

## Overview: Re-Regulation and New Regulation in the US: Technology Processing Requirements

### *Are we in a recession yet, Daddy?*

There is an old joke from the 1930's that defines the differences amongst **recession**, **recession** and **panic**. A **recession** is when your neighbor loses his job. A **depression** is when you lose your job. A **panic** is when your spouse/partner loses his/her job!

At the moment, we are only in a relative recession (inflation outstripping growth), except for those unfortunate folks in depression. These people comprise less than the 5% of the US workforce who have lost their jobs in the past six months. No cause for panic—yet. Just some food for thought for the next two-three years.

The bailout of a private investment bank by the Fed with a 29B Dollar guarantee is a secular change in government intervention into the economy. More drama comes from the departure of the major European bank chairman caught with a 5 Billion Euro trading loss. It could happen in the US—and it did with Enron, trading in energy and bandwidth. Look for the mini-series on that this year. The Bear Bailout mini-series will be more like a Michael Moore mockumentary or Bryan Burroughs as reality Wall Street.

What does this have to do with the Chief Compliance Officer (CCO), Chief Privacy Officer (CPO) and Chief Security Officer (CSO) in the modern corporation? Everything! When do they have to provide better, cheaper faster solutions that help optimize operational performance? Always!! As a result, Information Technology is the central focus of optimization. Suffice to say, at the same time in dealing with re-regulation of financial markets, the C-level executive faces a challenge of consolidating operations (more efficient organization) and operational facilities (more efficient processing).

This paper focuses on the latter challenge: better, cheaper, faster solutions in the entire life-cycle within operational facilities. This runs the gamut from definition through to the operation of new and changed business capabilities. The specific focus is on regulatory processing implications of concern for a financial firm's CCO, CPO and CSO.

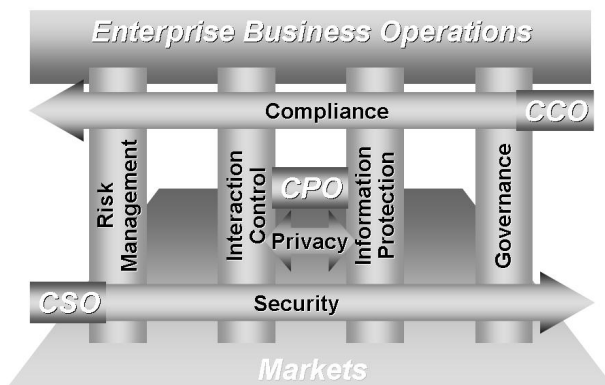
### ***Pillars of Trust Needed for Financial Markets***

Based on the unfolding news stories, re-regulation of U.S. financial markets is a certainty to proceed over the next decade. This comes at the turn up from the current 25+-year cycle of de-regulation. During the deregulatory period, lack of a more vigilant (not overbearing) oversight has precipitated a few poignant problems to rear up, like the corporate accounting frauds of Enron, WorldCom and Adelphia. These corporate frauds entailed losses of 10's of Billions and a slight degradation of public trust.

These three frauds and other financial event disruptors in 2000-2 were essentially cases of Private Profit, Private Risk. But, these particular failures pale in comparison to the current sub-prime bust and the resulting constriction in credit with its attendant

foreclosures, defaults and failures. The current sub-prime and related credit crises are examples of Private Profit, Public Risk. The current credit crisis entails projected total losses of about \$1T and significant loss of public trust in markets and government's ability to secure the general weal. These losses are significant. However, they are a mere 1% of US Wealth of over \$100T and less than ½ % of a total World wealth in excess of \$200T. The world is indeed flattening when it comes to the domiciles of wealth.

### Categories of CCO, CPO and CSO Concerns



**Figure 1: Pillars of Trust in Markets**

As a result, public and private trust in markets remains a huge issue. What are the main pillars needed to build, enhance and support trust in financial markets? How does a CCO, CPO or a CSO attend to and promote the strengthening and/or building of these Pillars of Trust? The short answer is they identify and articulate processing requirements to be realized by Business Processes, Work Flows and Information Technology.

Each of the CCO, CPO and CSO has his/her respective role attitude. With respect to the Enterprise, the CCO is external facing, while the CSO is internal facing, and, the CPO faces both outward and inward. Each contributes to the strength of the Pillars. The CCO is concerned with the broad class of surveillance implications derived from guidelines and rules. The CPO is concerned with safeguarding Client information from undue disclosure and generally, Client privacy. The CSO is concerned with the transactional implications of said same.

Figure 1 depicts four main categories (pillars) of concern for trust building by a CCO, CPO and a CSO. These four pillars cover the panoply of existing, evolving and to be written governmental and industry regulations and rules. They are an extension of Basel I and II Accord concepts and how the relevant corporate officers should think of them.

For the purposes of the considerations here and in future discourse, the following sections describe the scope of each of these four category pillars. These descriptions immediately below are not exhaustive of all the nuances of each. The goal is be illustrative of the

scope and depth of regulatory guidelines and rules facing the CCO, CPO and CSO today and going forward in the two/three-year future. The next installment contains a deeper discussion of each category and the framework for deriving transaction processing implications of each.

### ***Risk Management***

Risk Management is concerned with regulations of capital reserves and the assessment processes for measuring and identifying levels of exposure.

### ***Governance***

Governance is concerned with corporate, industry and government oversight of Public and Private Market activities. Generally it focuses heavily on assurance of transparency of all processes.

### ***Interaction Control***

Interaction Control is concerned with integrity of counterparty and market transactions in addition to assurance of non-conflict of interest within and among these transactions.

### ***Information Protection***

Information Protection is concerned with maintenance of privacy for counterparties and their respective proprietary and personal data.

### ***So what?***

In future installations, we will consider the IT processing implications for implementing the inevitable new and updated regulations in US markets and elsewhere.

The World is one integrated financial system, for better or worse. Automated oversight of financial transactions and interactions is the only way we will be able to accommodate these new requirements in a scalable fashion. Otherwise, they will be a huge impediment to US and World economic growth.