
The Curious Story of How CUSIP Numbers Became a Wall Street Battleground.

CUSIP numbers are like a Dewey Decimal System for stocks and bonds. They're also a source of illegal monopoly power, according to investor lawsuits.

They may not be the most exciting part of the securities markets, but CUSIP numbers are indispensable.

The arcane nine-digit ID numbers, issued by the Committee on Uniform Securities Identification Procedures, show up on everything from stocks, bonds, exchange-traded securities and mutual funds. They're also not free. In at least two class-action lawsuits, investors are alleging that the cost of CUSIPs has been artificially inflated for decades, as a result of monopolistic control by data providers including the American Bankers Association, FactSet and S&P Global.

Investors, who are seeking injunctions and damages, allege the CUSIP system's owners and exclusive licensees aggressively sought to dampen competition from other services offering free or lower-cost alternatives.

"The motive for their exclusion of competition is simple," says one of the complaints filed recently in Manhattan federal court, "CUSIPs are worthless except for the fact that they are the standard."

How the CUSIP system began

CUSIPs have been standard since the 1960s for identifying securities for clearing and settlement of trades. The system is owned by the ABA and a subsidiary of S&P's Global Market Intelligence, now called Factset Research Systems, which completed its purchase of the business from S&P this month for $1.925 billion.

The numbering system was originally a subscription service that provided physical books containing information on every financial instrument linked to a CUSIP and were updated quarterly or annually. But in the 1980s, vendors like Bloomberg began distributing the data directly and electronically to financial institutions, making it unnecessary to pay a fee to S&P.

To counter the loss of revenue, S&P changed its business model from a subscription service to a licensing one, and required financial firms using CUSIPs to pay substantial fees. S&P inserted language in its contracts with data vendors requiring them to cut off access to the CUSIPs for any financial institution that did not enter into a license agreement with S&P.

At about the same time, according to the lawsuits, ABA and S&P became more aggressive in trying to maintain their stranglehold on the system.

"Monopolies are rarely good for business," said Ronald J. Aranoff, a partner in the Litigation & Dispute Resolution Group at Wollmuth Maher & Deutsch LLC, which represents plaintiff Hildene Capital Management. "We trust the court to decide whether the exercise of monopoly power here was unlawful. We believe it is."

Flexing monopoly power

CUSIP was designated as a financial standard by a committee of the American National Standards Institute (ANSI), dubbed X9. But X9 is hardly an independent body, at least according to the class action suits. The ABA established X9 during the 1970s and it, as well as S&P's CUSIP Global Services, are still connected to X9 through voting positions on the committee's board of directors.

Hildene is an institutional asset manager headquartered in Stamford, Conn. Like all other investment managers and traders, it requires access to financial information for managing, monitoring, buying, and selling financial instruments. The company typically pays Bloomberg for access to data that includes CUSIP numbers. For Hildene, the cost of getting the data with CUSIP numbers ends up being about $10,500 a year.

"Hildene…[is] then left with two unenviable options: pay S&P's supracompetitive subscription rates or have CUSIP numbers stripped from their data feed and suffer, at a minimum, significant disruption to their businesses," the lawsuit states.

Hildene once balked at paying the licensing fees, and was sent "a series of increasingly hostile letters" and threats that it must pay the fee or face a debilitating lock out from access to CUSIP numbers, according to the suit. With no alternative, Hildene eventually signed the subscription agreement.

Making money by owning CUSIPs

The CUSIP owners generate revenue in at least three ways. First, S&P, now Factset, charges securities issuers a fee, typically about $280 per CUSIP number, to obtain CUSIP numbers for its securities. Second, S&P charges data providers, like Bloomberg, licensing fees for using CUSIPs in its databases. Third, and more recently, S&P demands that end users, like Hildene, enter their own subscription agreements with S&P under the threat of having the numbers stripped from their data feeds.

"Defendants have a clear interest in requiring that all data users use only the CUSIP identifier system," according to the suit. "That is because…the ABA retains 30% of CGS's licensing fees from all data users and the remainder is kept by S&P."

An earlier class-action complaint by Dinosaur Financial Group LLC further alleges that ABA and S&P are violating copyright laws, on the premise that ID numbers like CUSIP numbers can't be protected by copyrights.

"A CUSIP is a number that has been known to humanity literally for millennia," the complaint says. "Mathematicians, scientists, teachers, and financial markets' participants use numbers every day that happen to coincide with CUSIP numbers. Yet, defendants assert that the ABA has copyrighted those numbers and therefore can control the use of those numbers. That assertion is legally baseless."

Attempts to reach the ABA and S&P for comment about the suits were unsuccessful.

Past antitrust complaints

Complaints about the CUSIP system and allegations that it unfairly restrains competition have surfaced multiple times throughout its history.

In November 2009, the European Commission accused S&P of abusing its position as the sole provider of ISIN codes – the international version of the CUSIP – by requiring European financial firms and data vendors to pay licensing fees for their use. The European Commission noted that there are no acceptable alternatives for traders and financial institutions.

Although it disagreed with the commission's findings, S&P offered to create a lower-cost alternative feed of certain ISINs for market participants in Europe.

The Center for Municipal Finance, a U.S.-based nonprofit dedicated to improving the municipal bond market, has come out in support of a free alternative to CUSIPs, developed by Bloomberg, called Financial Instrument Global Identifiers. It's unclear however, whether the FIGI will gain traction in the market because it is not recognized as an industry standard.

"CUSIP is not the United States' financial instruments identifier standard because of any special technology or knowledge by S&P or ABA," Hildene said in its complaint. "After all, a CUSIP is just a string of numbers and letters. S&P is not uniquely capable of issuing and maintaining alphanumeric strings."

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