The Critical Nature of Data Quality in Today’s Regulatory Environment

The RMA/AFS Data Quality Survey indicates that all banks believe accurate data is essential for more timely identification of emerging problems and for reducing regulatory and legal risks.

Today's financial services marketplace is global in nature, and volatility appears to be the norm. Meanwhile, new waves of regulation are driving banking organizations to collect broader, deeper data sets, to enhance risk identification and control structures, to upgrade reporting capabilities, and to improve transparency. All of these interrelated goals depend on accurate, timely data.

Throughout the recent crisis and thereafter, RMA and Automated Financial Systems, Inc. (AFS) sponsored annual surveys of large financial institutions to assess the state of their enterprise data supporting credit risk management. The 2011 survey was the fifth to be conducted.

For the first time, RMA and AFS also conducted a data quality survey of the community banking industry. The goal was to benchmark the progress community banks are making in addressing challenges pertaining to data quality, integrity, availability, and transparency. In addition, RMA and AFS looked at differences in how large financial institutions and community banks manage their data.

Data Quality and Regulator Confidence

The Dodd-Frank Wall Street Reform and Consumer Protection Act has changed the way in which regulators approach and focus on data quality. The Dodd-Frank Act mandates, among other things, that large financial organizations conduct internal stress testing twice a year and that the Federal Reserve conduct its own annual independent stress test. Data-collection initiatives such as the Comprehensive Capital Analysis and Review are central to the Fed’s ability to meet this congressional mandate.

The large financial organizations are reporting loan-level details on essentially all of their significant asset exposures.
Responsibility for data quality management currently resides in the right place, as lines of business are taking primary responsibility. Community banks, on the other hand, have assigned responsibility for data quality management to loan operations or credit administration, or they have shared it across several areas.

- Regulatory requirements are more of a driver for large institutions’ data cleanup initiatives, while community banks are driven more by risk management and quality initiatives. For large banks, money budgeted for data quality improvement has yet to abate.
- Banks around the world are beginning to assign data management responsibilities to a senior-level position.
- All banks, regardless of size, report that accurate data is essential for more timely identification of emerging problems and for reducing regulatory and legal risks.

Rating the Quality of Data

Of the large-bank participants, 46% rated the quality of data within their institutions as either excellent or above average, which was unchanged from last year. Of the large-bank participants, 46% rated the quality of data within their institutions as either excellent or above average, which was unchanged from last year.

Approaches to Data Management

The surveys, which questioned participants about their data management practices in 2011, focused on two key areas: data quality and approaches to data management. Participating institutions provided views on their organizations’ state of data quality, how they are using the data to manage through the crisis, and what they are doing to improve the quality of their data. Improvements have been seen in the quality of data used to support credit risk management.

Key findings from the surveys include the following:
- Significantly more of the large banks report that responsibility for data quality management currently resides in the right place, as lines of business are taking primary responsibility. Community banks, on the other hand, have assigned responsibility for data quality management to loan operations or credit administration, or they have shared it across several areas.
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results in North America may have been influenced by three demanding stress tests in which institutions have had to supply reams of data to the regulators.

In addition, banks of all sizes reported these top three benefits from increasing the quality of data in support of credit risk management:

• More timely identification of emerging problems.
• A lessening of regulatory and legal risks.
• Reductions in credit losses, loan-loss provisions, and other costs.

Defining Data Quality

Data quality also means different things to different users. Senior managements might link data quality to the goal of receiving data that will help them make informed decisions about the risk within their institutions. Meanwhile, relationship officers might associate data quality with an accurate, timely view of their client relationships.

At the core of data quality is assurance that the data is entered accurately into the system and then presented in an actionable format. Regardless of their asset size, all participants rated accurate data entry as the key factor in defining data quality.

In addition to accurate entry, the other top factors entering into data quality definitions were as follows:

• Balances foot with accounting records.
• Robust data is being captured.
• End-of-period reconciliation is accurate.
• Data aggregation is timely.

Challenges in Risk Technology Systems

In complex financial institutions, particularly those that do a lot of acquisitions or portfolio purchases, data feeds from multiple source systems are the norm in reporting. And in efforts to combine data from various source systems, certainly one objective is to have the process not only as automated as possible, but scalable too.

For this question, survey participants were asked to rate the different challenges found in their risk technology systems or processes. A “1” indicates only a slight concern and a “5” a major concern (see table).

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This approach provides the banks and their regulators with an understanding of which organizations have the data and which do not, and it also provides information about the quality of the data. The European banks have been through a similar process.

With this experience fresh in the minds of many participants, the survey then asked them how effectively they think their organizations manage enterprise-wide risk. This year, 61% of the large banks and 49% of community banks indicated that they effectively managed risk across the enterprise. In addition, among large institutions, the North American banks were far more optimistic this year than were their European counterparts. For community banks, those in the Mid-Atlantic and western Midwest were far more optimistic than were banks in the South and Southwest.

Perhaps preparations for Dodd-Frank reporting, as well as reporting to the U.S. Treasury’s new Office of Financial Research as well as the Consumer Financial Protection Bureau, are paying off with more effective enterprise-wide risk management.

Drivers of Data Initiatives

Ongoing data cleanup initiatives remain extremely important and have become part of the yearly goals within financial institutions. When asked about plans for a formal cleanup initiative in the coming year, more than 80% of large institutions and more than 70% of community banks indicated that they had a data cleanup initiative under way or planned.

For banks of all sizes, the drivers for these data quality/cleanup initiatives were “risk management initiatives” followed by “regulatory requirements.” Quite a few participants indicated that it is part of their normal effort to keep data accurate. More and more, institutions are implementing automated efforts to ensure that data not only enters the system correctly, but remains accurate throughout its lifecycle.

In addition, among the initiatives to emerge from the financial crisis is that of banks at least beginning to explore the benefits of real-time credit risk systems. Although only 8% of the large-bank respondents were moving to real-time systems in some areas, a growing number are at least beginning to explore the benefits of going to real time. With regulatory pressures only expected to increase, particularly for the banks viewed as systemically important, it would appear that the number of banks moving in this direction will continue to increase.

RMA and AFS are grateful to all of the participants in the surveys. Identities were masked, and each participant received a full report of the survey results. For more information about RMA studies or to learn how you can participate in future surveys, contact Stacy Germano, RMA Associate Director, Enterprise Risk Management, at sgermano@rmahq.org.

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