Cost of Compliance 2019: 10 years of regulatory change

By Stacey English and Susannah Hammond

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With thanks to Chloe Bloomfield, Helen Camfield and James Douse

Executive summary

Thomson Reuters Regulatory Intelligence has carried out its annual survey on the cost of compliance. This year marks the 10th anniversary of the survey, which looks at the challenges financial services firms expect to face in the year ahead. Almost 900 senior compliance practitioners worldwide took part this year, representing global systemically important financial institutions (G-SIFIs), banks, insurers, broker-dealers and asset managers. As with previous years, the report builds on data from prior years' research and, where relevant, highlights year-on-year and regional trends.

The cost of compliance report has become the trusted voice for risk and compliance practitioners around the world. Over the lifetime of the report, there have been almost 6,000 participants and over 40,000 downloads of the report by financial services firms, G-SIFIs, regulators, law firms, domestic governments and consultancies. The unparalleled interaction with the global financial services industry and the frank and wide-ranging concerns and issues shared by practitioners continues to bring unique insight into the practical reality and challenges faced.

Thomson Reuters extends its profound thanks to all respondents along with a continued assurance that the responses, so generously shared, will remain confidential. The report findings seek to help financial services firms with planning and resourcing, while allowing them to benchmark their own approach and practices to determine whether their strategy and expectations are in line with the wider industry. The experiences of G-SIFIs are analysed where these can provide a sense of the stance taken by the world's largest financial services firms.

The questions asked have remained largely consistent to enable year-on-year comparison. However, we are acutely aware of how the role of compliance of officers has changed over the 10 years of this research. We have therefore paid extensive attention to the open-ended responses in determining the context and wider aspects of compliance. Uniquely, this year's survey also asked respondents for their view of the next ten years. While firms deal with regulatory uncertainty and the impact of technology, there is an emerging sense that they have recognised the need for risk and compliance officers to

have an increasingly enhanced role within the business to have the best chance of thriving into the medium term.

The main points to note are:

- **Compliance challenges –** Regulatory change remains the single biggest challenge for compliance officers in the year ahead. Other challenges identified have flexed year-on-year. For 2019, the increasing regulatory burden, financial crime, AML and sanctions compliance, together with culture & conduct risk and the adequacy and availability of skilled resources, were all raised as challenges. In contrast, for 2018, data privacy and the General Data Protection Regulation together with enhanced monitoring and reporting requirements were highlighted in addition to continuing regulatory change.

- **Budgets –** Compliance budgets are expected to continue to rise. There has been year-on-year consistency in the percentage of firms who expect to have more budget available: 63% in 2019, compared to 61% in 2018. The budget changes sit alongside 65% of respondents reporting an expectation that the cost of senior compliance staff will rise in 2019.

- **Compliance teams –** Growth in compliance teams is slowing. Approximately one third (31%) of G-SIFIs expect the size of their compliance teams to grow in 2019 (38% all firms), with 58% of G-SIFIs expecting team size to remain the same (59% all firms). G-SIFIs are an outlier, with 11% expecting their compliance team to shrink in 2019 (3% all firms).

- **Regulatory change -** The majority of firms expect more regulatory activity in 2019. 71% of firms expect the amount of regulatory information published by regulators and exchanges to increase over the next 12 months (43% slightly more, 28% significantly more). The percentage of firms who had expected the amount of regulatory information published by regulators and exchanges to increase had fallen year-on-year between 2011 (83%) and 2017 (62%). In parallel, an increasing number of firms are expecting more liaison with regulators (53% in 2017, 58% in 2018, rising to 71% in 2019) with the top three drivers for the expected increase being information requests from regulators, the need to understand changing regulatory expectations and more onerous regulatory and reporting requirements.

- **Personal liability –** Personal liability continues to rise. There has been a steady year-on-year increase between 2017 (48%) and 2019 (60%) in the percentage of firms who expect the personal liability of compliance professionals to increase. Overall, this has increased from 2014 (53% more), to 2019 (60% more). Personal liability is also on the rise for G-SIFIs. In 2015, 64% of G-SIFIs expected personal liability of compliance professionals to increase, compared to 74% in 2019.

- **Board challenges –** Broadly in line with compliance expectations, the biggest challenges seen to be facing boards of directors in the coming year are keeping up with regulatory change, cyber resilience, personal accountability, and culture and conduct risk. In contrast, in the prior year the main challenges were seen as continuing regulatory change and the intensity of supervisory scrutiny.

- **Outsourcing -** Firms who outsource all or part of their compliance function has remained consistent, ranging between 24% and 28% year-on-year since 2016. Over a third (36%) of G-SIFIs now outsource at least part of their compliance function. This is highest rate since 2016 when the question was introduced to the survey. Reasons for outsourcing included cost (53%) and need for additional assurance on compliance processes (41%).

- **Predictions over the next 10 years –** The expected compliance changes for the next 10 years are myriad. The most widely anticipated were cited as the automation of compliance activities, continuing regulatory change, an enhanced role for compliance within the business, the 'new normal' of culture and conduct risk expectations and the rise of technology risk.

INTRODUCTION AND RESULTS

Thomson Reuters Regulatory Intelligence (TRRI) conducted its 10th annual cost of compliance survey in Q4 2018. Almost 900 responses were received from risk and compliance practitioners worldwide, including Asia-Pacific, the Americas, UK and Europe, the Middle East and Africa, representing firms across all sectors and sizes of the financial services industry including banking, insurance, broker-dealers and asset management.

> "To be clear, it is not the supervisors' job to dictate the internal culture of a firm, but when there are market failures such as externalities or information asymmetries, then there is a role for the official sector to push firms to do more to address these issues and mitigate misconduct risk."
>
> Kevin J. Stiroh, Executive Vice President at the Federal Reserve Bank of New York. Remarks at the 4th Annual Culture and Conduct Forum for the Financial Services Industry, London (October 2018).

Since the financial crisis, financial services firms have seen unprecedented levels of regulatory change as governments and policymakers have sought to ensure that a similar global downturn could not happen again. The first cost of compliance survey report was published when the global financial crisis was at its height and it has tracked the changing role, remit, challenges as well as the cost of compliance ever since. TRRI has grown and adapted, alongside the financial services industry it has, and continues to, serve. Over the lifetime of the report, TRRI's coverage has grown year on year and now tracks over 1,000 regulatory bodies worldwide, publishing over 220 developments every day.

Ten years ago, there was an understandable focus on financial stability and, in policy terms, that led to the creation of the Financial Stability Board (FSB) as a successor to the Financial Stability Forum. The FSB which operates under the aegis of the G20 is the supranational policy maker working with (among others) each of the major sectoral policy makers - the Basel Committee on Banking Supervision (BCBS), the International Organisation of Securities Commissioners (IOSCO) and the International Association of Insurance Supervisors (IAIS). It is to the FSB that risk and compliance officers now look as the original source for much of the regulatory change continuing to be introduced around the world.

While balance sheets have been rebuilt and the rulebooks have fundamentally changed, it remains to be seen whether the changes imposed limit the potential for major global economic harm. For compliance officers, the last 10 years have also been a time of unprecedented change. Not only have they had to cope with the challenges presented by the sheer volume and complexity of regulatory change, but in that time their remit has substantially morphed and changed. The responses to the cost of compliance survey have tracked and measured the changing remit and the concerns of compliance officers. Indeed, the free-text comments so generously shared with TRRI have been an invaluable source of information enabling the continuing analysis of current and potential future concerns.

Where pertinent, free-text comments have been included (with permission) as direct quotes from compliance practitioners to highlight and illustrate particular points.

The TRRI annual cost of compliance report is the acknowledged voice of the industry. This report is, and has been, TRRI's most requested and downloaded report. Given the richness of the data set gathered over a decade TRRI has, where useful in this edition of the report, highlighted the changes over multiple years enabling a longer-term perspective of numerous risk and compliance issues. The graphics in the report are variable, multi-year to best show the year-on-year trends.

There are three key areas where the role and expectations on the compliance function have changed out of all recognition in the last 10 years:

- Culture and conduct risk
- Personal liability
- Technology

The inclusion of culture and conduct risk in the stated regulatory expectations around the world has become the new normal with financial services investing heavily to tackle the 'how' as well as the 'what' with regards to substantive issues such as firm culture, sales practices and how best to consistently demonstrate the required good customer outcomes. Over the last few years, culture and conduct risk issues are no longer being considered as a separate and distinct area of risk and compliance, but rather have moved much closer to being seen as inherent in the business - and treated as such.

Indeed, the capacity to be able to demonstrate a strong positive culture in action, as well as the ability to mitigate any conduct risks arising, has become a required core competency for firms and their compliance officers with all of the challenges associated with a qualitative, rather than a quantitative, issue.

On personal liability, there has been an inexorable rise in the implementation of accountability regimes around the world.

Substantive regimes have been introduced in Australia, Hong Kong and the UK, with Ireland and Singapore in the planning or consultation stages. As with so many aspects of regulation, the compliance function may well take the lead in determining how best to identify, manage and mitigate the rise of personal liability in financial services firms with the added complexity of having to accommodate evolving culture and conduct risk expectations.

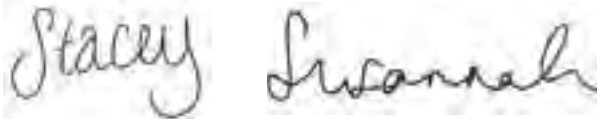
It is perhaps with technology that the greatest change has been seen over the last ten years in terms of remit, expectations and terminology. In 2019, fintech, regtech, insurtech, suptech and bigtech are all common currency alongside all things cyber. Risk and compliance functions have had to consider and deal with substantive issues before firms can begin to realise the potential benefits offered by technological innovation.

The successful deployment of technology and the ability to automate future compliance activities is seen as one of the greatest potential innovations for the next ten years in compliance. While there will be numerous challenges to overcome, there are huge possible benefits to firms and their customers alike from solutions deployed successfully on a secure IT infrastructure by highly skilled in-house specialists. Much of the benefit is focused on process with the potential to automate with increased accuracy and speed. The endgame being smoother, efficient operations enabling risk and compliance functions to focus on more 'value-add' matters.

A word about assessing the monetary 'cost' of compliance. The 10 years of the cost of compliance survey has shown it is extremely difficult for firms to isolate out the monetary costs associated with compliance alone. One complication is the definition of what precisely is included in 'compliance' - one firm's compliance is another's quality control or regulatory risk. Another complication is the assumption that spending on compliance activities is something that firms would not do unless required to by a rulebook. The line between what a firm would spend to remain in business, treat its customers well and act prudently and what it spends simply to be compliant with a rulebook is often blurred and often non-existent. Estimates for spending on compliance make great headlines but they should be treated with a degree of caution. Non-compliant firms will find the enforcement action (both corporate and personal) substantially more expensive, in all senses, compared to investing in compliant activities in the first instance.

The challenges in isolating out the monetary spend on compliance activities and solutions has not stopped firms from working on the problem. One recent report from KPMG expects that regtech will make up 34% of all regulatory spending by 2020, with a forecast regtech spend of US$ 76bn, up from US$10.6bn in 2017. The same report also estimates that firms' annual compliance spend is US$270bn.[1]

We hope the findings from this 10-year special report on the cost of compliance are useful in developing and benchmarking your firm's approach and practices.



Stacey & Susannah

1 https://assets.kpmg/content/dam/kpmg/uk/pdf/2018/09/regtech-revolution-coming.pdf

BUDGET AND SKILLED RESOURCES

"As digitalization and automation become more prevalent in the financial industry, our people will be affected as jobs evolve. There is a need to place emphasis on people and skills. The extent to which businesses can capture productivity gains depends on how quickly the workforce is equipped with new skills to leverage technology to perform new tasks or roles."

Indranee Rajah, Minister in the Prime Minister's Office Singapore, Second Minister for Finance and Education. Speech, "Window To The Past, Portal To The Future", at Standard Chartered Bank's 160th Anniversary Celebration Dinner (February 2019).

What is the biggest change you predict for compliance in the next 10 years?

"...As compliance controls and monitoring becomes more automated, I believe we will see a shift in the skill sets required for compliance personnel. They will need to become not only proficient in the regulations, but have a strong data analytics base as well. In addition, as the big firms continue to build out globally, compliance experts need to know cross jurisdictional compliance issues and have expertise in more than one area."

Head of Compliance, Investment Bank, United States
Survey respondent, Thomson Reuters Regulatory Intelligence – Cost of Compliance 2019.

Budgets and the skilled resources available to compliance functions are intertwined. Risk and compliance function must have access to appropriate expert and skilled resources, preferably in-house, to enable the identification, management and mitigation of any and all risks arising. Key among the skill sets required for now and the future is that of data science and technology. Budgets are not infinite and firms need to invest, and invest wisely, in suitably deployed technology to improve the efficiency and effectiveness of the compliance function and its activities.

Examples of compliance-related costs taken from firms' annual reports

"...as part of our restructuring program, we have invested significantly in upgrading our compliance and control frameworks. We increased our headcount in compliance by over 40% over the last three years. We also completed a significant review of over 30,000 legacy clients and over 10,000 control issues and improvements were implemented across the Group. We used cutting edge technology, as previously mentioned, to move from 12 legacy platforms to one strategic platform."

Credit Suisse Group AG, Annual Report 2018

"We continue to invest heavily in our detection capabilities and core systems as part of our financial crime prevention program. We are exploring new technologies to combat financial crime, and implementing rule-based monitoring by applying self-learning systems to identify suspicious transactions."

UBS Group AG, Annual Report 2018

"...increased and ongoing compliance requirements and uncertainties have resulted in higher costs for Citi. For example, Citi employed roughly 30,000 risk, regulatory and compliance staff as of year-end 2018, out of a total employee population of 204,000, compared to approximately 14,000 as of year-end 2008 with a total employee population of 323,000. These higher regulatory and compliance costs can impede Citi's ongoing, business-as-usual cost reduction efforts, and can also require management to reallocate resources, including potentially away from ongoing business investment initiatives..."

Citigroup Inc., Annual Report 2018

"Operating expenses in the period under review came to €6,879m, only a slight increase on the prior-year period. The increase was primarily owing to sustained investment in digitalisation and growth, and also due to increased costs for regulatory projects and levies, such as the Deposit Protection Fund and the Polish banking tax."

Commerzbank, Annual Report 2018

"Since 2016, we have invested approximately €700 million in upgrading our key control functions. These investments have enabled us to improve across the spectrum of prevention, detection and investigation. We are running more automated processes with improved transaction filtering and client review capabilities. And, beyond our investments, we have also significantly reduced our presence in high risk countries, products and client groups. We believe that our control spending will peak in 2019 and we can then begin to use technology to extract savings."

James von Moltke, Chief Finance Officer, Deutsche Bank AG Q4 2018 Analyst Conference Call

The greatest compliance challenge(s) I expect to face in 2019 is/are...

"...Volume of oversight needed will increase, but due to the size of the firm budgetary constraints could keep us from obtaining the technologies needed to provide the most efficient compliance oversight."

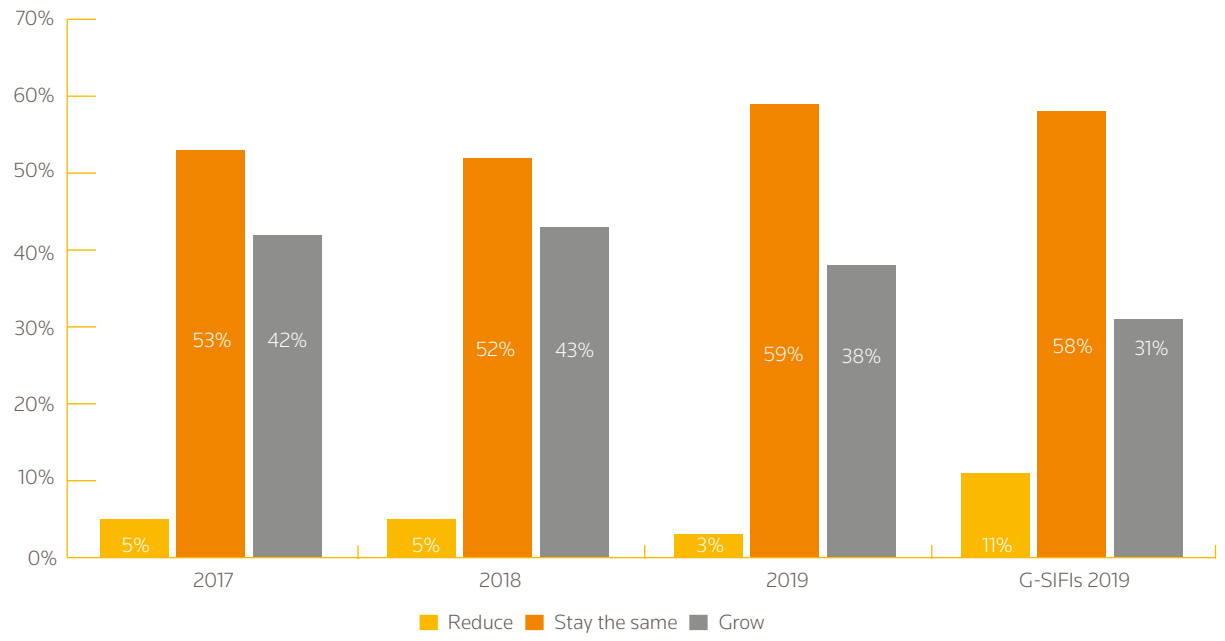
Compliance Director, US Law Firm
Survey respondent, Thomson Reuters Regulatory Intelligence – Cost of Compliance 2019.

The size of a compliance team isn't necessarily a robust indicator of sufficient investment in the compliance function but the expectation of how the compliance team size is likely to change over the coming year highlights the likely investment and budget trend. For 2019, more than half (59%) of respondents expected the size of their compliance team to remain the same year-on-year, with over a third (38%) expecting their compliance team to grow. Those expecting the size of their compliance team to grow in the coming year has stayed relatively static (42% in 2017, 43% in 2018 and 38% in 2019).

For the G-SIFI population, often seen to be a leading indicator for the rest of the industry, 31% expected the size of the compliance team to grow in the next twelve months. In contrast, 11% expected the team size to reduce which may be as a result of the conclusion of big set piece regulatory implementation projections such as that for MiFID II/MIFIR.

There were some regional variations in the results with, for instance, two thirds (64%) of firms in North America expecting compliance team sizes to remain the same in 2019.

Over the next 12 months I expect the size of my compliance team to...

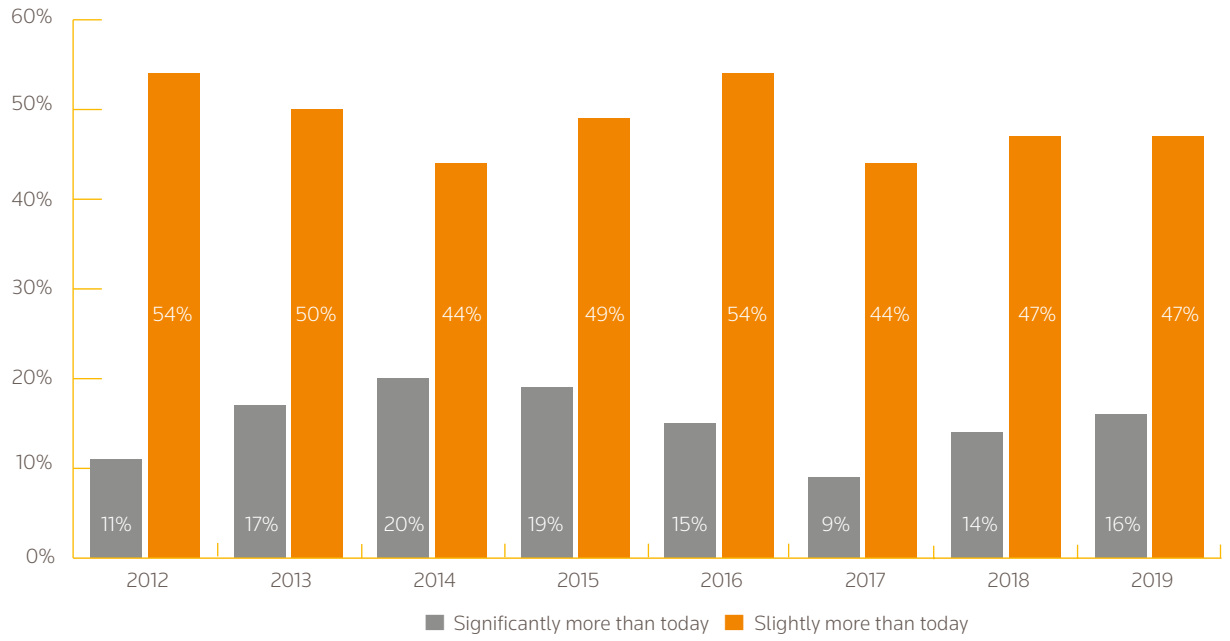


Source: Thomson Reuters Regulatory Intelligence – Cost of Compliance 2019: 10 years of regulatory change, by Stacey English and Susannah Hammond.

Compliance budgets are expected to continue growing. Over time those expecting their compliance budget to grow has remained reasonably consistent. In recent years there has been a steady uptick in those expecting a significant increase in the total compliance team budget from 9% in 2017, 14% in 2018 to 16% in 2019.

Regionally, expectations are highest in Australasia where 75% of firms expect compliance team budgets to increase over the next 12 months, which is likely to be driven at least in part by the widespread changes recommended in the conclusions from the Hayne report and the Royal Commission in Australia.

Over the next 12 months, I expect the total compliance team budget to be...

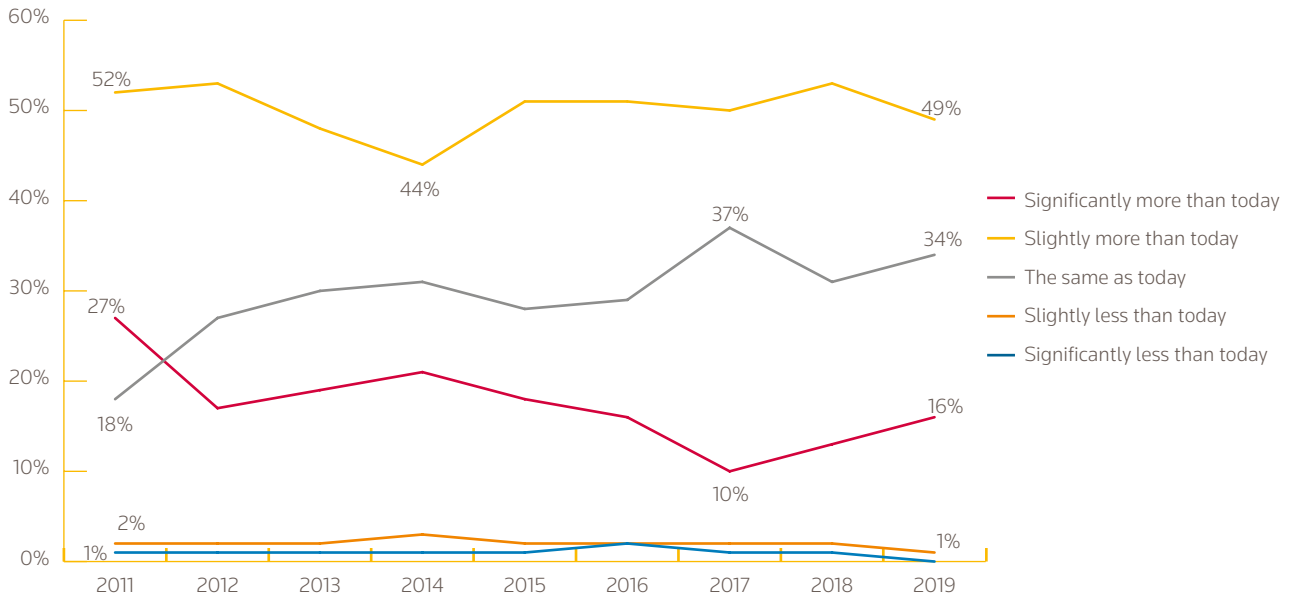


Source: Thomson Reuters Regulatory Intelligence – Cost of Compliance 2019: 10 years of regulatory change, by Stacey English and Susannah Hammond.

Over half of respondents continue to foresee an increase in the cost of senior compliance staff driven by the increasing need for expert skills and knowledge needed to handle the challenges and complexity of the compliance issues facing financial services firms.

Regionally, 82% of practitioners in Australasia expect the biggest increase in the cost of senior compliance staff (51% slightly more than today, 31% significantly more) again driven by the need for skilled staff and knowledge.

Over the next 12 months, I expect the cost of senior compliance staff to be...



Source: Thomson Reuters Regulatory Intelligence – Cost of Compliance 2019: 10 years of regulatory change, by Stacey English and Susannah Hammond.

PERSONAL LIABILITY

"These reforms will constrain the ability of senior executives to escape liability for wrongdoing; the days of individuals hiding behind the collective will be numbered."

Seana Cunningham, Director of Enforcement and Anti-Money Laundering at the Central Bank of Ireland. Speech, "Individual accountability – our approach", at a Deloitte Ireland event (August 2018).

What is the biggest change you predict for compliance in the next 10 years?

"Day by day compliance challenges are growing and so the personal liability of compliance-staff. We expect, if the trend remains same, it will become more and more difficult to find qualified and experienced staff specially at higher level."

Risk and compliance executive, Middle Eastern Bank
Survey respondent, Thomson Reuters Regulatory Intelligence – Cost of Compliance 2019.

One of the key global regulatory changes in the wake of the financial crisis was the rise of personal accountability regimes, partly as a result of political concern that very few individuals were found responsible for causing the crisis and partly as a means by which to drive better risk-aware behaviors from senior managers in the future. Personal accountability regimes aren't just aimed at risk and compliance officers but rather at all senior individuals in a firm. The UK led the way with the sector by sector roll-out of the Senior Managers and Certification Regime (SMCR), the final tranche of which comes into effect in December 2019. Jurisdictions around the world have taken similar but slightly different stances all with a focus on ensuring clarity of what senior personnel are responsible for, and then holding them accountable for compliance breaches in their area of responsibility.

As a snapshot, in addition to the roll-out of the SMCR in the UK, personal accountability regimes in force or being planned include:

- Banking Executive Accountability Regime (BEAR) in Australia with further accountability measures likely in the wake of the Royal Commission report recommendations;
- Managers in Charge (MIC) regime in Hong Kong;
- Proposed guidelines on individual accountability and conduct in Singapore;
- Proposed senior executive accountability regime and other measures in Ireland to be modelled on the UK SMCR with the Central Bank of Ireland noting that the UK Financial Conduct Authority had found the new approach 'effective' and that 'great benefit has been found in other jurisdictions in relation to the adoption of this policy';
- Proposed responsibility mapping in Malaysia.

The greatest compliance challenge(s) I expect to face in 2019 is/are...

"...heightened regulatory scrutiny and expectations and demands from senior management and Boards."

Risk and compliance executive, Australian Bank
Survey respondent, Thomson Reuters Regulatory Intelligence – Cost of Compliance 2019.

Personal accountability isn't simply driven by financial services regulators. In the U.S., two successive chief executives of Wells Fargo resigned (the latter in March 2019) in the wake of political and investor pressure following the spotlight that was shone on a series of poor sales practices. In the UK, similar but different concerns arose again centred on damage to the required good customer outcomes. As witnessed by TSB in the spring of 2018, a series of IT outages meant that customers were, among other things, unable to access their accounts. The depth and nature of the IT problems at TSB led to the Treasury Committee launching an inquiry under which it will consider the preparation for, implementation of, and results of, the system migration, and TSB's handling of the customer outage problems that ensued.

As part of that inquiry the chair of the Committee published, in June 2018, a letter expressing a 'loss of confidence' in the chief executive of the bank:

'As a result, the Committee considers that the TSB Board should give serious consideration as to whether Dr Pester's position as Chief Executive of TSB is sustainable. The Committee has lost confidence in his ability to provide a full and frank assessment of the problems at TSB, and to deal with them in the best interests of its customers. It is concerned that, if he continues in his position, this could damage trust not only in TSB, but in the retail banking sector as a whole. I ask that the Board consider the Committee's view as a matter of urgency.'

Dr Pester resigned as chief executive of TSB in September 2018.

The greatest compliance challenge(s) the board expect to face in 2019 is/are...

"...local senior manager made accountable for decisions formulated at Group/Global level."

Head of Compliance, Asia
Survey respondent, Thomson Reuters Regulatory Intelligence – Cost of Compliance 2019.

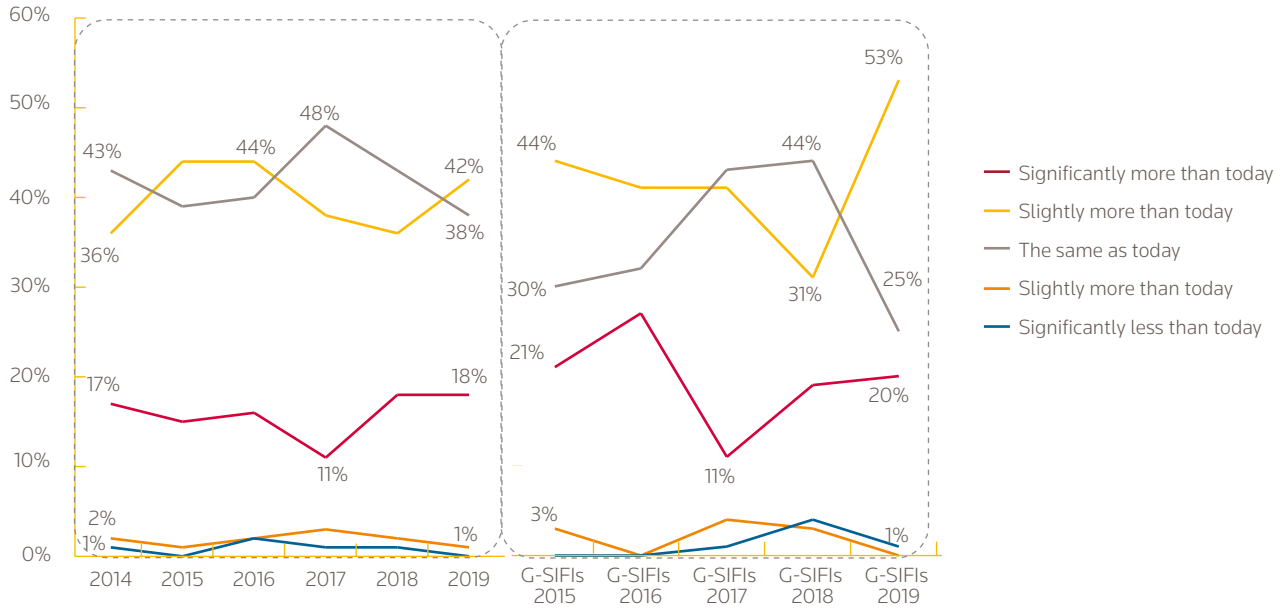
"...the Senior Managers Regime does not stop at the regulatory perimeter – it is a whole firm concept. And that in my view is right because responsibility should not be limited as a principle and should guide conduct. To put it simply, you can't behave yourself inside the perimeter and "let it all hang out" outside the perimeter – that's not really a sustainable way of going about things. But obviously, by creating that whole firm regime in terms of responsibility, it does create an issue for us as the regulator about how we judge conduct outside the perimeter if we don't have rules setting detailed standards for that conduct. There is a role for well-constructed standards that we can endorse and use to put the SMR into practice."

Andrew Bailey, Chief Executive Officer at the UK Financial Conduct Authority (FCA). Excerpts from the transcript of his speech delivered at The FMSB Event: "Two Years on from the Fair and Effective Markets Review". FMSB Annual Report 2018, "Towards Fairer Markets" (March 2019).

Personal liability understandably remains a key concern for compliance officers. The results from both G-SIFIs and all firms show that the vast majority (98% for both) expect the personal liability of compliance professionals to either remain the same or grow in the coming year. In a substantive change from 2018, 73% of G-SIFIs expect the personal liability of compliance professionals to increase in the next 12 months (20% expecting a significant increase). The population of all firms is not far behind in its expectations of increasing personal liability for compliance professionals, 60% expect an increase with 18% expecting a significant increase in the coming year.

Regionally, a quarter (24%) of firms in Continental Europe expect a significant increase in the personal liability of compliance professionals, compared to just 9% among peers in North America.

Over the next 12 months, I expect the personal liability of compliance professionals to be:



Source: Thomson Reuters Regulatory Intelligence – Cost of Compliance 2019: 10 years of regulatory change, by Stacey English and Susannah Hammond.

Over time, concerns about increasing personal liability for compliance professionals has been persistent with year-on-year expectations of growth driven, at least in part, by the spread of accountability regimes around the world and the global focus on the need to eradicate misconduct in financial services.

Expectations of high and increasing personal liability for compliance officers have become the norm. The underlying thread of compliance officers needing to 'cope' with the challenges expected in the year ahead is set against that backdrop. Compliance may well take the lead in determining how best to identify, manage and mitigate the increasing personal accountability. There are several benefits for compliance officers thinking through how to best manage their own personal regulatory risk. Most obviously is that they themselves stay out of regulatory trouble. Other benefits include being able to advise other senior managers on the likely best practices associated with managing personal regulatory risk, and, once their own risk is appropriately managed, they will be able to devote more attention back to the day job of firm compliance.

Compliance officers cannot manage compliance and regulatory risks alone. They can and must be supported by their board and other senior managers. Board members are not expected to be experts in everything, but they do need to have sufficient knowledge and to have an appropriate range of skills to understand the issues, able to set an appropriate risk appetite, drive a strong compliant culture, understand and challenge all risk and compliance reports as well as engage appropriately with regulators.

One means by which firms could seek to tackle any potential issues around a possible lack of individual or collective understanding is through training. For boards, a strong and effective suite of training needs above all else needs to be tailored to the audience. Given the seniority and diversity of experience at the board level, bespoke training tends to be used with regular, often face-to-face, bite-sized updates to accommodate busy schedules. It is critical that any and all training is robustly and consistently captured and recorded with any absences from training course(s) followed up and completed in a timely manner. Specifically, training needs to be seen as a key mechanism by which individuals (senior or otherwise) can use to identify, manage and mitigate any and all personal regulatory risks.

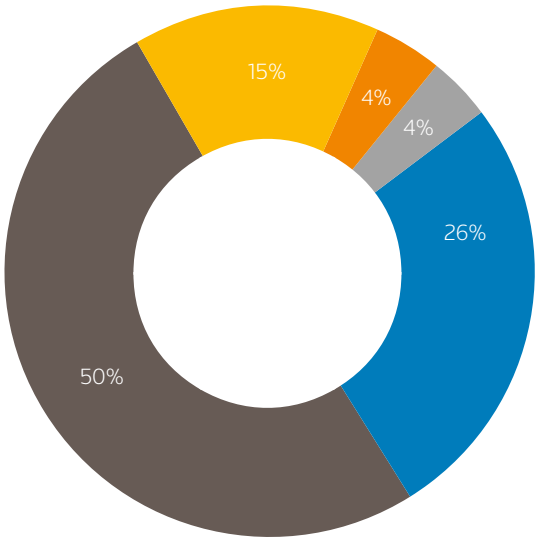
TYPICAL WEEK OF A COMPLIANCE OFFICER

The greatest compliance challenge(s) I expect to face in 2019 is/are...

"The need for the compliance function to be diversified, skilled and flexible enough to support diverse fast-paced technology driven business projects."

Compliance Practitioner, G-SIFI, United Kingdom
Survey respondent, Thomson Reuters Regulatory Intelligence – Cost of Compliance 2019.

Typical week of a compliance officer in 2019

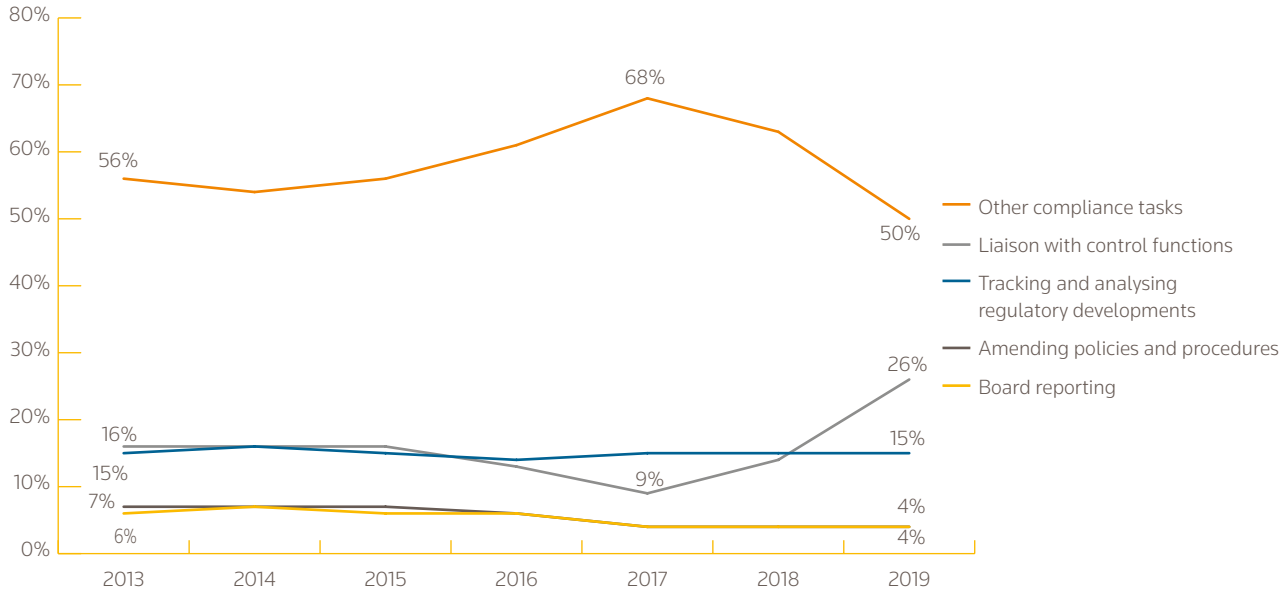


- Tracking and analysing regulatory developments
- Board reporting
- Amending policies and procedures
- Liaison with control functions
- Other compliance engagements, including:
  - ✓ Accountability regimes
  - ✓ Administering internal controls
  - ✓ Aligning global compliance requirements
  - ✓ Assessing and monitoring conduct risk
  - ✓ Brexit preparations
  - ✓ Cyber resilience
  - ✓ Evaluating compliance activities against cost
  - ✓ Implementing and ensuring compliance with new regulations
  - ✓ Improving compliance culture of the organisation
  - ✓ Monitoring financial crime risk, sanctions, market conduct
  - ✓ Outsourcing arrangements
  - ✓ Overseeing corporate strategy and growth
  - ✓ Overseeing privacy and data protection
  - ✓ Regulatory reporting
  - ✓ Remediation programs
  - ✓ Reviewing new initiatives and existing products
  - ✓ Setting out corporate governance standards from board down
  - ✓ Training

Source: Thomson Reuters Regulatory Intelligence – Cost of Compliance 2019: 10 years of regulatory change, by Stacey English and Susannah Hammond.

Compliance officers by necessity are multi-taskers. Those skills have been often severely tested in the years since the financial crisis, with the sheer range of issues that have been added to the core tasks of tracking and analysing regulatory change, board & regulatory reporting, amending policies and procedures and liaising with other control functions.

Year-on-year review: Typical week of a compliance officer



Source: Thomson Reuters Regulatory Intelligence – Cost of Compliance 2019: 10 years of regulatory change, by Stacey English and Susannah Hammond.

The list of 'other' activities where compliance practitioners are spending their time does not get any shorter. The drop from the apparent 'peak' of 68% in 2017 to 50% in 2019 may be indicative of firms' investment in technological solutions to capture regulatory developments, or a shift in responsibilities and focus skilled compliance resources to other key areas such as liaison with control functions, which has seen a rise over the same period.

What is the biggest change you predict for compliance in the next 10 years?

"Compliance being considered at every stage of the business process - not just when things go wrong. It will be an integrated, valued inclusion, from initial planning and strategy development, through all phases of product or service development, to delivery and reporting."

Compliance Director, Australian Bank
Survey respondent, Thomson Reuters Regulatory Intelligence – Cost of Compliance 2019.

Key regulatory events

Global financial crisis

2009

- Former CEO of the UK FSA tells firms they should "be very afraid" of the regulator
- G20 declaration on strenthening the financial system; Financial Stability Board established

2010

- US Foreign Account Tax Compliance Act (FATCA) is signed into law
- Basel III regulatory framework agreed
- US Dodd-Frank Act passed

2011

- Hong Kong banks pay $813m compensation to investors of structured products or minibonds distributed by collapsed US bank Lehman Brothers
- US Consumer Financial Protection Bureau founded

2012

- Fines imposed on Barclays for Libor manipulation; scandal widens over the coming months with other banks fined
- European Market Infrastructure Regulation (EMIR) enters into force
- Financial Services Act 2012 passed in the UK, creating a new twin peaks regulatory framework for financial services and abolishing the FSA

2013

- The UK's FCA and PRA commence operations
- The UK's Financial Services (Banking Reform) Act 2013, enters into force, sets the foundation for SMCR
- The UK Parliamentary Commission on Banking Standards publishes its report 'Changing Banking for Good'

2014

- European Union law, MiFID II, adopted
- US DoJ fines BNP Paribas a record $8.9bn for sanctions violations
- US DoJ fines Bank of America $16.65bn for subprime mortgages failure
- The UK FCA imposes substantial fines on five banks for manipulation of the Forex market
- The final report of Australia's Financial System Inquiry is published

2015

- The UK Banking Standards Board commences its work
- Malaysia establishes taskforce to investigate allegations relating to 1MDB
- US DoJ publishes the Yates Memo stressing individual accountability

2016

- EU's Solvency II comes into effect
- UK's SMCR replaces Approved Persons Regime for banks, building societies, credit unions and dual-regulated investment firms
- Legislative changes passed extending the UK's SMCR to all FSMA firms
- Wells Fargo fined $185 million for fraudulent savings and checking accounts

2017

- FX Global Code establishing a common set of guidelines for good practice in the FX market released
- Hong Kong's SFC Managers-In-Charge regime comes into effect
- Australia launches Royal Commission into misconduct in the banking, superannuation and financial services industry

2018

- The UK's FCA and PRA jointly fine CEO of Barclays following his attempts at discovering a whistleblower's identity
- First stage of implementation of Australia's Banking Executive Accountability Regime (BEAR)
- The UK's SMCR extended to all dual-regulated insurers

2019

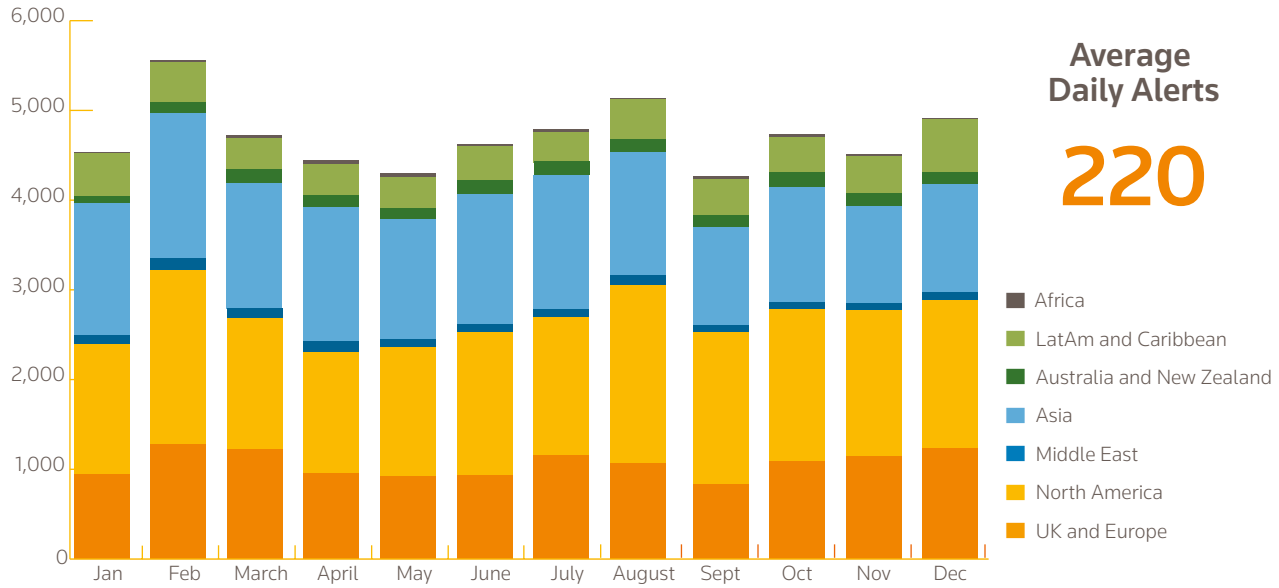
- Australia's Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry publishes final report
- Central Bank of Ireland launch the Irish Banking Culture Board, focusing on behaviour, ethics and culture
- The UK FCA imposes fines totaling over £60m on Goldman Sachs and UBS for longstanding transaction reporting failures

Source: Thomson Reuters Regulatory Intelligence – Cost of Compliance 2019: 10 years of regulatory change, by Stacey English and Susannah Hammond.

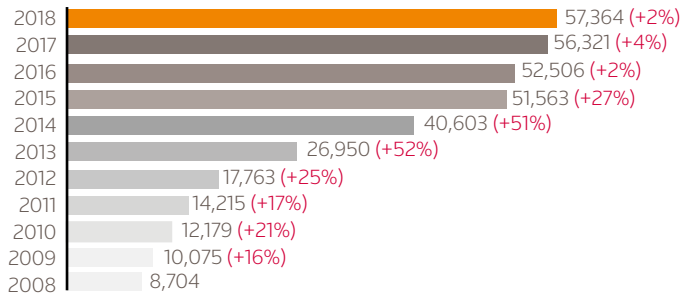
REGULATORY CHANGE AND CONTINUING UNCERTAINTY

A central thread throughout all the challenges for boards and compliance functions alike is that of continuing regulatory change. The plethora of changes introduced in the wake of the financial crisis have come full circle with the FSB moving from new policy mode to assessing the effectiveness of the changes made. As many firms have found, the current patchwork quilt of over and under-lapping regulatory requirements requires careful and expert navigation. This is particularly pertinent when it comes to geopolitical risk and sanctions.

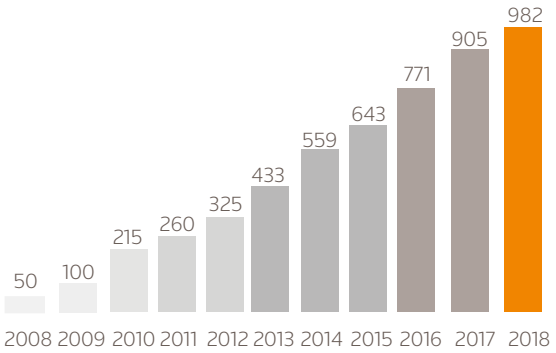
Regulatory Intelligence Content Metrics | Tracked 2018



Total Yearly Alerts



Total Organisations Monitored

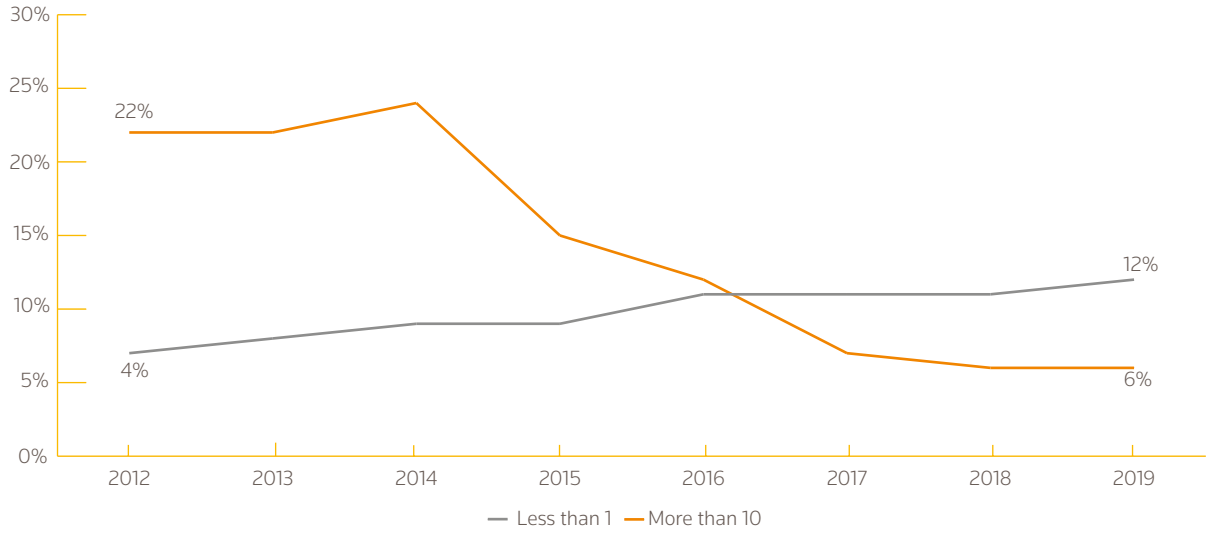


Source: Thomson Reuters Regulatory Intelligence – Cost of Compliance 2019: 10 years of regulatory change, by Stacey English and Susannah Hammond.

The number of regulatory bodies tracked by TRRI has continued to grow and in 2019 reached the milestone of 1,000 regulatory bodies being tracked. From those TRRI captured 57,398 regulatory alerts averaging 220 updates a day.

It is perhaps a reflection of the increasing automation provided by solutions such as TRRI that the percentage of compliance teams spending adequate time tracking and analysing regulatory developments continues to fall year-on-year. In 2012, over a fifth (22%) of firms dedicated more than 10 hours a week, compared to just 6% in 2019. This pattern continues among G-SIFIs (29% 2015, 9% in 2019).

In an average week, how much time does your compliance team spend tracking and analysing regulatory developments? (in hours)



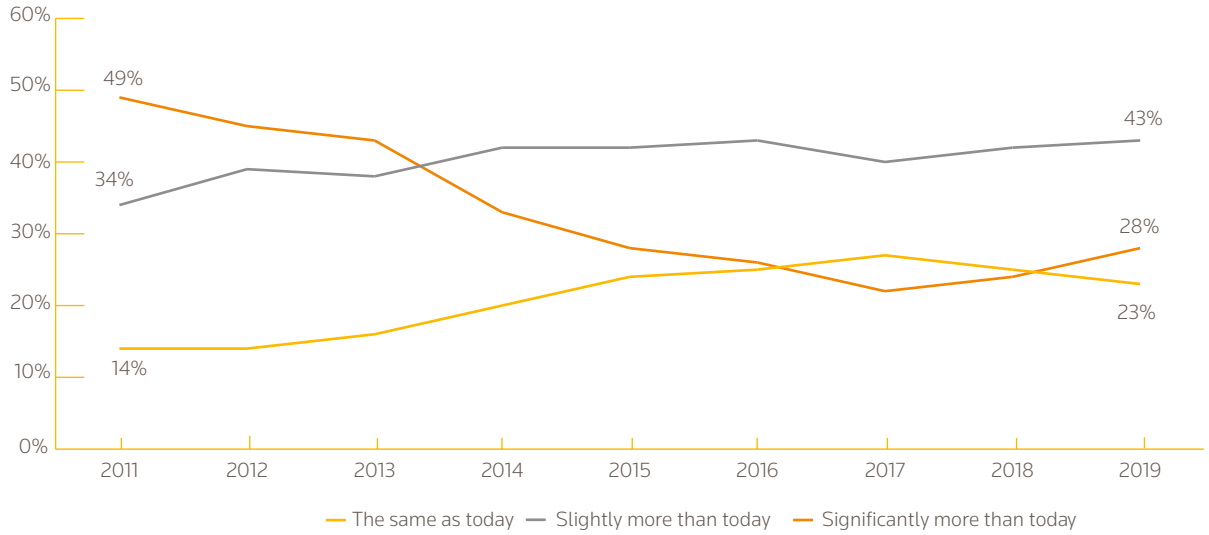
Source: Thomson Reuters Regulatory Intelligence – Cost of Compliance 2019: 10 years of regulatory change, by Stacey English and Susannah Hammond.

In 2019, 71% of firms expect the amount of regulatory information published by regulators and exchanges to increase over the next 12 months (43% slightly more, 28% significantly more). There is an inflexion point in the expectations in 2017. Before that, there was a steady decline in respondents who expected the amount of regulatory information published by regulators and exchanges to increase, since 2017 the sense is that firms are expecting an increasing rate of growth in the levels of regulatory information published. Increasing expectations around the amount of regulatory information likely to be published is a key driver of the challenges around continuing regulatory change.

Regionally, firms in Australasia are expecting the biggest increase with more than half (56%) of firms expecting a significant increase in regulatory information published by regulators and exchanges over the next 12 months. This may well be a response to the Royal Commission into misconduct in the banking, superannuation and financial services industry in Australia. The findings from the Royal Commission also triggered regulators in New Zealand to instigate a first-of -its-kind joint review by the Financial Markets Authority and Reserve Bank of New Zealand into the culture and conduct of 11 New Zealand banks.

Similarly, almost half of firms in the Middle East (47%) also expect a significant increase in regulatory information published by regulators and exchanges over the next 12 months. This may relate to an increased focus around technology and innovation, such as its role in the Global Financial Innovation Network as well as the planned Financial Action Task Force visit to the United Arab Emirates.

Over the next 12 months, I expect the amount of regulatory information published by regulators and exchanges to be....



Source: Thomson Reuters Regulatory Intelligence – Cost of Compliance 2019: 10 years of regulatory change, by Stacey English and Susannah Hammond.

REPORTING

"The cost of interpreting and removing ambiguity from regulatory rules and the collation of relevant data, were the most commonly referenced costs associated with the current reporting regime. Responses also highlighted significant costs related to updating systems to deal with new requirements and maintaining and reporting through multiple systems, particularly for firms operating in several jurisdictions. Ad hoc requests were seen by several respondents as compounding these costs. Some responses noted the fines associated for non-compliance or erroneous reporting have the potential to be higher than the cost of reporting itself.

Digital Regulatory Reporting – Feedback Statement on Call for Input (FS18/2). Financial Conduct Authority (October 2018).

What is the biggest change you predict for compliance in the next 10 years?

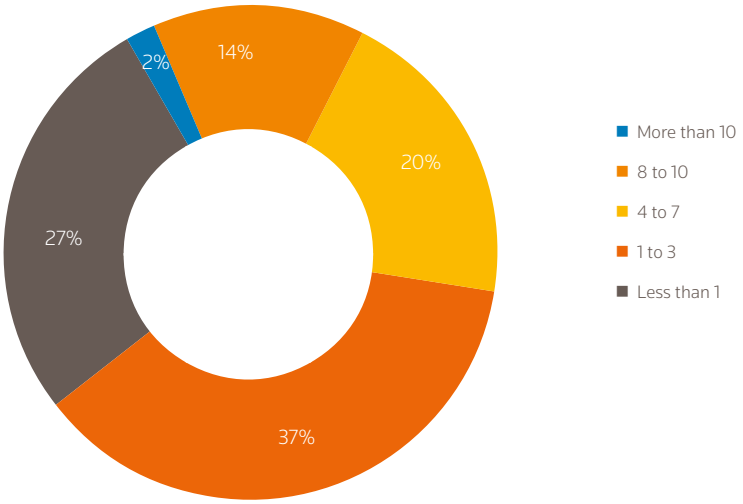
"Increasing reliance on regtech (RPA/AI) to manage daily compliance tasks, data/information management and reporting."

Head of Compliance, Australia
Survey respondent, Thomson Reuters Regulatory Intelligence – Cost of Compliance 2019.

While the percentage of compliance teams spending between 1 and 3 hours per week creating and amending reports for the board has remained relatively similar year-on-year, the percentage of compliance teams spending more than 8 hours per week has doubled compared to 2011 results (7% to 14% in 2019). Regionally, compliance teams in North America spend the least time on board reporting (80% 0 to 3 hours).

Compliance functions need to find the time to produce succinct, accurate and timely reports for the board and other senior managers. This is not only to ensure that the board has an appropriate line of sight to the identification, management and mitigation of regulatory risks but it is increasingly important evidence in the discharge of personal accountability obligations.

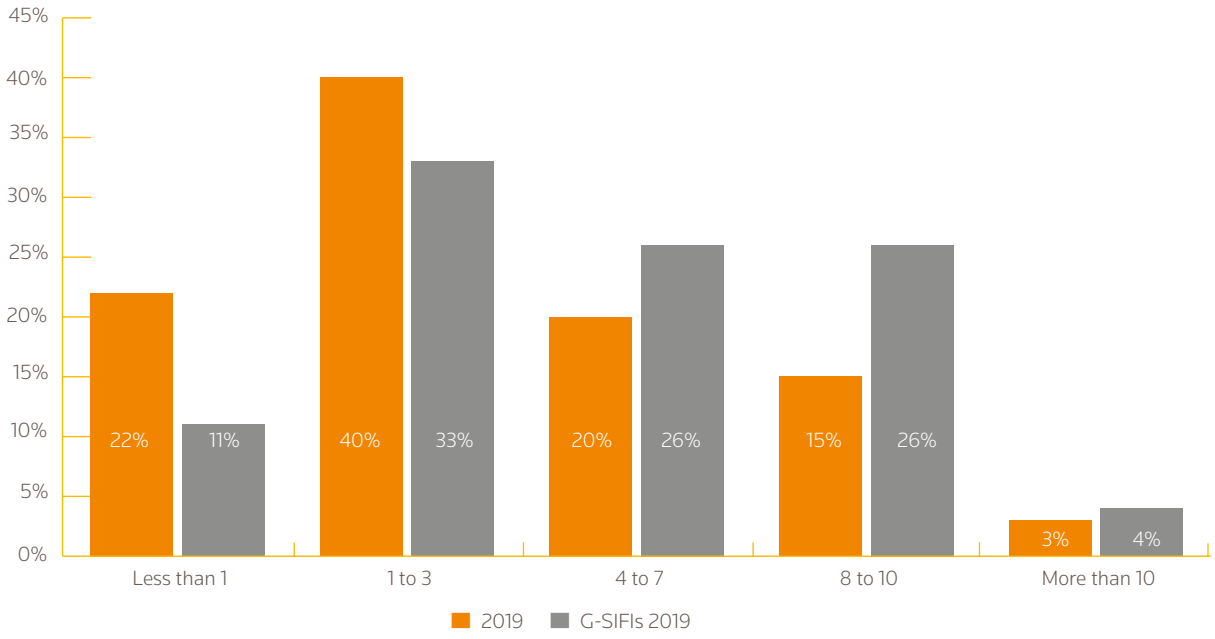
In an average week, how much time does your compliance team spend creating and amending reports for the board? (in hours)



Source: Thomson Reuters Regulatory Intelligence – Cost of Compliance 2019: 10 years of regulatory change, by Stacey English and Susannah Hammond.

The average time compliance teams spend amending policies and procedures to reflect the latest regulatory rules has remained consistent year-on-year since 2011, with an average 61% of firms spending less than 3 hours in a week (62% in 2019). The percentage of compliance teams at G-SIFIs who spend more than 10 hours a week amending policies and procedures has fallen significantly from 25% in 2015, to 3% in 2019 again perhaps as a result of an investment in automation.

In an average week, how much time does your compliance team spend amending policies and procedures to reflect the latest regulatory rules (in hours)?



Source: Thomson Reuters Regulatory Intelligence – Cost of Compliance 2019: 10 years of regulatory change, by Stacey English and Susannah Hammond.

ALIGNMENT WITH OTHER RISK AND CONTROL FUNCTIONS

"Under no circumstances should banks cut costs at the expense of risk management and of the quality of risk data aggregation and reporting. On the contrary, they should fortify their operational management, risk control and compliance, as well as their independent internal audit function. They should make sure that, for each risk, accountability and ownership are defined and well understood throughout the organization."

Danièle Nouy, Chair of the Supervisory Board at the European Central Bank (ECB). Keynote speech, "Good governance – an asset for all seasons" at the farewell seminar of Jan Sijbrand, "From Lehman to Bitcoin – trends and cycles in financial supervision", Amsterdam (June 2018).

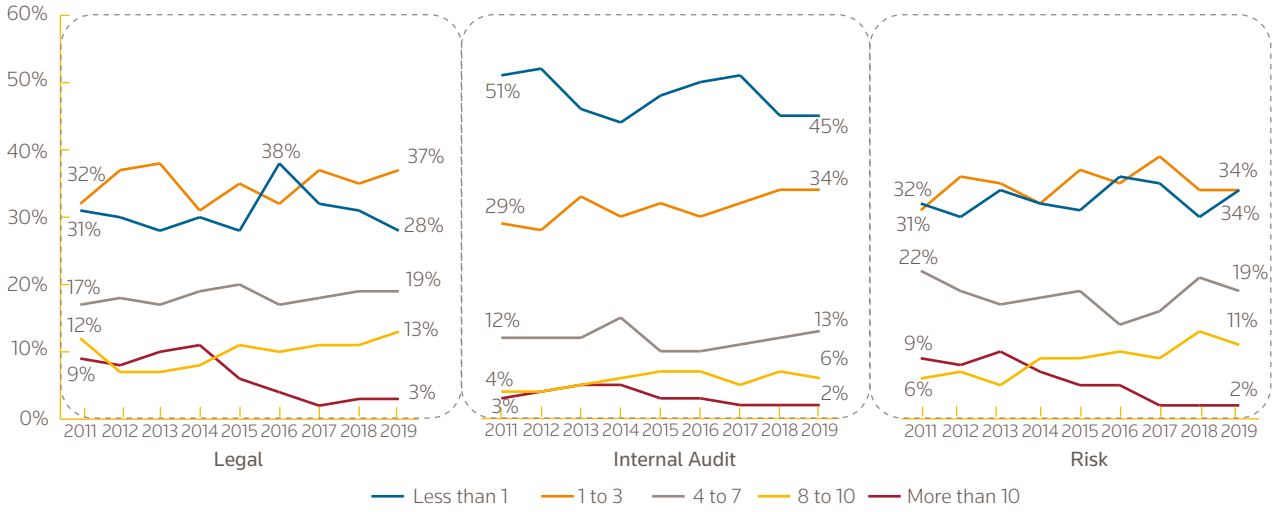
The greatest compliance challenge(s) I expect to face in 2019 is/are...

"There has been much confusion as to what compliance really is all about. Companies often mix it up with risk, audit or even legal."

Compliance Practitioner, Asia
Survey respondent, Thomson Reuters Regulatory Intelligence – Cost of Compliance 2019.

From the compliance perspective, the interaction and alignment with the other risk and control functions in a firm has been less of a priority in terms of time and focus. Compliance, legal, audit and risk functions all have different and distinct roles, but there is much to be gained by overt cooperation particularly in terms of firm-wide risk assessment and reporting.

In an average week, how much time does your compliance team spend liaising with the legal, internal audit and risk functions on compliance issues (in hours)?



Source: Thomson Reuters Regulatory Intelligence – Cost of Compliance 2019: 10 years of regulatory change, by Stacey English and Susannah Hammond.

Firms, on average, dedicate more of their time liaising with the legal function, followed by risk, then internal audit.

A third (37%) of compliance teams spend, on average, between 1 and 3 hours per week liaising with the legal functions. There has been a shift in the G-SIFI population from 2015, when 21% of G-SIFI compliance teams reported spending more than 10 hours a week liaising with legal functions dropping to just 2% in 2019.

Similarly, a third (34%) of compliance teams spend less than 3 hours a week liaising with risk. This has remained fairly consistent for all firms, including G-SIFIs, year-on-year between 2011 and 2019. Of most concern is perhaps the lack of time compliance teams spend with internal audit. In 2019, almost half (45%) spend less than 1 hour a week liaising internal audit.

LIAISON WITH REGULATORS

Good regulatory relationship management is a required core competency for all senior compliance officers. Whilst there has been a rise in electronic reporting requirements, the focus on culture and conduct risk together with the roll-out of accountability regimes means that strong, proactive regulatory relationship management is more important than ever.

There has been an ebb and flow in the expectations around the time spent liaising and communicating with regulators and exchanges. Respondents have consistently reported an expected increase with in 2010, 66% of firms expecting an increase, falling to 53% in 2017, and back up to 71% in 2019.

The top three reasons why firms expect an increase in the time spent liaising and communicating with regulators over the coming year are:

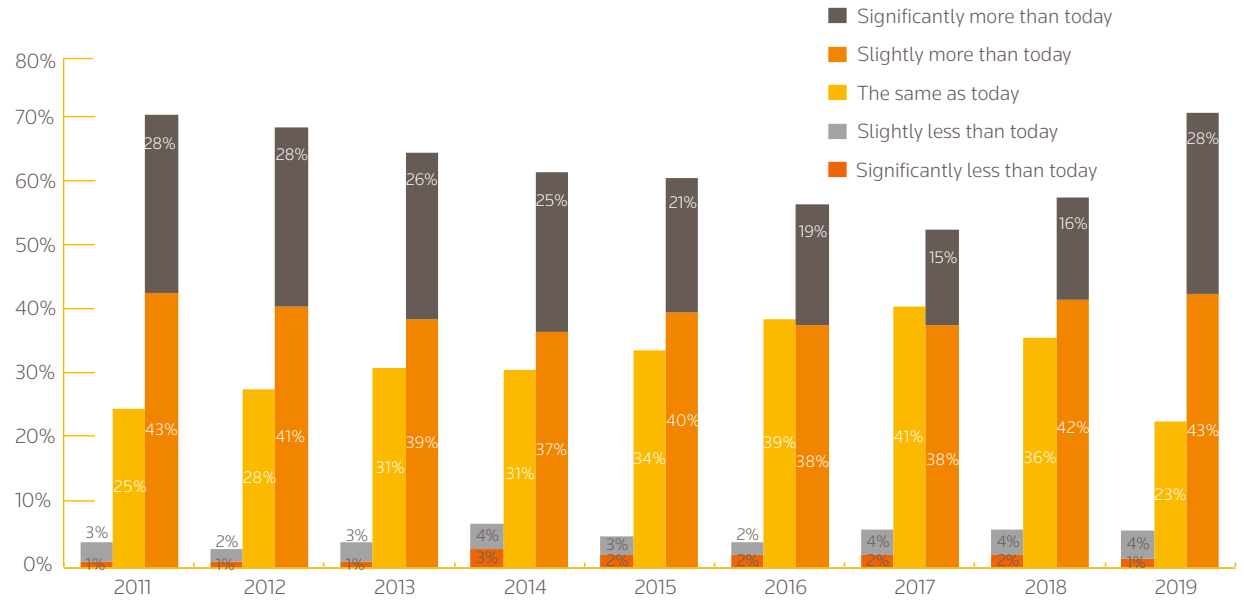
1. increased information requests from regulators (57%);
2. need to understand changing regulatory expectations (56%); and
3. more onerous regulatory and reporting requirements (54%).

All of the top three reasons given for an expected increase in time spent liaising and communicating with regulators and exchanges require expert management and may also require additional skilled resources together with additional investment in technology and/or automation.

"...a 'one-size-fits-all' approach is tempting because it is simple. But its simplicity is precisely why regulators must avoid it. Effective regulation today demands differentiated regulatory requirements that cater for a spectrum of risk profiles."

Abdul Rasheed Ghaffour, Deputy Governor of the Central Bank of Malaysia (Bank Negara Malaysia). Keynote address, "Reimagining the regulatory landscape for payment systems", at the Global Payments Week 2018, Kuala Lumpur (December 2018).

Over the next 12 months, I expect the time spent liaising and communicating with regulators and exchanges to be....



Source: Thomson Reuters Regulatory Intelligence – Fintech, Regtech and the Role of Compliance in 2019, by Stacey English and Susannah Hammond

A measure of the critical nature of regulatory reporting is highlighted in the April 2019 initial response of the UK Prudential Regulation Authority (PRA) and Bank of England (BoE) to an independent review of the prudential supervision of the Co-operative Bank which suffered a £1.5bn capital shortfall. One of the specific recommendations made by the review was on regulatory reporting. The PRA has agreed that it should consider introducing more formal third-party reviews of key prudential information supplied by banking groups through their regulatory data returns.

Accurate regulatory returns are an essential part of the PRA's supervisory approach and third-party reviews were a feature of previous banking supervision in the UK when banks would typically be subject to a review under s39 of the 1987 Banking Act (the equivalent of 'reports by skilled persons' under s166 of FSMA). This approach was halted as a routine part of supervision because it was felt to be disproportionate. That said, such reviews of returns do take place where supervisors have grounds to believe that the poor quality of returns pose a material risk to the PRA's objectives.

Specifically, the PRA will assess:

- whether the benefits of any such reviews would outweigh the costs;
- to which types or sizes of firms they might apply;
- which data might be within scope;
- whether reviews would be targeted or regular; and
- whether the results of the review would be private or public.

As part of the consideration, the PRA has made clear that with regard to the accuracy of regulatory returns:

- Firms have responsibility for complying with relevant regulations and rules, and need to take reasonable steps to ensure that information submitted is accurate, fairly and properly based, and complete. In addition, under the Senior Managers Regime firms are required to assign a 'prescribed responsibility' for the production and integrity of regulatory reporting.
- The PRA carries out validation and plausibility checks on prudential information for all firms. In addition, line supervisors review prudential information as part of day-to-day supervision.
- Where the PRA has particular concerns about the accuracy of regulatory information, it may require individual firms to carry out work, for example internal audit reviews or remedial procedures, or it may commission an external view, potentially under s166.

This example puts all firms, regardless of jurisdiction, on notice that the quality, completeness and accuracy of regulatory returns will be under the supervisory spotlight and would be well advised to review the controls and approach as well as the skilled resources allocated to regulatory reporting and returns. In particular, firms would be well advised to remediate any issues found and inform the relevant regulator as a matter of urgency of any substantive or material errors or updates.

Implications of Australia's Royal Commission

Widespread and persistent conduct concerns led to the Australian government setting up a Royal Commission to consider misconduct in banking, superannuation and financial services industry. The Royal Commission's final report was published in February 2019 and will not only rewrite the approach to financial services in Australia with a suite of 76 sweeping reforms but it has also claimed (very) senior casualties – as a direct result, the CEO of National Australia Bank Andrew Thorburn will step down on February 28, 2019 and the chairman, Ken Henry, will step down once a permanent successor to the CEO is found.

Both, the Australia Securities and Investment Commission (ASIC) and the Australian Prudential Regulation Authority (APRA) have received additional funding from the federal government, and changed their enforcement approaches announcing legal actions against major financial institutions. After the Royal Commission final report, the approach of these regulators appears to be a "litigate first and talk later" stance in order to deal with serious compliance and regulatory failures that affect consumers and deposit holders. There is no doubt that additional costs in compliance maybe financial institutions having to deal with more aggressive regulators.

More widely, it is estimated that banks in Australia have set aside AUD$2bn to meet the likely costs of remediation. The thread throughout the Commission report is that senior managers can no longer ignore the need to improve compliance and boards can no longer 'fob off' advice from the compliance function without potentially serious implications for both firm and individuals.

There are numerous lessons for all firms in all jurisdictions including the need for:

- better quality risk and compliance reporting for boards;
- improved compliance and risk oversight, focused on key regulatory issues;
- more openness in communications with regulators;
- boards to have the wider skill sets needed to provide the oversight and scrutiny required for issues such as prevention of money laundering, culture and conduct risk and regulatory relationship management;
- whistleblowers to be encouraged and listened to; and
- remuneration to be designed, expressly, to drive better risk-aware behaviors.

MANAGING REGULATORY RISK

The greatest compliance challenge(s) the board expects to face in 2019 is/are...

"Obtaining comfort that regulatory risk is effectively managed."

Senior Compliance Practitioner, European Bank
Survey respondent, Thomson Reuters Regulatory Intelligence – Cost of Compliance 2019.

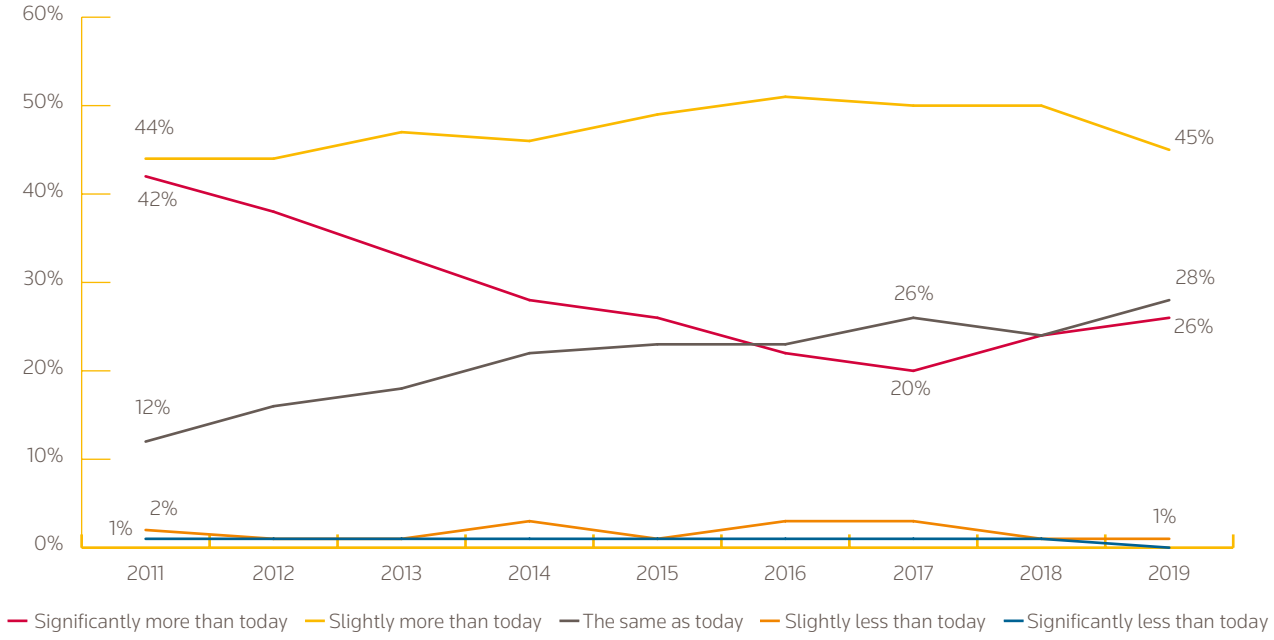
The focus on the need to manage regulatory risks effectively has been unrelenting. Over time the expectation that the regulatory focus on managing regulatory risk will increase in the coming year has, in terms of an overall expected growth, declined from 86% (44% slightly more, 42% significantly more) in 2011, to 71% (45% slightly more, 26% significantly more) in 2019.

At the same time, the number of practitioners who expect the focus on managing regulatory risk to remain the same has increased and now at its highest point (28%).

Looking at a five-year time-span, the same pattern can be seen among G-SIFIs, where 75% of firms in the 2015 survey expected an increased focus on managing regulatory risk, compared to 68% in 2019.

The reasons given as to why firms expect an increased focus on managing regulatory risk have shifted over the history of the survey, from increased interest from senior managers and board in 2013, to regulatory focus on culture and conduct risk between 2014 and 2016, and finally to continued regulatory change between 2017 and 2019.

Year-on-year review: Over the next 12 months, I expect the focus on managing regulatory risk to be...



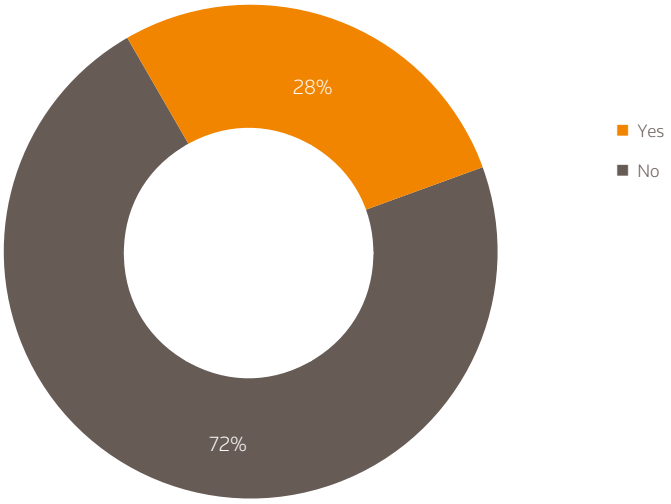
Source: Thomson Reuters Regulatory Intelligence – Cost of Compliance 2019: 10 years of regulatory change, by Stacey English and Susannah Hammond.

OUTSOURCING

"Ultimately, boards and senior management of regulated firms are responsible for the management of outsourcing risk. Significantly, in the case of intragroup outsourcing, it is also their responsibility to understand how and where their firms' systems and data sit within the group's priority list. Should something go wrong, it is the boards and senior management of regulated firms that will be held accountable."

"Outsourcing – Findings and Issues for Discussion", Central Bank of Ireland (November 2018).

Do you outsource any or all of your compliance functionality?



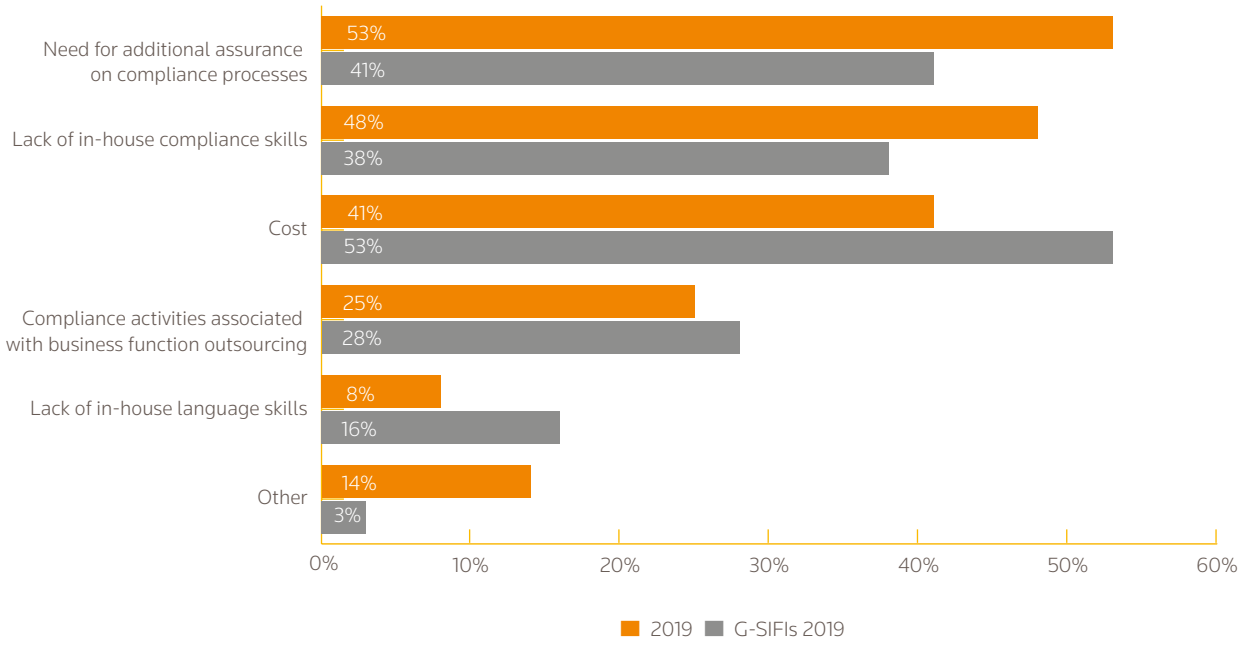
Source: Thomson Reuters Regulatory Intelligence – Cost of Compliance 2019: 10 years of regulatory change, by Stacey English and Susannah Hammond.

Those firms who outsource all or part of their compliance function have remained consistent, ranging between 24% and 28% year-on-year since 2016. Over a third (36%) of G-SIFIs now outsource all or part of their compliance function, the highest level since 2016 when the question was first asked in the survey.

The reasons for outsourcing any or all of a firm's compliance functionality include the need for additional assurance on compliance processes (53%), lack of in-house compliance skills (48%), and cost (41%). These three have remained the top drivers for outsourcing.

The persistence and consistency of the outsourcing of any or all of a firm's compliance functionality is a matter of potential concern in particular where there is seen to be a lack of in-house compliance skills. Firms should consider carefully, and be prepared to answer regulatory questions, as to why the investment has not been made into in-house compliance skills. A persistent lack of the specific skills required to identify, manage and mitigate regulatory risks is a risk in and of itself. Even more so when set against the backdrop of the regulatory focus on culture and conduct risk and the roll-out of accountability regimes.

What were the drivers for outsourcing?



Source: Thomson Reuters Regulatory Intelligence – Cost of Compliance 2019: 10 years of regulatory change, by Stacey English and Susannah Hammond.

"To put it bluntly, we found significant risk management deficiencies on a widespread basis. More broadly, we concluded that, when it comes to outsourcing arrangements, governance and risk management standards are emphatically not where they need to be.

Derville Rowland. Director General at the Central Bank of Ireland. Opening remarks at the Central Bank Outsourcing Conference, Dublin. (April 2019)

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TECHNOLOGY

"...let us not delude ourselves: no matter how mature our framework for responding to protracted outage scenarios, no matter how sound our procedures, no matter how tested our protocol, we never want to rely on these measures from a contingency perspective. The ultimate lesson for any market infrastructure (and for directors, governing bodies, and supervisors), is to so invest in resiliency and security in the core of its operation that it never finds itself in such a state."

Richard Dzina, Executive Vice President at the Federal Reserve Bank of New York. Speech, "Four Questions on the state of Cyber Resilience and Endpoint Security", at the Clearing House and Bank Policy Institute's 2018 Annual Conference, New York City (November 2018).

The greatest compliance challenge(s) the board expect to face in 2019 is/are...

"...the cost of technology adoption as a longer-term solution to hiring more people who are neither better qualified nor worth their salary adjustments."

Senior Manager, Asia professional services firm
Survey respondent, Thomson Reuters Regulatory Intelligence – Cost of Compliance 2019.

It is universally acknowledged that technology will play an increasing part in the future of compliance and regulatory risk management in financial services firms. That said, the revolution promised a few years ago has morphed into a more pragmatic stance with adoption of technological solutions and automation being approached cautiously to ensure that the promised benefits are deliverable. The practical reality is that there are challenges to overcome in order for firms to begin to realise the potential benefits offered by fintech, regtech and insurtech. At a minimum, many firms need to invest, potentially significantly, in the upgrade of their IT infrastructure, which is itself a challenge, not least because whilst that an upgrade is underway, the expectation is that good customer outcomes will be unaffected. Another investment seen to be needed is in specialist skills for both the board and the risk and compliance functions.

Last, but certainly not least, is the increasing role that technology is being seen to play in the personal liability and accountability of senior managers. Senior individuals can, and will be, held responsible for the misuse, failure or lack of resilience of any and all technology and as such would be very well advised to ensure that their skill set is, and remains, as up to date as possible. As with the example under personal liability on page 13 of the CEO of TSB, regulators and politicians have shown themselves to be increasingly intolerant of senior managers who fail to take the expected reasonable steps with regard to the deployment of and transparency around the state of the firm's technology.

What is the biggest change you predict for compliance in the next 10 years?

"Compliance officer must become experts in regtech/ fintech to provide guidance and advice to business partners."

Compliance officer, US Bank
Survey respondent, Thomson Reuters Regulatory Intelligence – Cost of Compliance 2019.

CYBER RESILIENCE AND DATA PROTECTION

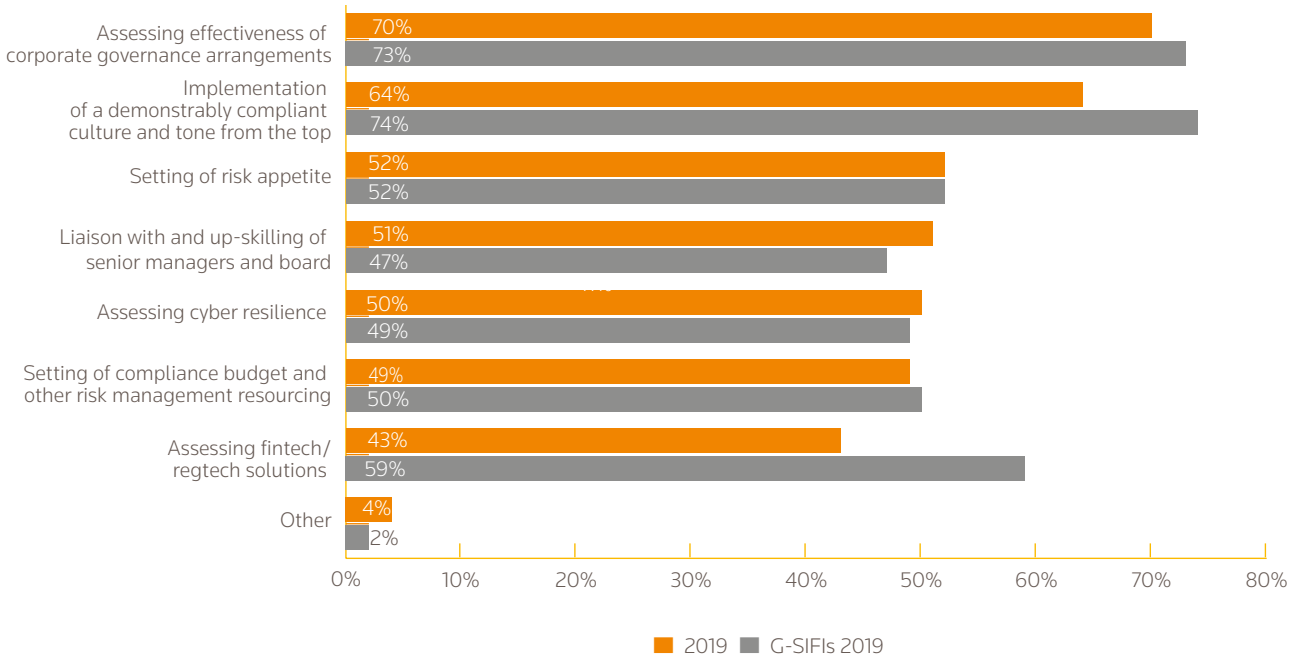
"From a market oversight perspective, we continue to prioritize cybersecurity in our examinations of market participants, including broker-dealers, investment advisers and critical market infrastructure utilities. In assessing how firms prepare for a cybersecurity threat, safeguard customer information, and detect red flags for potential identity theft, for example, we have focused on areas including risk governance, access controls, data loss prevention, vendor management and training, among others. And given the interconnectedness of our markets, we will continue to work closely with our counterparts at other federal financial regulatory agencies and the international community."

Jay Clayton, Chairman to the U.S. Securities and Exchange Commission. Speech, "SEC Rulemaking Over the Past Year, the Road Ahead and Challenges Posed by Brexit, LIBOR Transition and Cybersecurity Risks", New York (December 2018).

The top three areas where compliance practitioners expect more compliance involvement have remained the same from the previous year, and include assessing effectiveness of corporate governance arrangements; implementation of a demonstrably compliant culture and tone from the top; and setting of risk appetite.

Looking at regional variations, over half of practitioners in North America and Asia expect more compliance involvement in assessing cyber resilience (52%, 51% respectively). In Europe, more than half (58%) of practitioners expect more compliance involvement in assessing the effectiveness of corporate governance arrangements.

Over the next 12 months I expect more compliance involvement in...



Source: Thomson Reuters Regulatory Intelligence – Cost of Compliance 2019: 10 years of regulatory change, by Stacey English and Susannah Hammond.

What is the biggest change you predict for compliance in the next 10 years?

"Changing skillsets and profile of compliance officers (fintech/Big data, cybersecurity, data protection and other emerging risks to cope with) while being replaced by robotic-advisory and AI for compliance monitoring."

Head of Compliance, Asia Financial Services Firm
Survey respondent, Thomson Reuters Regulatory Intelligence – Cost of Compliance 2019.

"The GDPR gives us a range of new tools to investigate and to enforce. We can demand algorithmic transparency, we can carry out 'no notice' inspections of premises, and we can demand the destruction of data and call a halt to processing we are not happy with in terms of legal compliance. These are powerful tools. The action we can take when we discover a breach ranges from observation and monitoring, through to reprimands, audits, assessments and inspections, information notices and, when needed, formal investigations, civil financial sanctions or criminal prosecutions."

James Dipple-Johnstone, ICO Deputy Commissioner (Operations) at the Information Commissioner's Office. Speech, "Regulating the tech giants in the digital age", at the Institute of Directors, London (October 2018).

Governments are seeking to make cyber resilience and data protection personal, an example of which is the changes to the UK law with regard to the Privacy and Electronic Communications (EC Directive) Regulations 2003 (PECR) which governs, among other things, nuisance calls. In December 2018, the UK government implemented changes to curb 'those who intentionally and repeatedly flout the rules on nuisance calls' by giving the Information Commissioners Office the power to fine directors individually up to £500,000 each for breaches of PECR.

Under the previous iteration of PECR, the ICO could only take action against a company rather than individual directors or other senior officers. This meant that a rogue director could have avoided fines for breaches of PECR, by dissolving their company at the point they are issued with a fine and starting a new company with a new name (known as "phoenixing") to continue their illegal activities. The legislative changes mean that the ICO can pursue an individual in the same way as a firm with the amendments intended to ensure that the penalty regime for breaches is "effective, proportionate and dissuasive".

The changes to PECR sit in parallel to the UK Data Protection Act 2018, which enables the ICO to fine organisations up to £17 million or 4% of the organization's annual turnover, whichever is higher for the most serious offences which includes breaches of the consent requirements.

CHALLENGES COMPLIANCE OFFICERS FORESEE IN 2019

The greatest compliance challenge(s) I expect to face in 2019 is/are...

Source: Thomson Reuters Regulatory Intelligence – Cost of Compliance 2019: 10 years of regulatory change, by Stacey English and Susannah Hammond.

Respondents were asked to identify their greatest compliance challenge for the coming year. The top challenges for 2019 are:

1. volume and pace of regulatory change
2. increasing regulatory burden
3. financial crime, AML, sanctions
4. culture & conduct risk

This has changed somewhat from the prior year when the greatest compliance challenges were identified as:

1. continuing regulatory change
2. data privacy and GDPR
3. enhanced monitoring and reporting requirements
4. increased regulatory scrutiny

With the exception of data privacy and GDPR included in the 2018 expectations, there has been some consistency in terms of key challenges highlighted by compliance officers over the last few years. The level of consistency in the top challenges does not take away from the sheer scale and sweep of the challenges identified and by association the range of issues which compliance officers expect to face in 2019.

One area of particular challenge is that of AML, sanctions and financial crime. Firms are contending with further changes to the requirements including the European fifth money laundering directive (5MLD) which is due to come into effect in January 2020. Among other things 5MLD covers virtual currencies, the need for enhanced due diligence on countries deemed to be risky and enhancements to the beneficial ownership disclosure regime.

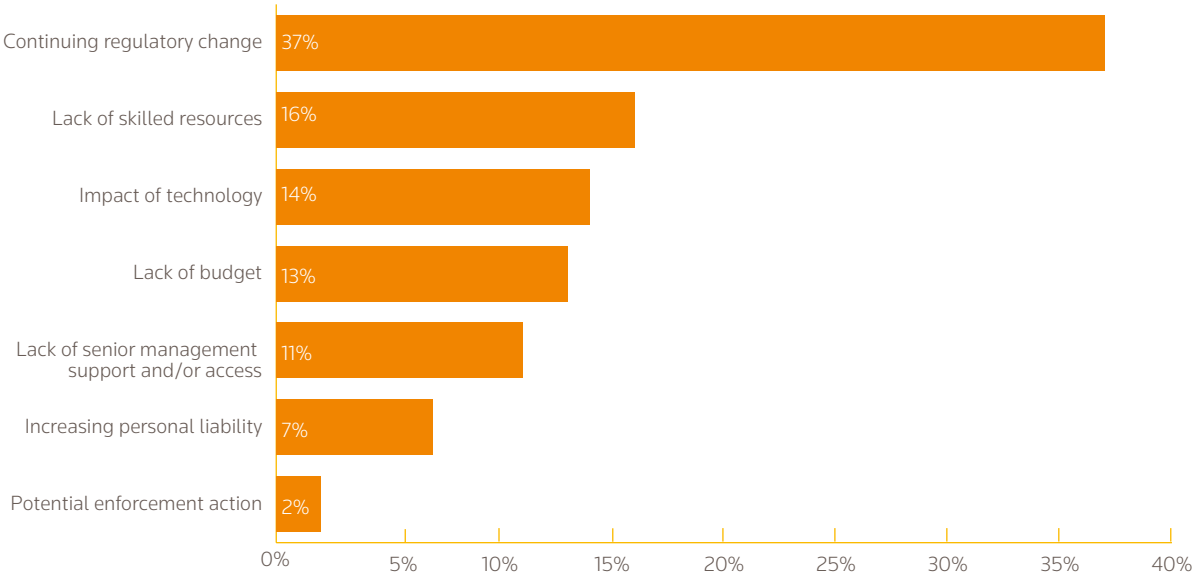
Other issues include the spotlight resulting from visits from the Financial Action Task Force, the geopolitical uncertainty accompanying some sanctions requirements as well as the fines running into the billions of dollars for breaches of the requirements (Standard Chartered's US$1.1bn fine imposed in April 2019 being a recent example).

Specific areas of regulation which are seen to pose the greatest challenge for the coming year were highlighted as:

- Bank Secrecy Act (BSA), United States
- California Consumer Privacy Act (CCPA), California, United States
- Common Reporting Standard (CRS), Global
- Community Reinvestment Act, United States
- Fair Debt Collection Practices Act (FDCPA), United States
- Financial Action Task Force (FATF) Recommendations, Global
- FINRA Rule 8210 Request (Information and document request similar to SEC subpoena), United States
- Foreign Corrupt Practices Act (FCPA), United States
- General Data Protection Regulation (GDPR), Europe
- Insurance Data Security Model Law, United States
- Managers-In-Charge Regime, Hong Kong
- Markets in Financial Instruments Directive (MiFID II), Europe
- Modern Slavery Act, United Kingdom
- Senior Managers and Certification Regime (SMCR), United Kingdom
- The Cyber Security Law of the People's Republic of China, China
- The Fifth Money Laundering Directive (5MLD), Europe
- The Payment Card Industry Data Security Standard (PCI DSS), Global
- The United States-Mexico-Canada Agreement (USMCA), United States, Mexico, Canada

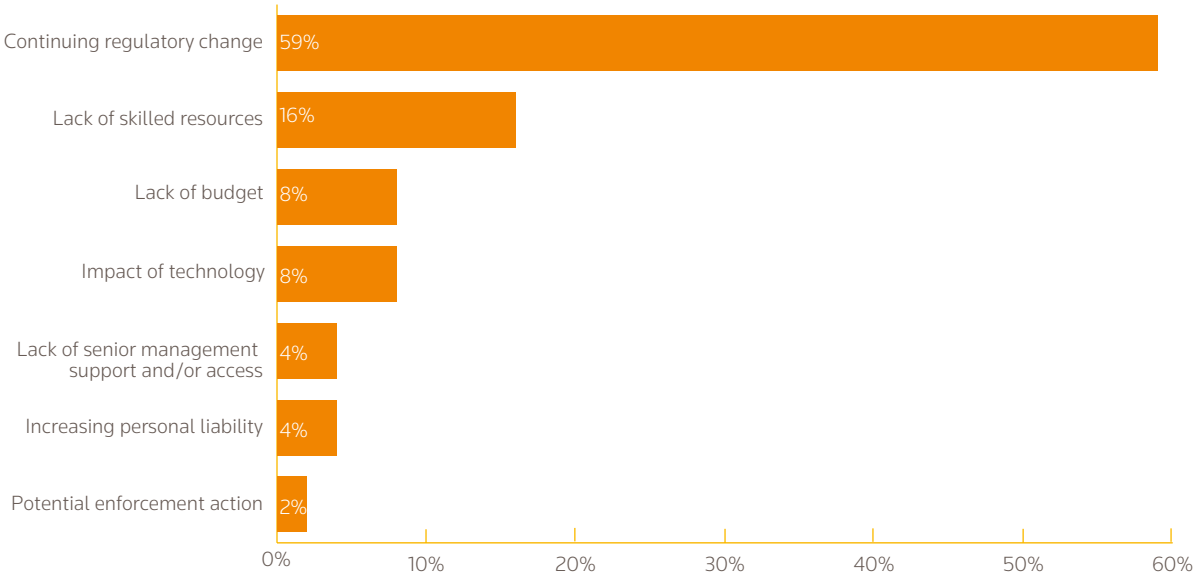
At the start of 2019, compliance practitioners across the world joined a series of live Thomson Reuters Regulatory Intelligence webinars on the compliance priorities for 2019, 10 Things Compliance Officers must do in 2019 . The results from 814 participants who took part in a live poll which asked: 'What is the single greatest challenge for compliance officers in 2019?' were in line with the challenges identified for the coming year by the cost of compliance survey respondents. In both the webinar polls and the cost of compliance survey, continuing regulatory change was singled out as the greatest challenge. Depending on the region, other key challenges included a lack of skilled resources, the impact of technology and, for Asia, a lack of budget.

TRRI webinar series, global poll question: What is the single greatest challenge for compliance officers in 2019?



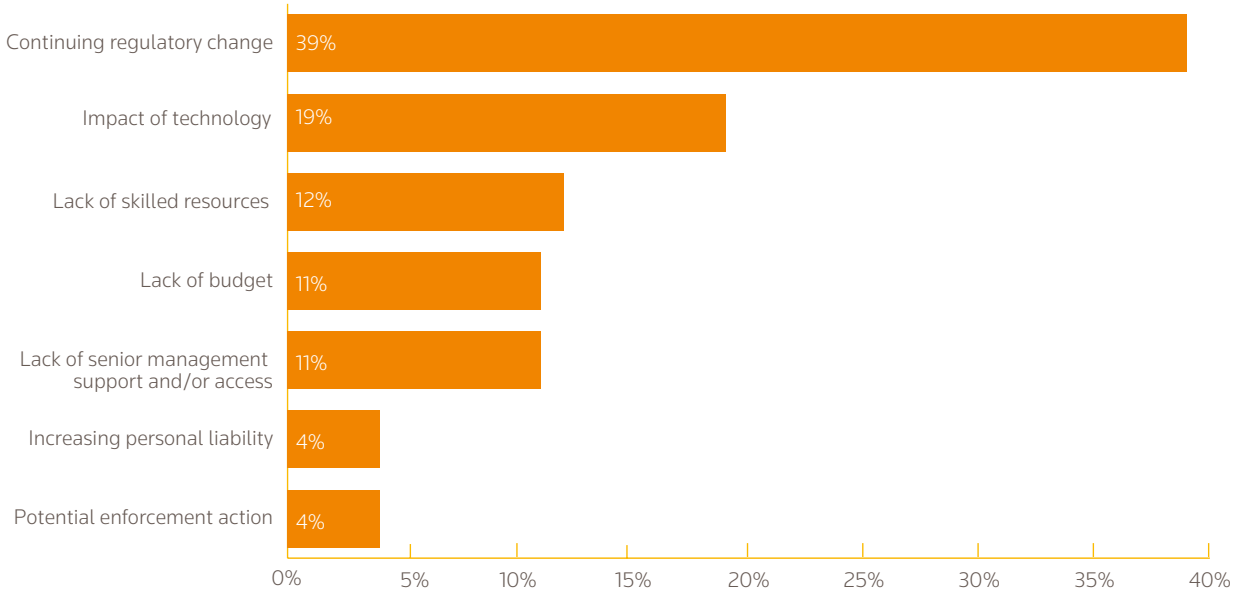
Source: Thomson Reuters Regulatory Intelligence – Cost of Compliance 2019: 10 years of regulatory change, by Stacey English and Susannah Hammond.

TRRI webinar series, APAC poll question: What is the single greatest challenge for compliance officers in Asia-Pacific in 2019?



Source: Thomson Reuters Regulatory Intelligence – Cost of Compliance 2019: 10 years of regulatory change, by Stacey English and Susannah Hammond.

TRRI webinar series, US poll question: What is the single greatest challenge for compliance officers in 2019?



Source: Thomson Reuters Regulatory Intelligence – Cost of Compliance 2019: 10 years of regulatory change, by Stacey English and Susannah Hammond.

"Many banks used the crisis as a baseline against which they measure progress. They feel confident that, given their bank managed to come through the crisis, they are well-placed successfully to complete the current organizational transformations. In short, they are setting the bar too low and underestimating the scale of the challenge ahead."

Derville Rowland, Director General at the Central Bank of Ireland. Speech, "Why culture matters: Insights from the Central Bank of Ireland Review of Behaviour and Culture in the Irish Banking Sector", at the European Banking Institute Global Annual Conference on Banking Regulation, Frankfurt (February 2019).

The greatest compliance challenge(s) the board expect to face in 2019 is/are...

Source: Thomson Reuters Regulatory Intelligence – Cost of Compliance 2019: 10 years of regulatory change, by Stacey English and Susannah Hammond.

Respondents were asked to identify the board's greatest compliance challenges for the year ahead. The top challenges for the board in 2019 were identified as:

1. Keeping up with regulatory change
2. Cyber resilience
3. Personal accountability
4. Culture and conduct
5. Financial crime, AML and sanctions

There has been a shift from 2018 when the top challenges for the board were identified as:

1. Continuing regulatory change
2. Enhanced supervisory scrutiny
3. Data privacy and GDPR
4. Cyber security
5. Balancing compliance and commercial demands

Perhaps the most telling change year-on-year is the perceived rise of personal accountability as a key challenge. The board along with other senior managers are, by deliberate regulatory policy design, more likely to be held accountable for their (in) actions and need to be prepared for the challenges associated with not only compliant activities but also being able to evidence that compliance.

What is the biggest change you predict for compliance in the next 10 years?

"Continued change of view that compliance is not a 'necessary evil' but an important cog in the running of a business and that they are seen as a solution provider to enable the business to meet its targets whilst remaining compliant."

Compliance Specialist, UK Bank
Survey respondent, Thomson Reuters Regulatory Intelligence – Cost of Compliance 2019.

PREDICTIONS FOR THE NEXT 10 YEARS

"Like our infrastructure peers we are challenged to maintain the integrity of existing operations while contending with a brave new world; constrained by the demands of cost recovery and limited resources; challenged by the multiplicity of risk and compliance frameworks with which to comply and governance and stakeholder bodies to satisfy; conscious that we have to defend across an extended front while our adversary need only find a single point of entry; and keenly aware that we must be perfect every day, our foe successful but once. These are heavy burdens; I speak not to you, but of you."

Richard Dzina, Executive Vice President at the Federal Reserve Bank of New York. Speech, "Four Questions on the state of Cyber Resilience and Endpoint Security", at the Clearing House and Bank Policy Institute's 2018 Annual Conference, New York City (November 2018).

What is the biggest change you predict for compliance in the next 10 years?

"Compliance qualifications having to be enhanced as compliance officers must familiarize themselves with ever changing fintech to stay relevant."

Senior Compliance Practitioner, Africa Investment Firm

What is the biggest change you predict for compliance in the next 10 years?

Source: Thomson Reuters Regulatory Intelligence – Cost of Compliance 2019: 10 years of regulatory change, by Stacey English and Susannah Hammond.

For the 10th annual cost of compliance survey report, respondents were asked to look into their crystal balls and predict the biggest change for compliance in the next ten years. The top five predictions for the biggest change over the next ten years were:

1. Automation of compliance activities
2. Continuing regulatory change
3. Enhanced role for compliance within the business
4. Culture & conduct risk
5. Technology risk

The ten years of the cost of compliance report have seen significant changes for compliance and the compliance function. The next ten years look likely to be equally substantive in terms of change. As with so many other compliance challenges, the automation of compliance activities will require skilled resources to ensure that the desired benefits can be gained. The automation process itself will require oversight and then continuing compliance monitoring will be required to ensure that the results of the automation can be relied upon. In theory, increasing automation should free up compliance resources to focus on more value-add, in person, compliance activities such as regulatory relationship management, lobbying and an enhanced role within the business.

Compliance officers themselves will need to keep changing with the times. Skillsets will need to remain under review and budget found for investment in the ever-evolving technology related knowledge and skills.

Comparison between the greatest compliance challenges expected in the year ahead and the greatest change predicted for compliance in the next ten years shows many similarities. Despite the immediate challenges being faced, compliance officers may well wish to consider how they can best prepare themselves and their firms for the possible future where they are likely to be even more essential to the success of their firms.

CLOSING THOUGHTS

"...the reality for many companies is that Brexit is already here. I would think that management and boards have not thrown up their hands in light of the uncertainties and declared that "nothing can be done" – they have been preparing for the variety of outcomes well in advance of March 29. Businesses have not been able to take a wait-and-see approach. Rather, they've had to prepare for a range of outcomes."

William Hinman, Director, Division of Corporation Finance at the U.S. Securities and Exchange Commission. Speech, "Applying a Principles-Based Approach to Disclosing Complex, Uncertain and Evolving Risks", at the 18th Annual Institute on Securities Regulation, London (March 2019).

The 10th cost of compliance survey report is the end of one era and the start of a new one. It has been 10 years since the resolution of the financial crisis and in that time, financial services firms, and their compliance officers, have changed radically. It would be safe to say that pre-crisis compliance functions often struggled to have a voice at the board table, that has now changed out of all recognition as boards are now not only much more risk and compliance aware but also have a better understanding of the fundamental importance of a well-resourced and skilled compliance function.

The rise of culture and conduct risk regulatory expectations, the 'how' as well as the 'what' and the use of judgement based supervision are not set out in a black and white rulebook but rather need the input of a skilled compliance officer to analyse and interpret the practical ramifications for the firm. In a similar vein, the introduction of accountability regimes which require the allocation of prescribed responsibilities for all senior managers is another area where the value added by a skilled compliance function has come to the fore. New ways of working are being adopted and increased recognition for the compliance function has become the new normal.

Technology, whether the implementation of fintech and regtech, or the possible threats posed by cyber-attacks, will continue to transform both firms and their compliance functions and will require the expansion of existing skill sets in all areas of a firm. Of potentially equal impact is the uncertainty created by geopolitical risk around the world. Former political co-operations and certainties are shifting creating potential fragmentation and will again require expert compliance skills to help navigate the challenges.

Compliance is an acknowledged core competency for a financial services firm and the cost of that compliance is the continued and consistent investment in appropriately skilled compliance resources and infrastructure. The TRRI cost of compliance research will continue to capture relevant industry insight to enable firms to develop and benchmark their approach and practices.

"...Banks have made large investments in top notch quantitative models that try to gauge the magnitude of risks. Although this does sharpen our focus, and is undoubtedly important, we must not allow it to cloud our intuition, the propensity we have for being alert to 'unknown unknowns', the dark matter of the financial universe. It was ten years ago that several dangerous developments collided in an explosive cocktail that saw the financial system on the brink of collapse. What will be the toxic ingredients of tomorrow?"

Frank Elderson, Executive Director of Supervision of the Netherlands Bank. Speech, "Changing gears – about cycling and the future of banking", at the Netherland's Bank banking seminar, Amsterdam (March 2019).

About the authors

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The new book Conduct and Accountability in Financial Services: A Practical Guide by Stacey English and Susannah Hammond is available now to purchase from Bloomsbury Professional. Use code TRRI1 for 15% discount.

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