

# waters

## The Options Symbology Mandate

Like some politicians, the options market has character issues. Is your firm ready for the character representation changes under the new Options Symbology Initiative?

*Moderated by Phil Albinus with photos by Amy Fletcher*

There is a new mandate in the financial IT arena. The new Options Symbology Initiative (OSI) will implore investment firms that support trading in listed options to increase an option's current three- to five-character symbol to a total of 21 characters. Needless to say, this four-fold increase will require an overhaul of trading systems to meet the deadline, which was pushed back from August 2009 to a yet-to-be-determined date in 2010. In March, Waters gathered a panel of industry elites to discuss this vexing new mandate. Our panel included Kevin McPartland, a senior analyst with Tabb Group; James Leman, principal and head of capital markets at Westwater Corp.; George Tull, CTO of OnPoint Executions; and Archie Acharya, client relation manager for Infosys, the briefing's sponsor.

**Waters:** At first glance, the Options Symbology Initiative resembles a mini

Y2K. But Y2K had a hard stop date, and every firm had to be ready by Jan. 1, 2000. Now, it sounds like the OSI deadline is being pushed back eight to 10 months. Will this allow for breathing room or will it lead to further procrastination?

**James Leman, Westwater Corp.:** I think it will probably bring a little bit of both depending upon whether or not the adoption of the initiative is more than voluntary. There was a lot of pressure by the exchanges to get this done inside the industry, but if there is not a regulator bearing down on you, the possibility of slippage exists. In terms of getting the kind of resources that have to be put in play to address the issue, you really don't want to prolong it past a certain point. There probably will be an attempt to escalate the importance of getting things done by a certain point with certain minimum things accomplished. It is quite possible the Options Clearing Corp. (OCC) doesn't

want to let things linger if they are prepared. They will ask that things be done by a certain date and put pressure on the clearing firms—which are a small universe—to accomplish it. The market data vendors have to be in it as well.

**Waters:** This is an industry that is fairly notorious for putting off large-scale IT projects to the last minute. If you look at the EU's Markets in Financial Instruments Directive (MiFID) and other compliance initiatives, do you think that will repeat itself with OSI?

**George Tull, OnPoint Executions:**

I think that it has already. If the OCC is pushing back the dates then they are considering this already. It doesn't surprise me at this point. When I was dealing with the exchange system, there were many dates and many critical issues that were always pushed back.

**Waters:** Is it on the industry's radar now? Are they aware that this is coming or is there still an education process going on?

**Tull:** I believe that at the exchange level, all the exchanges have been following this closely or dealing with it in some way or another. If we look at Nasdaq's initial initiatives, they were deviating from the initial OCC plan. Currently, a lot of the member firms, the smaller brokerage firms executing for the larger institutions, and the institutions themselves are still trying to find their way in this topic.

**Archie Acharya, Infosys:** There is a sense of awareness and there are discussions. Most of them have realized that they need to act now, and there is an attempt to put a governance structure in place, as with the Y2K project. But this shift in dates that the OCC keeps coming up with is giving a false sense of security, as if there



Archie Acharya, Infosys, and Kevin McPartland, Tabb Group



From left: Archie Acharya, Infosys; Kevin McPartland, Tabb Group; Jim Leman, Westwater Corp.; George Tull, OnPoint Executions

is plenty of time to act. I think that could turn critical later on.

**Waters:** Is this going to require brand new hardware and software or are we just talking about small patches and fixes?

**Kevin McPartland, Tabb Group:** There is already a bit of a hardware and software upgrades going on in the options world just because of the messaging volumes. Everybody is already thinking about how they deal with this crazy amount of data. How do we mine the data? How do we process it in real time to make decisions? That is already going on.

A smart path would likely be to work this into those plans so you are not just adapting for volumes in the current world but adapting for volumes in the new world. From a buy-side perspective, I think they are looking to their brokers to deal with that for them in many cases. It is really going to be up to the brokers to make sure that they are ready, not just for symbology but for the growth and data volumes that are going to come with all the other market factors.

**Waters:** Do you foresee a brand new set of back office systems?

**Leman:** With heightened volatility comes more quotation mechanisms. The brokers going for more revenue are seeing this as an opportunity to set strategies with people on the buy side, and the trading volumes will continue to increase. The exchanges will continue to have an appetite to introduce new products. They will put pressure on adopting OSI and the buy side adopting it is going to keep the pressure up on moving forward and seeking more efficiencies. I would say there is going to be a push-and-

pull going on with this and it's not going to be completely transparent or considered a back-office issue.

**Waters:** Right now, firms are avoiding the "R" word, as in "recession." With tighter budgets and resources, could that have an impact on preparedness for this long-range mandate?

**Acharya:** It certainly is an issue. But the fact is that there is a lot of evangelizing that is going on in the firms today. That said, it has not reached the critical mass yet. Those firms realize that beyond this date, it is going to turn critical. Apart from OSI, there are other initiatives that firms are working on right now. There are a lot of things that are being juggled by firms, such as capacity and initiators, and these are all conflicting activities that are going on at the same time.

**McPartland:** It is a mandate, so they can't ignore it completely, but I think the cost and budget will lead to more procrastination and quite possibly could lead to cutting some corners. Rather than re-architecting the system or an entire database to deal with the new data structure, we could try to retrofit it in or put a square peg in a round hole, rather than making the hole square. That is something that happens probably more frequently than it should, and with cutting costs, it is going to even be more likely.

**Waters:** It sounds like the clock is ticking but it's not ticking very loudly just yet.

**Leman:** The hedge fund community is very important to the brokerage community. When you associate revenue with initiatives, it moves those initiatives a bit more to the head of the line. It is going to continue

to attract attention because it represents a revenue opportunity as well the operational necessity of trying to eliminate costs, exceptions and exposure. It's appealing to both ends of the expense revenue curves and it is not going to go away. It will probably trump other things that sound like they are important but may not have a direct revenue impact.

**Waters:** Is there a possibility that some financial entities will refuse to participate in the OSI?

**Tull:** Well, this is a regulatory mandate. At the end of the day, the meaning of this mandate is an issue of time, and they are already pushing back timelines at this point. In the industry as a whole, out of the 140 institutional customers that I have, not one of them has asked me about OSI. We feel it is our responsibility to provide that service to our clients and deal with it at our level at this point.

**Leman:** As with Y2K, people will make decisions not to rehabilitate a system but to go for a new one. People will decide not to clear options anymore but outsource it to someone else. You will get those kinds of decisions because people will make the economic decision. Are the margins shrinking? Do I want to do this myself or do I want to have someone else do it? Do I want to give up this system because it doesn't seem like it is really prepared enough for the future and I'm going to go to this newer thing? The same thing happened with Y2K, where certain systems lost favor and people moved to new systems. Some firms got onto service bureaus and some gave up clearing or changed their business model. They still stayed in the business to a degree but they

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got out of a part of it where there would be a lot of expense detracted.

**Waters:** What are the main challenges in the OSI directives? What are the significant impact areas?

**Acharya:** I would say the need to act now is at the top of the list. You have to realize that these are systems that were in place 25 years ago, so they are fairly mature systems. Software practices at that time were not as advanced as they are now, such as coupling or architectural niceties. All of these were not present in these systems. The design decisions that firms make in terms of Microsoft Excel spreadsheets, outsourcing or anything else, are challenges. This would probably be the right time for firms to brush off their processes because the last time it happened was during the Y2K project. Whether it is testing processes, software development, lifecycle processes, communication, change management, configuration management—all of these are going to be revisited. These are all challenges that will vary from firm to firm.

**Waters:** It sounds like communication is critical, not only inside the investment firms that have to deal with this problem, but also with customers and clients. Are there any committees or panels that are helping with the exchange of ideas and the setting of certain standards?

**Acharya:** The internal communication has begun. There are groups that are doing road shows that are

exchanging information packets and getting ready. I don't believe external communication has happened on such a large scale, but we will see evidence of that very soon.

**Waters:** Will the pace of the communication and the chatter increase as the weeks and months go by?

**Leman:** I think it will have to. I think it will be vendors talking to their customers to make sure that the customer knows that the vendors are going to be ready for it—again, so that the customer doesn't decide to go somewhere else. I think the industry organizations like FIX Protocol Ltd. (FPL), the International Securities Association (ISITC) and others are going to be talking about it because they will be prepared for it. People will read about it in the press. It is definitely going to pick up pace because the implementation will be getting closer and closer. Even the delay of dates will throw a certain amount of information in the air that people will pay attention to. So yes, it will increase.

**Waters:** Can you speak about the need for communication between clients and vendors and also the investment firms?

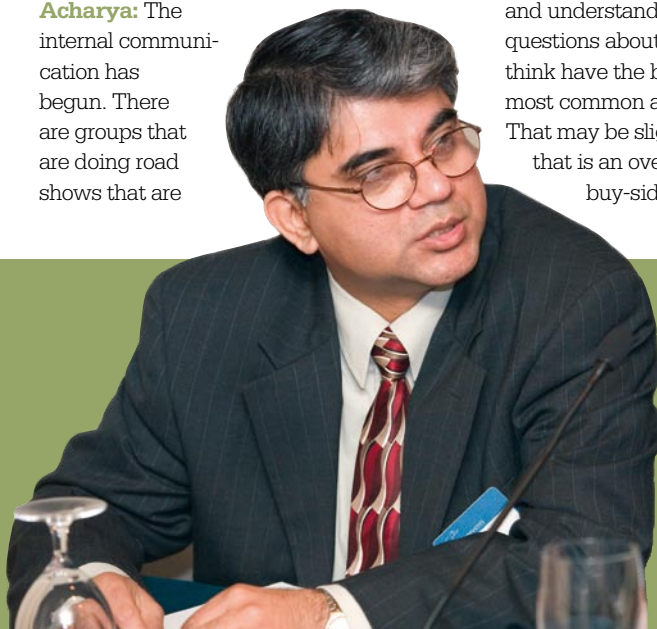
**McPartland:** It is critical. I spoke a few times about other growing areas in the options world like algorithms. That really falls on the broker-dealers to make sure that their clients understand what is going on and understand market structure. We ask questions about which exchanges they think have the best market structure and the most common answer was, "I have no idea." That may be slightly different, but I think that is an overall theme in that a lot of the buy-side asset managers and hedge

funds don't understand the intricacies of the options market. This is a good case in point, and education is going to be important. And the broker-dealers that are going to be interacting with these buy-side traders daily are the ones that are best positioned to help pass that information along.

**Waters:** OSI-scripted industry testing is expected to be a huge effort in this space right now. What will you recommend to financial institutions as the right approach to that?

**Acharya:** I want to step back and say that the scripted industry testing is just one aspect of the testing. The OCC prescribed two phases: the first phase is really the internal testing and going by the previous dates, it is from July to December. This phase is format validations. As long as it matches the format, you are fine. They are not going to look at the content within the format. The second phase has about four or five sub-phases, which start from a throughput testing, and then there is beta script testing for limited participants. Then there is the implementation date testing and there is post-implementation date testing. Again, all these are guidelines and firms are expected to take cues from these dates. Firms are expected to be connected to the test environment and external test strategy of the OCC.

But, there is much more; that is just the tip of the iceberg. There is a lot that is going to happen beneath the surface within your firms, such as internal testing, system testing, the test environment, the dedicated test environment and a dedicated governance strategy. So there are a lot of things that will go on even before you get connected to the scripted industry testing.



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*Archie Acharya, Infosys*



Kevin McPartland, Tabb Group, and Jim Leman, Westwater Corp.

The dates are just a guidepost. These are guidelines and there will be some scenario details that will circulate in time. But once you get those scenarios you will have to have your own system test plans and then start testing your internal systems.

## THE AUDIENCE QUESTIONS

**Audience Member:** The first initiative we have been addressing is a change in the symbology standards for the underlying equity symbols. As we understood it, those were going to change originally in a couple of weeks and now are put off until September, which will allow more than alphabet symbols. You can have symbols like a tilde as part of the underlying symbol. Is that still on that schedule or has that slipped too?

**Tull:** I believe what you are talking about is what Nasdaq has identified as some of their changes to some of their symbology methodology. As far as I know, that issue is up in the air at this point.

**Audience Member No. 2:** Yes, there will be an announcement coming out from Nasdaq soon and that plan is being dropped. So the whole symbology of special characters is going to be dropped. They are going to work with the industry on a common symbology.

**Waters:** On that point, is there still a lack of set standards that still have to be hashed out?

**Leman:** It would appear so. We've been monitoring some of the committee meetings and I think there are some things

still up in the air. I don't know that it is completely ironed out yet.

**Waters:** What impact does that have inside an investment firm? Not only are they pushing back deadlines, but if there isn't a set speed limit, how can you know if you are breaking the law?

**Leman:** I think they have just recently put out the test symbology that will be used for testing systems. They may have a bit more time, but they do need to come to a conclusive end about how they want to do it and it doesn't appear that they have done it just yet. But they are going to issue symbology; in fact, I think it came out in the last meeting that there are test symbols that will be used for the range of testing that will have to be conducted.

**Audience Member No. 3:** I am from Bank of America. This question is more from a front-office trading perspective. I understand that there is going to be a symbology or graphical user interface (GUI) display change on the screen, but is the auto entry also going to change? Will traders have to put in the date now to pull up

electronic contracts, whereas earlier they didn't have to do that? For example, today a trader might put in Apple June 5 call 50. But going forward, they might have to put in Apple June 15 2005 call 50. Wouldn't that be a change from the buy-side client entry as well?

**McPartland:** I think that is logic that can probably still be built into the order management system (OMS) or the execution management system (EMS). A lot of that can be masked. That's why I said the buy-side probably won't care. I think a lot of that can probably be masked to the trader, where the order entry won't change. An exception could be someone like Bloomberg, where they are actually typing in the Options Price Reporting Authority (OPRA) codes, rather than filling in data fields. Otherwise, I think that logic can still be embedded into the system to understand exactly what the calendar date of the expiration would be based on the month.

**Leman:** You could still have either a slang table or pull-down menu. That is really not trivial but it is something that could be introduced so the person doesn't have to know the entire string. But it will still be represented to them to look at to make sure it is right.

**Acharya:** Just as a follow-up on that question. For example, if there were two contracts in the month of January, there would be two different dates, right? So in that case, it might become mandated for the



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Erin Collins, Options Clearing Corp.



trader to put in the date as well to pull up part of the contract.

**Waters:** Have the OMS vendors already begun refreshing their OMS offerings?

**Leman:** Some of the OMS vendors had options to begin with and some of them didn't have options at all. I think they are going to bend to pressure from their customers as to what they do. I would say they are probably all examining it now and breathing a sigh of relief when this other delay of dates goes in. But they are very much driven by their clients' demands.

**Waters:** Do you think investment firms will outsource this migraine?

**Acharya:** It's possible. It's possible that people might find it easier to outsource this headache in the short-term. That is a possibility.

**Audience Member No. 4:** I am from Citigroup. Correct me if I'm wrong, but all the market data vendors are still going to use the OPRA code, which will be 17 characters. There was a large outcry about why OPRA coding and OCC are still different. Why not have the generic symbology?

**Tull:** From my point of view, there has always been contention from all the self-regulatory organizations (SROs) out there,

especially regarding the options industry as a whole. That is true: OPRA is looking at only using their OPRA codes for the dissemination of data. When we looked at the impact analysis on OnPoint and our technology infrastructure, we identified four key areas that will have to be addressed. One is on the user interface for our proprietary order management application. The second piece is in our market data and order routing, both on the interface side, in back-office handling and through the different application structures. The last part was on comparison.

**Audience Member No. 5:** I am with Bank of New York. Is there a plan to let the existing five-character approach peacefully coexist with the new one?

**Leman:** I think at least up to this point, the committee says it is all-or-nothing on that one. The OCC will continue to put out data both ways until that date and then they stop.

**McPartland:** The historical data can always stay in the old format. That will be, at some level at least, a coexistence that will have to be maintained for probably a couple of years.

**Leman:** Yes. If you are looking at quantitative data and you have models going back,

will you go back and change that data, or will you live with two worlds? Will you live with the new data and the old data? But I think in terms of publishing new data that is the date on which it stops.

## THE OCC SPEAKS

**Erin Collins, Options Clearing Corp.:**

I don't really have a question but a follow-up comment. As to the question about the volumes for the market data and extra 13 characters on the OPRA code, OPRA already supports the extra 13. They are not actually adding 13 new elements to their feed. That is one of the reasons why it is a little bit different than "there are 17." They are trying to keep the amount of data that they are pushing around on each message within the current frame of what already goes out. I don't know if it is a different way that you are going about receiving the data, but it is already something that you take in on the OPRA feeds today. I don't know that it should increase the volume or the traffic that you are seeing, as they are not adding 13 extra.

**Waters:** Would the panel care to comment?

**Tull:** I think this has to deal with the OPRA code on the market data feed. The key identifier, which is really going to be apparent in the OCC and the OPRA feed and how they interoperate, is really

going to be do I point to in order to create this transmission of this logic? What am I locking onto? What is my key identifier? Today, in the OPRA feed, everybody uses the key identifier OPRA code. If they look at pointing at the new explicit strike series or the OCC-recommended symbology, then those characters will be added into the message format and then will impact the feed capacity. Currently, if OPRA follows that mandate where they are only going to use the OPRA code itself, it wouldn't be because it is really just part of the extraneous data within that message.

**Collins:** Right. It's more about how you go about looking at the data and what you're pulling back and about whatever symbol you are sending out. For the most part, everybody is almost there and sending out all the data that we need today to be explicit symbology. It is more about how you get it and what you use to receive than what you are all pushing around.

**McPartland:** I guess it comes down to moving the data around internally. A lot of them were probably just five bites and the database codes are probably five bites. If that starts to expand then storage capacity and internal messaging might start to get

hammered a little bit from that increase.

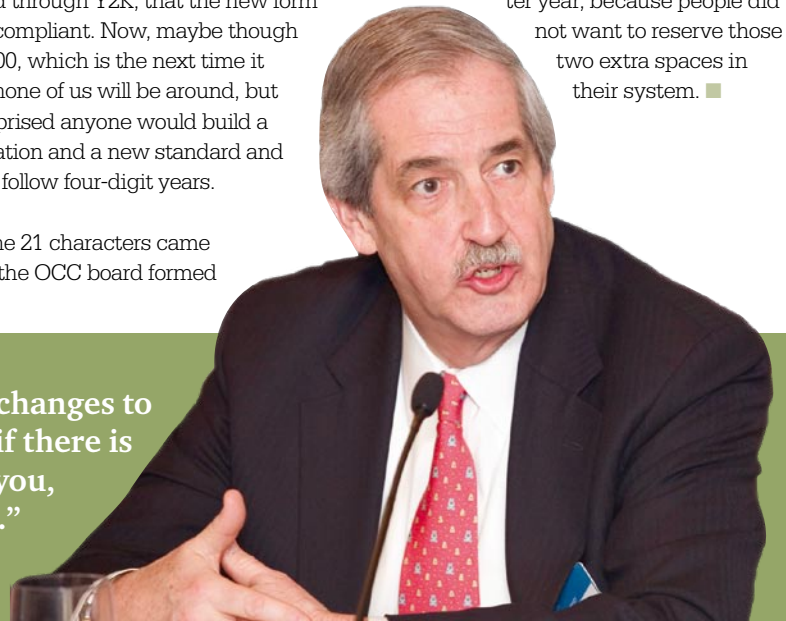
**Acharya:** But there is another angle here. For the duration that testing is going to continue, firms will have to have a dedicated environment. Right now there are a lot of things that are juggled and initiatives come and go, so you have storage, an environment that is used for a short period of time and then released. However, if this is going to go on for six to nine months, you are going to have that environment locked up, because it is going to be a sandbox for your firm. Does this mean it will translate into additional capital expenditure for hardware? Most likely yes. So that is a cost and I don't know whether firms have figured out yet.

**Audience Member No. 6:** I'm from The Bank of New York. This is more of an observation than a question. I'm surprised, having lived through Y2K, that the new form is not Y2K-compliant. Now, maybe though the year 2100, which is the next time it comes up, none of us will be around, but I'm just surprised anyone would build a new application and a new standard and not make it follow four-digit years.

**Collins:** The 21 characters came about after the OCC board formed

this symbology committee and was asked by the board, which is a compilation of the exchanges and clearing members, to address this issue. When they went about figuring out what the new key was, there was a whole period of conversation about what is the right kind of information to pass around. They talked about having a four-character year and it came down to issues like the market data vendors and people trying to limit their systems.

When you look at the 21 characters, it is actually the minimum representation that is recommended for use. From an OCC standpoint, we already push everything into a four-character year, so we will have a four-character year on all of our uplink data. It is up to each entity that looks at implementing this as to whether they want to exceed those minimum requirements. They couldn't get consensus on the four-character year, because people did not want to reserve those two extra spaces in their system. ■



“There was a lot of pressure by the exchanges to get this done inside the industry, but if there is not a regulator bearing down on you, the possibility of slippage exists.”

*James Leman, Westwater Corp.*

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