WEALTH MANAGER

Regtech: still much to learn about how it can help

By **Selin Bucak** / 08 Dec, 2016

Regulatory technology (regtech) is being touted as a way for financial institutions to ensure they comply with upcoming rule changes, but there is a danger its development could stall as the industry enters a Mexican stand-off with the Financial Conduct Authority (FCA).

Greater use of technology is expected to help firms get ready for Mifid II, while also driving down costs and embedding good conduct into how a firm operates.

Jonathan Hammond, managing consultant and technology practice lead at Knadel, is concerned that an impasse is emerging

between the regulator and financial services software providers however, with both looking to the other to take the lead.

‘The FCA has been encouraging, but the participants in this are looking to the regulator for a bit more direction, which to date it has been particularly light on providing,’ he said.

‘Everyone’s looking to the regulator to provide solutions of its own. I think the regulator’s intentions are good but so far it has been looking to the industry and the industry is looking to them.’

Regtech, which has been heralded by Deloitte as the ‘new fintech’, is itself still in its infancy. While the FCA is trying to drive innovation through its sandbox initiative and ‘hackathons’, there is still much to learn about how regtech can help the industry.

Culture change and compliance

Technological advances and cultural change go hand-in-hand, with corporate culture dictating how a firm operates and views compliance.

According to Adrian Shedden, senior associate at Burges Salmon, the industry may face a challenge in bridging the current gap between operations and services, however.

Speaking at a roundtable organised by The Realization Group, he said: ‘We have

something that is quite human, based around the customer. Acting in the customer's best interest, where each customer has very different needs and wants, and on the other side, large financial institutions that have become successful by focusing on the product, making processes uniform and, to an extent, disassociating from the customer. The conundrum is how to mesh those two together.'

Shedden said the individuals at companies in charge of implementing the changes required by Mifid II and other regulations, such as the European Market Infrastructure Regulation (Emir), are driven by fear of falling foul of the rules, rather than what will benefit the end client.

He believes the incentives are the wrong way around.

'The challenge financial institutions face is meshing those two together and building from the bottom up with the customer at the heart of it. Of course, in light of the immense regulatory burden given the siloed nature and legacy infrastructure, with a patchwork of fixes, there has to be compromise,' he said.

'The way to get past that is have a culture where you take some of the more innovative design-led ideas to inform the culture of designing solutions. You don't necessarily need to do it in-house. There are firms that are actively doing those

solutions.'

The siloing approach taken by the industry has meant customers have been treated on a product by product basis, according to what they buy, Shedden says. He advocates a more joined up approach to ensure clients' needs are met, and said this was already becoming more common.

'This is what start-ups are doing in focused ways and it's up to financial services incumbents whether they follow suit,' he added.

'I understand it's difficult to get to that place after decades of being driven by products. Culture is about incentives – you are incentivising the salesforce to maximise the sales of a particular product rather than the specific outcome for a customer. Within financial institutions you have an inherent conflict and that requires a substantial overhaul.'

Identifying conduct risk

Apart from cultural issues, companies also face conduct risk – one of the main problems the Senior Managers Regime has been designed to address. Through more efficient data collection and automation there may be ways that regulatory technology can actually help compliance teams identify conduct risk.

Banks and large financial institutions have to put in place processes and technology that records all transactions

and reports this to the regulator in a timely and easily digested way, according to Mike O'Hara, partner at The Realization Group.

In a research paper, 'New Initiatives in Compliance Technology', O'Hara pointed out that after series of financial scandals, compliance teams are now aware that audit trails need to span 'multiple desks, offices and systems'.

This means firms are looking to replace existing practices, which are expensive and prone to error, with 'scalable, highly automated solutions that not only capture a wide variety of inputs across communications and other IT platforms, but also allow indexing, storage and retrieval of the required information in accordance with regulatory mandates'.

These changes can be beneficial for companies in the long term, especially when it comes to issues of culture and conduct.

He added: 'While the primary driver might be regulatory, the up-front investment required to achieve compliance can also yield long-term benefits, by helping to identify at an early stage behaviour patterns that might otherwise lead to conduct risk.'