity data plays a significant part in this. The emergence of golden copy logic and enterprise data management in the entity data space is a positive step forwards for the industry with regards to better data management. Financial institutions are continuing to invest in improving their entity data management and the vendors in this space have stepped up to the plate to provide more integrated services. Connectivity and integration have become important buzzwords for the entity data landscape.

The space is not without its challenges, for example the lack of an industry standard business entity identifier, but it seems that evolution is well underway.

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# An evolutionary process



Virginie O'Shea, Editor, A-Team Group

This year has seen the entity data management space experience the beginnings of an evolution, as its role in the wider enterprise data management (EDM) framework becomes clearer. Golden copy logic may have finally found its place in the counterparty data world with the announcement at the start of the year of a couple of partnerships between entity data vendors and EDM vendors.

In February, Standards & Poor's and Siperian announced that they were entering into agreement under which S&P's Security to Entity CrossWalk would be added to the Siperian master data management platform MDM Hub. During the same month, EDM vendor GoldenSource and Avox announced their strategic alliance under which the Avox business entity data service would be integrated with the GoldenSource EDM platform.

Both deals indicate that EDM is influencing the entity data space via the creation of linkages between data sources so that the data is ultimately more comprehensive. This desire for a golden copy approach can be linked to a desire to avoid data inconsistencies and inaccuracies that have previously plagued the market and led to incomplete consolidations, out-of-date information and exposure to regulatory risk, trade and settlement risk and reputational risk.

The two announcements at the start of the year build on existing relationships that both vendors have developed in the entity data space. Siperian already has relationships with both Avox and CounterpartyLink and GoldenSource is already linked to D&B and

CounterpartyLink. Furthermore, linkages are starting to be provided within data feeds by the data vendors. Feeds like CrossWalk, RED and Avox are beginning to combine issue and issuer/product and financial institution information in the feed so that there are more comprehensive data sources within the entity data space.

Entity data includes a number of buckets of information comprising legal information, credit data, risk data and operational data, which all come from a range of sources. Different providers cover different areas and there is no definitive list of the data vendors that cover all data feeds. Connectivity is vital as there isn't currently this single source for all entity data and therefore a platform is needed to link together different types of information from different sources. EDM is being positioned as a solution to this dilemma and the golden copy logic for security master data can be applied to legal entity data. This is less for comparing different sources of the same data, and rather for the intelligent linking of different data items.

However, the developments in the entity data world this year have not been limited to those being driven by EDM vendors, Markit announced the launch of its new counterparty and compliance documentation library at the start of May. With a view towards greater transparency and connectivity, Markit has said its new offering will allow financial institutions to post, manage and share compliance, counterparty credit and regulatory documents securely.

Markit Document Exchange automates KYC, anti-money laundering and compliance certification processes in

order to reduce risk and lower operational costs in the counterparty data space. The service is aimed at both the buy side and the sell side and five banks and two asset managers have signed up for the service thus far.

Despite the downturn in the markets, investment by financial institutions in the entity data space has not tailed off. This is supported by the launch of these vendor initiatives and suggests that institutions are using these solutions to more proactively manage risk. Research by A-Team last year also highlights this trend towards investment in improving client and counterparty data as a "defensive" measure against risk exposure.

The report, *New Wave for Counterparty and Client Data: Traditional Methods Make Way for Proactive Risk Management & Compliance*, found that 87% of the respondents, which were made up of banks, broker-dealers and asset managers, considered compliance to be the most important reason for aggregating customer data. This was closely followed by risk, at 73 per cent, and credit, at 60. Firms want to achieve full awareness of potential risk exposure on an ongoing basis and the credit crunch reinforced this trend, the report indicated.

These projects have been going for some time and 93 per cent of the respondents in the report indicated that they had either been engaged in reorganising their internal counterparty data via the process of centralisation or planned to do so soon. Most respondents had modified or planned to modify their in-house solutions, at 76 per cent, or legacy systems, at 72, and 38 said they had implemented a third party solution to address the issue.

This preference for using legacy in-house systems for this type of data may be down to the nature of the data itself. Unlike instrument data, client and counterparty data is fundamentally tied to an institution's business practices and strategy and it has therefore traditionally been managed in-house. As institutions have grown both organically and via acquisitions, the legacy systems that deal with this data have been stitched together to get a better idea of risk exposure. Moreover the lack of standardisation in the entity data landscape as a whole means that proprietary solutions may seem the simplest option.

The A-Team report, however, suggests that this bias towards in-house solutions may be challenged as a side effect of the search for greater flexibility and scalability. The movements being made by vendors towards adopting a golden copy approach and EDM principles in the entity data space may also make third party offerings far more attractive to institutions.

Furthermore, the report suggests that as the lines between instrument and counterparty data repositories continue to blur, the need for the two types of data to be integrated increases. This can be illustrated by looking at the modelling of relationships in complex collateralised debt transactions, which demonstrates the interrelated nature of instrument and counterparty data. Legal entity data seems to therefore be taking its rightful place at the reference data table as a result of its contribution to better risk management.

However, the entity data market has not been without its issues over the last few years. The lack of an industry standard business entity identifier (BEI) continues to cause serious issues within the market and recent research by the EDM Council, Bearingpoint and Swift indicates that this problem is not likely to go away any time soon. The industry is still unconvinced that the benefits of introducing a BEI outweigh the cost, the report states.

The report is the culmination of primary research that included formal multi-

person interviews with representatives from 15 institutions and a number of informal discussions with other practitioners. It indicates that although there is broad agreement in the industry about the value and importance of an industry standard BEI for external cross-referencing, the processing of corporate actions, automation of post-trade processes and for non-standard regulatory reporting requirements, the cost of its introduction is still too high.

Institutions are therefore more willing to invest in "point solutions" on a departmental or functional basis with their own internal identifiers than to invest in an enterprise-wide implementation of BEI. There is a lack of a sufficient incentive to move away from proprietary identifiers such as a regulatory mandate, the report contends. To this end, the industry witnessed an international vote of no confidence concerning the introduction of the ISO 16372 international business entity identifier (IBEI) when eight countries voted against the standard last year.

Eight European countries have since adopted the IBEI, but it failed to gain the backing of countries such as the UK and the US during the second ballot among national markets at the end of 2007. The countries that have adopted the standard thus far currently comprise Switzerland, France, Luxembourg, Liechtenstein, Belgium, Germany, Austria and Spain. Vendors such as Telekurs and WMDatenservice have also indicated their support for the IBEI. To this end, Telekurs Financial implemented the IBEI codes for its Valordata Feed and its financial display Telekurs iD in May this year.

One of the key reasons for the failure of the ISO IBEI effort was the lack of a volunteer to be the registration authority for the standard. The industry was calling for Swift to do it, but Swift was reluctant to take on the task of managing the allocation of codes to the millions of entities that would need to be covered by a truly global solution.

However, the IBEI is not the only option being considered by the industry for

entity identification; there has also been some serious discussion about making the bank identifier code (BIC) a universal identifier. Swift has talked about extending the code to cover investment funds via collective investment vehicle identification codes (CIVICs), although this plan appeared to hit a stumbling block at the start of 2008.

Swift's plans were put under review at the start of the year reportedly due to concerns around cost and the lack of a concrete business case. It has supposedly been difficult to establish a sound business case for creating codes for the broader legal entity community that could be used for a whole range of different purposes, rather than for well-defined business purposes such as transaction reporting.

Although all seems to have gone quiet on the CIVICs front and the IBEI has stalled, all is not lost as there is another contender to the standard entity identifier title. Standard & Poor's is proposing that an industry solution could be created from the six character issuer identification component of Cusip instrument codes. S&P, which operates the Cusip Service Bureau on behalf of the American Bankers Association, has said that it is looking seriously at how it can contribute its experience to the BEI landscape.

According to S&P, as well as identification of instruments, Cusip codes also contain unique identification of issuers and this is one of the factors that distinguish Cusips from other numbering conventions. S&P's plan to ensure coverage across the entire counterparty space is to seek viable collaborations with appropriate partners and discussions are underway to this end.

Regardless of which BEI initiative bears fruit, the very fact that so many discussions are going on in this area is indicative of the importance of entity data management to financial institutions in today's economic climate. Rather than the historical view of entity data management as a low priority concern, it has now become integral to risk management.

# The Headache of Standardisation



James Redfern, Head of Sales & Marketing, CounterpartyLink Ltd

**W**e live in a world that is increasingly governed by standards in every walk of life, none more so than in the world of regulatory compliance, risk management and data processing. All of us have had to adapt our systems and processes to meet compulsory legislation and align ourselves with industry standards that have become accepted as the norm. Examples of these range from The Patriot Act, Basel II and UCITS III legislation, to name but a few.

It is nevertheless interesting to note that within the investment and financial services community there remain vast universes of content that have defied the best efforts to conform to standards. I refer in particular to the sector in which we work, namely legal entity data.

**Where do the headaches begin? Certainly in sourcing, collecting, extracting, standardising or normalising content, and thereafter maintaining international legal entity data for your in-house and external requirements**

Where do the headaches begin? Certainly in sourcing, collecting, extracting, standardising or normalising content, and thereafter maintaining international legal entity data for your in-house and external requirements.

If we start by looking at the origination of legal entity content, we find ourselves at the many hundreds of company registry authorities around the world.

Needless to say, the way companies and other legal entities such as funds are

registered varies enormously from jurisdiction to jurisdiction, many of which reflect inherent national and business cultures.

So, the first obvious barrier might be the language in which the registration is filed. Date formats are varied, orders and formats of postal and physical location addresses are numerous; the type, definition and number of fields completed at registration authorities are inconsistent – and all this before we realise that some registration authorities are paper based, others are on-line, some are free, many require payment to access, and output formats are all different.

Even among businesses from within the European Union, cultural differences predominate and there remains little standardisation in respect to the registration, filing and retrieval of information from the many national and regional registration authorities across this union.

Now, compound all the above with the fact that in a global financial services organisation you will have many consumers of legal entity data. They will exist at many points within their own internal business units.

You will therefore find different teams dedicated to maintaining versions of the same content for different applications, such as account opening, risk management, customer mailing, or reviewing clients for KYC/AML purposes.

CounterpartyLink faces these issues with every client and we have made a business providing solutions to these issues. We are always faced with duplica-

tion of legal entity data content in any organisation we work with – even before we consider the accuracy of the content held in internal repositories.

We are faced with many of the same challenges as our clients in keeping legal

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**We have built up nearly four years of expertise in this area, knowing where to go to research exotic companies and funds, and maintaining and refining processes all the time**

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entity data accurate and current. One of our challenges, however, is not duplication, as we only maintain one repository of legal entity data.

We need to keep the content historically – for our clients – and continually focus on repapering or reviewing content to reflect changes in the entities as they occur. We keep proof of the data we have added to our database in the form of electronically stored copies of the sources from which we actually extracted content – our ‘Audit Trail’.

The key point is that all data we manage conforms to our own data schema, which is bounded by written definitions for each field. In this way we can normalise content from all the world’s registration authorities and ensure that they can be compared side by side, and perhaps more importantly, be fed into client repositories and applications in a single form.

So, in many respects we are a mirror of your internal functions. However, there are some key differences.

This is all we do – we are only in the business of supplying accurate legal entity data content to our clients. Our maintained content is available to all at a fixed cost per entity.

You will have many variable costs to manage by maintaining this content in-house. We have built up nearly four years of expertise in this area, knowing where to go to research exotic companies and funds, while maintaining and refining processes all the time.

Furthermore, we handle information in something like 25 languages. We cover more than 190 different registration authorities.

So, why keep much of the data validation functions in house? No doubt there are historical reasons to do so – it is only recently that a small number of vendors such as ourselves have emerged to provide highly accurate and auditable legal entity data to the industry – as well as

concerns about ‘losing control’ of internal processes, and the inevitable internal politics.

We can now help you with this. We are now able to make available to you the software and workflow we use in combination with the lists of external data sources, maintained by CounterpartyLink, along with sets of rules relating to how such sources need to be processed – again maintained by us.

You are able to supplement your own in-house data processes in the knowledge that sources and business rules are continually being monitored for changes.

This facility is particularly important in helping to maintain your high-risk and sensitive client accounts in-house, details of which cannot be passed outside your organisation.

View us as a partner, and use us to raise not only the quality and normalisa-

tion of your global legal entity data, but also use us to help manage your costs in doing so.

*CounterpartyLink provides global legal entity data, collected and maintained with processes consistent with the stringent standards required by today's risk management and regulatory compliance legislation.*

*Detailed information on legal entities, which include corporations, governments and funds, is collected in centres around the world, from primary sources and registration documents, with all data supported by an audit trail back to the source.*

**CounterpartyLink**  
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# Credit Derivatives

By Neil Edelstein, Senior Director of Product Solutions at GoldenSource

**T**rading in OTC derivatives has grown dramatically in the past few years and firms have faced a number of challenges in processing and settling these trades in a timely way. These innovative products have become important risk management tools offering deep liquidity for brokers, asset managers and hedge funds alike.

As in many fast growing markets, regulators have been concerned about the ability of the market's young infrastructure to accommodate its phenomenal growth effectively. Is the market capable of handling the volume of activity in a manner that does not create undue risk especially in a meltdown environment?

There are those, Warren Buffet, the richest investor in the world among them, who have warned for years that financial innovations such as derivatives, credit swaps and repackaged debt were a disaster waiting to happen. Yet the growth and popularity of OTC derivative trading continues unabated even through the credit crunch. OTCs remain customised structured products that suit many investment strategies. They are here to stay and are going mainstream.

## Market Implosion

Yet post trade operational concerns remain. The mundane, but important, activities of confirmation, documentation, assignation and processing seem to have fallen behind in the rush to 'do the deals'. With growth also came complexity as investors sought to represent different levels of credit risk with more sophisticated instruments. A market was being conducted with huge and often unknown exposures to Counterparties, and overall market risk.

As an example, within a decade the Credit Derivative Swap (CDS) market emerged practically out of nowhere to

record notional values to the tune of \$50 trillion, according to the Bank of International Settlement (BIS) end of 2007 survey. With the bursting of the housing bubble in the US and elsewhere, those left guaranteeing those assets are getting wiped out and resulting counterparty effects are reaching every corner of the global financial landscape.

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## Regulators have been pushing hard to get market participants to focus on harnessing appropriate industry infrastructure and technology to gain efficiency in the OTC derivatives processing area

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Regulators have been pushing hard to get market participants to focus on harnessing appropriate industry infrastructure and technology to gain efficiency in the OTC derivatives processing area. The backlog has been cleared, but the length of time it is taking to clear trades is still too long leaving systemic counterparty exposures too high. A report produced by Market Analyst Celent entitled "OTC Derivatives: The Post-Trade Landscape for Hedge Funds and Asset Managers" estimated that up to 30 per cent of OTC derivative trade confirmations contain an error (or errors) and require subsequent handling for rebooking or amendment."

Although it might be tempting to blame the financial engineers behind derivative innovations for the current market implosion, real failures can also be attributed to many institutions demonstrating a poor understanding of these new instruments or the underlying assets, as well as lack of transparency into the real counterparties exposed to the deal. On a more practical level poor operational processes with limited auto-

mation are also root causes.

The most significant difference between the buying holding and selling of securities and OTC derivatives is the introduction of counterparty credit risk in addition to the market risk of the underlying securities. The operational overhead in terms of affirming, confirming, marking to market, calling or posting collateral, scheduled fixings, payments and corporate actions of potential changes in the underlyings of a trade that may be open for years is enormous.

## So What Are The Answers?

All of the above operational processes require up to date unambiguous reference data pertaining to all aspects of the trade including location where trade is booked, credit rating, mark-to-market, legal product definitions for confirmation nettings and collateral contracts, etc. Both parties to an OTC trade need to have a clear and consistent understanding of all the relevant information around a particular instrument so that they can answer:

- When and where this instrument is settling?
- What is the actual exposure?
- What is the credit rating of all the paper?
- Who is the issuer?
- Who is customer?
- What is the position?
- Who are the transaction partners?

If any of the data is wrong or incomplete there is the immediate risk that the trade either cannot be legally confirmed or that it is confirmed wrongly which then spills over into problems with portfolio matching, netting, margining and settling of trades with that counterparty. Failed and disputed trades and volume constraints caused by operational inefficiencies are lost business opportunities.

On a wider level each party needs to aggregate this data with all its other

trades in order to calculate its true exposure to the counterparty, underlying securities and their issuers. Inability to measure credit risk and audit all data processes contributing to its calculation is extremely costly under Basel II and Sarbanes Oxley regulations.

The above example is fairly simple with straightforward equity underlyings. As products become increasingly complex they often cross boundaries between traditional divisions such as equities, fixed income, FX or commodities, making counterparty tracking and exposure measurement even more onerous.

Nearly all OTC trade documentation also defines additional termination events beyond default on the trade itself such as material change of ownership, ratings downgrade or default on other securities issued by the counterparty or any of its affiliated companies. To truly manage the risk this should also be linked to the trade.

As has often been the practice, siloed solutions were developed for structured products processing. Although this may solve the immediate time-to-market issues, it does not allow for an integrated approach or view. When OTC support systems are fragmented, the potential for costly errors and manual reconciliations is compounded.

From a purely operational perspective, the tendency to implement a new point solution for each new product group has left institutions with a set of incompatible and inflexible management tools

that are no longer capable of responding to the demands of a global market for innovation. From a strategic point of view, the lack of coherence not only translates into higher cost of sales, but – more importantly – makes it all but impossible to accurately assess risk and manage P&L at the level of the entire enterprise.

**For Hedging or Speculation**

Investors use derivative products (whether OTC or exchange-traded) either for hedging or speculation. Derivatives that trade on an exchange are transparent, since mark-to-market data can be generated from the daily trading of these products and there is no perceived counterparty risk. This can be stored as referential data then used for operations, trading, and analytics and so on.

**OTC derivatives are not transparent, and financial institutions cannot easily maintain accurate referential data for them**

By contrast, OTC derivatives are not transparent, and financial institutions cannot easily maintain accurate referential data for them. With no clear view across many siloed systems, the institution will be significantly exposed to unknown risk. To successfully mitigate the risks of the latest generation of complex structured products, the Risk Managers of these firms need to be able to see all the facts: instruments, customers, counterparties, trades, positions – and to un-

derstand how they are linked.

While most financial institutions have been addressing their securities and market data management platforms, counterparty data is becoming more critical to the success of a firm’s enterprise data management efforts.

To enable an adequately rapid and low-risk response to the challenges of managing complex structured products, institutions need robust fit-for-purpose systems based on a centralised, comprehensive financial model that is adaptable to new requirements and that supports very high speed-to-market.

Adopting Enterprise Data Management (EDM) is the way forward. It is based on the creation and maintenance of a trusted golden copy of data, which includes wrappers that define and provide context for that data

Building a new product – no matter how exotic – on a capable EDM platform immediately enables an institution to see all of the underlying links and dependencies, and to understand the credit risk across all components and counterparties for a particular product. EDM can also readily provide detailed insight into the profitability associated with any customer or instrument.



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GoldenSource solutions dismantle barriers. Using the industry's most comprehensive financial data model, GoldenSource creates a consistent and centralized data management layer. This transforms your reference data for all financial instruments, clients and counterparties into trusted and interlinked data assets across your company.

GoldenSource can also store positions, balances and transactions to show a real-time aggregated view of risk and exposure. That is why our applications are used by so many leading financial institutions. To find out more, email [info@thegoldensource.com](mailto:info@thegoldensource.com) or visit us online.



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