

The state of

Financial Services Compliance

2022

→ Annual Compliance Health Check Report



SteelEye

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Foreword

This inaugural Compliance Health Check Report demonstrates the breadth and complexity of challenges facing today's compliance professionals. Regulatory change, a changing operational environment and growing data volumes are forcing firms to rethink their processes and procedures for regulatory reporting, trade and communications surveillance, record keeping, and more.

It is clear that firms are beginning to recognize the role technology can play in removing regulatory complexity, while helping compliance teams innovate and streamline their functions to suit the modern environment. Indeed, projections for the year ahead show almost half of firms anticipate an increase in RegTech investment, and a further 41% expect to invest the same as they did last year.

Despite 42% of respondents saying they find the regulator more challenging to deal with, 73% believe financial services firms are well equipped to handle more stringent regulatory rules over the next five years. Investment in technology might explain this sense of optimism.

Digitalization is well-underway for most large firms, 75% of whom have started investing in or have fully implemented technologies like artificial intelligence (AI) and machine learning (ML) in compliance. There is, however, a need to reach smaller firms, where uptake is lagging. Arguably it is these teams who are least equipped to adequately manage the challenges ahead.

Whilst challenges and priorities vary across firms of different sizes and those operating in different markets or in different verticals, across the board, all signs point to the increasingly important role of technology in solving compliance challenges in financial services.

As an industry under pressure to prove it has learned from its past mistakes, this is pivotal in handling the growing burdens that face the modern compliance professional.

I hope you enjoy the report.



Matt Smith
CEO, SteelEye

Executive Summary

The issues defining an increasingly complex compliance landscape in 2022

Firms continue to face significant compliance challenges amid regulatory uncertainty. Managing regulatory change is the most prominent challenge as firms strive to catch up with the speed of change whilst continuing to meet existing obligations.

Many of the challenges stem from difficulties around the effective management, consolidation, and normalization of data. Other challenges include managing market abuse risk and staff resourcing.

How compliance spending is shifting

A significant majority of firms are now investing more in compliance than they did five years ago, and some (10%) even claim that they're spending twice as much. Much of this spending is concerned with enhancing compliance processes to better meet regulatory obligations, prompting key investments in RegTech.

Use of Artificial intelligence and Machine Learning in compliance

Firms have started to address their compliance issues by implementing artificial intelligence (AI) and machine learning (ML) into their compliance processes and the majority of firms today are actively investing in these technologies. Those that have implemented AI are reaping the benefits - whereby all respondents who have fully implemented AI for compliance said that the quality of their Management Information (MI) has improved.

The compliance team of today

Compliance teams overall seem to favor a centralized compliance management structure. Centralized structures are more prominent in smaller firms. Larger businesses pivot towards partially or fully decentralized compliance management structures. Modern compliance teams are also saddled with repetitive administrative duties and results show that compliance overall is responsible for a sizable portion of a firm's overall expenditure.

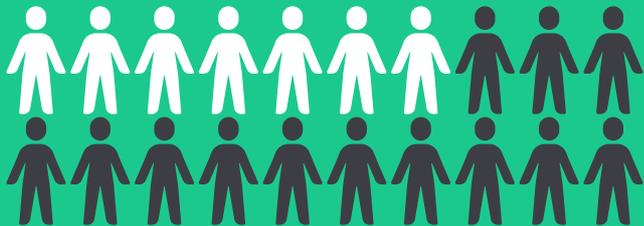
2022's Compliance Challenges and Priorities Overview

- ➔ **Biggest challenges in meeting regulatory obligations**
 - ➔ **Dealing with the regulator**
 - ➔ **Future focus - compliance priorities for the year ahead**
 - ➔ **Navigating a shifting international landscape**
-

KEY FINDINGS



Compliance challenges vary but managing regulatory change is the biggest challenge for 1 in 5 compliance teams.



34% of people have rated managing regulatory change and the implementation of projects as their top priority for the next 12-months.

2022's Compliance Challenges and Priorities

Biggest challenges in meeting regulatory obligations

The speed of regulatory change is leaving people behind

Firms are struggling to meet their compliance obligations amid continued regulatory uncertainty of the past few years – prompted by events such as Covid-19, the transition to hybrid working, the UK's EU withdrawal, and growing data volumes. 20% of respondents overall said that keeping up with regulatory change was their single biggest challenge in meeting their regulatory obligations today.

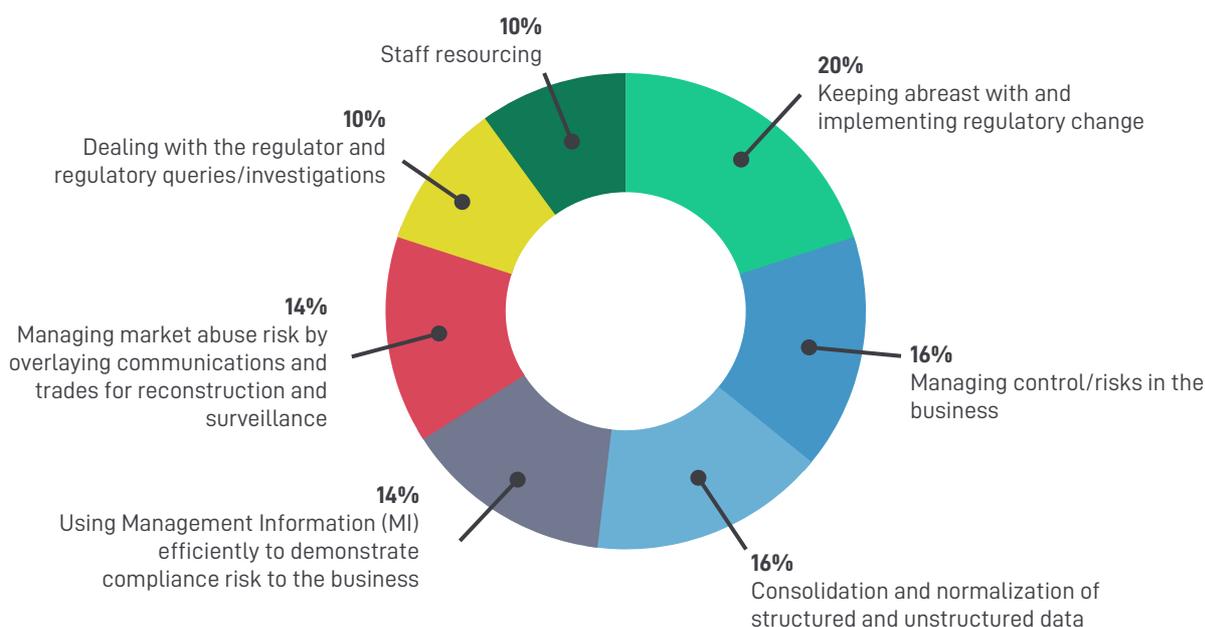
The pace of regulatory change following the Global Financial Crisis can still be felt today. While digitalization has brought many benefits to the financial services industry, new channels of communication and ways of working – such as remote and hybrid arrangements driven by COVID – have complicated the picture for compliance professionals seeking to ensure their firm is constantly meeting or exceeding regulatory obligations.

Data management is a significant pain point

Data management continues to be a major challenge. 44% of respondents selected either, "consolidating and normalizing data", "using MI to effectively demonstrate risk", or "managing market abuse risk by overlaying communications and trades" which all deal with the wider theme of data management.

This is not surprising given the fact that at the heart of all regulatory obligations is the need to bring together, analyze and store vast amounts of data for record keeping, reporting, oversight, and control. Compliance requires organizations to have a thorough command over their data.

What is the biggest challenge you face in meeting your regulatory obligations today?



2022's Compliance Challenges and Priorities

Biggest challenges in meeting regulatory obligations

Challenges vary by size and firm type

Managing regulatory change was more challenging for smaller firms at 32%. It was also one of the main challenges for medium-sized firms at 17%, but for large firms, the prominent challenge was using Management Information efficiently to demonstrate compliance risk, with regulatory change dropping down to 12.5%.

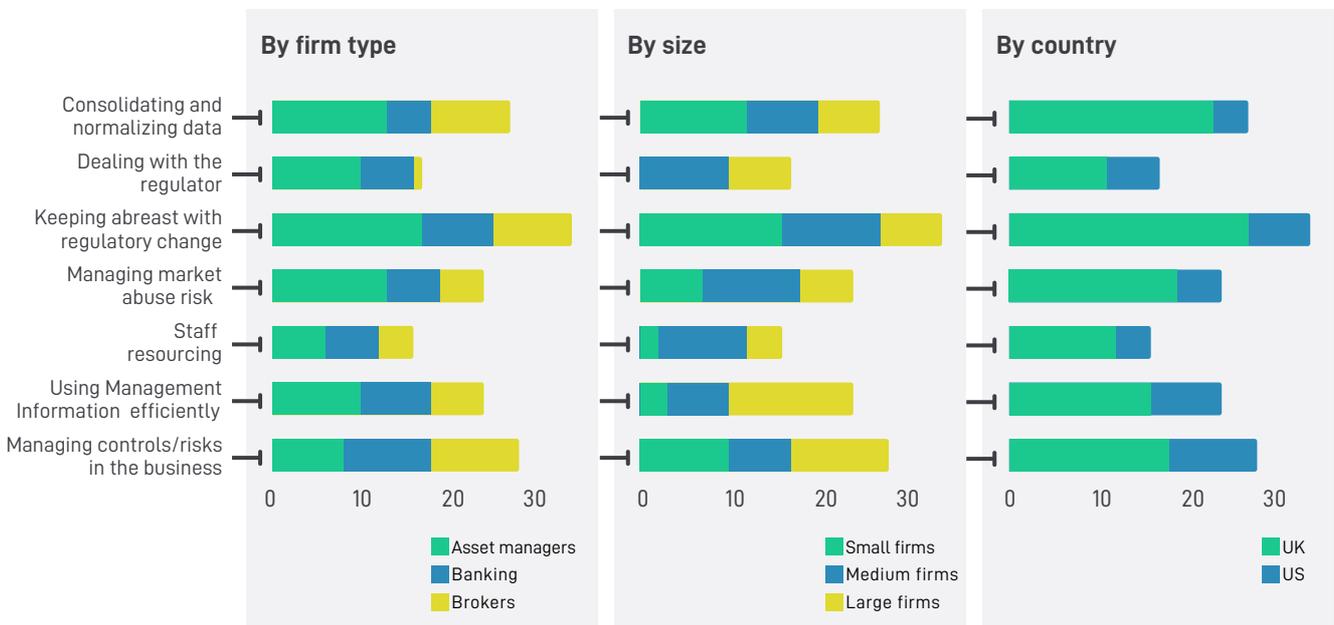
For asset managers, managing regulatory change is the biggest challenge at 22%, where banks and brokers were more concerned about managing controls/risks in the business.

When looking at regional splits, UK firms consistently ranked managing regulatory change as their biggest challenge whereas US data suggests that managing control/risks in the business was the biggest challenge.

The great resignation – not as bad as we thought

While there has been a marked shortage of talent across industries, staff resourcing emerged as a relatively manageable challenge in compliance, at just 10% overall. This could indicate that despite the wider industry struggles with staff resourcing and recruitment, technology is doing its job in helping firms to address the talent gap.

What is the biggest challenge you face in meeting your regulatory obligations today?



2022's Compliance Challenges and Priorities

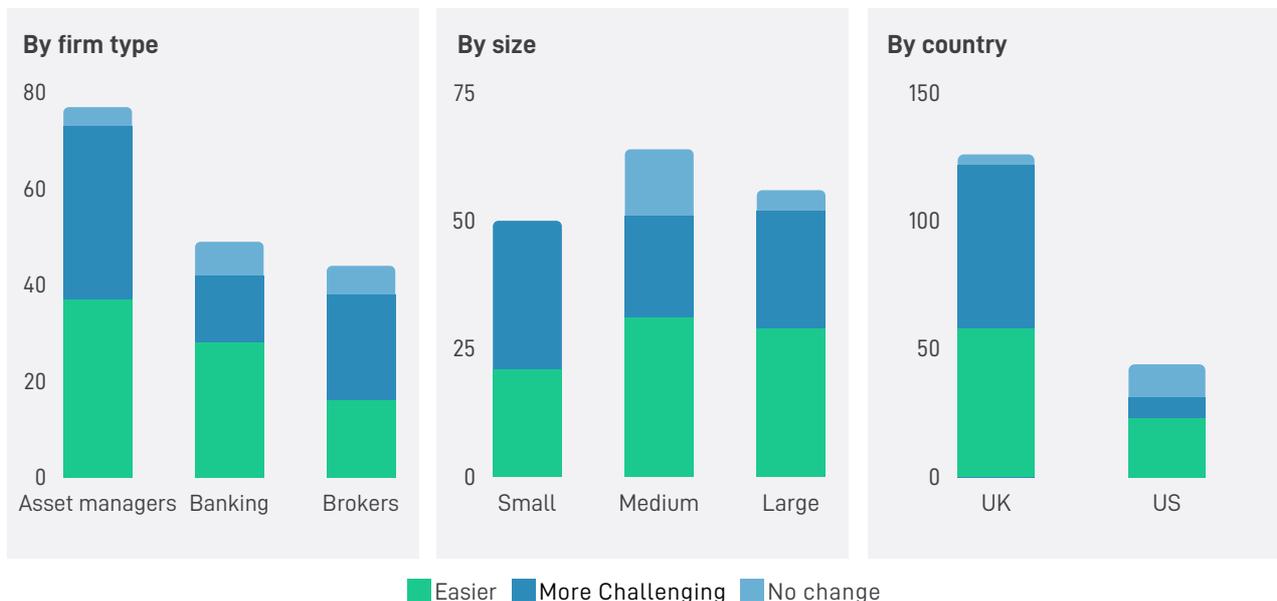
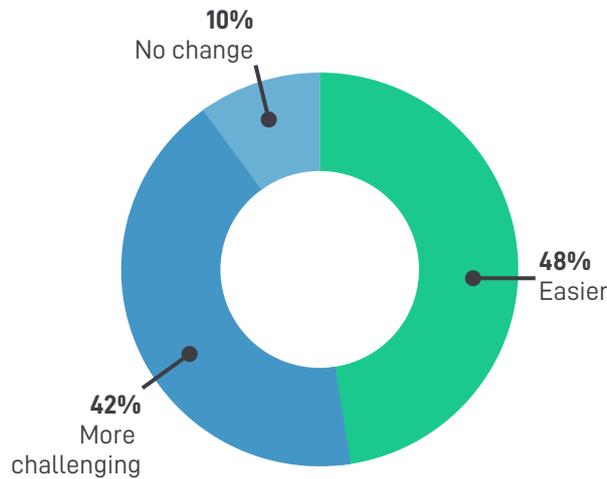
Dealing with the regulator

Dealing with regulators split opinions

The challenges around dealing with regulators split opinions evenly among our respondents. While 42% said regulators were now more challenging to deal with, 48% said they now find it easier than ever before. This could in part be due to technology making compliance processes more streamlined and straightforward.

The story becomes more mixed when looking at the size of a firm, with 58% of smaller firms finding it more challenging. It was also clear that US respondents found regulators easier to deal with, with under a fifth (18%) saying dealing with the regulator was more challenging compared to more than half (52%) in the UK.

In your opinion, is dealing with the regulator (FCA, SEC, FINRA, ESMA) easier or more challenging compared to five years ago?



2022's Compliance Challenges and Priorities

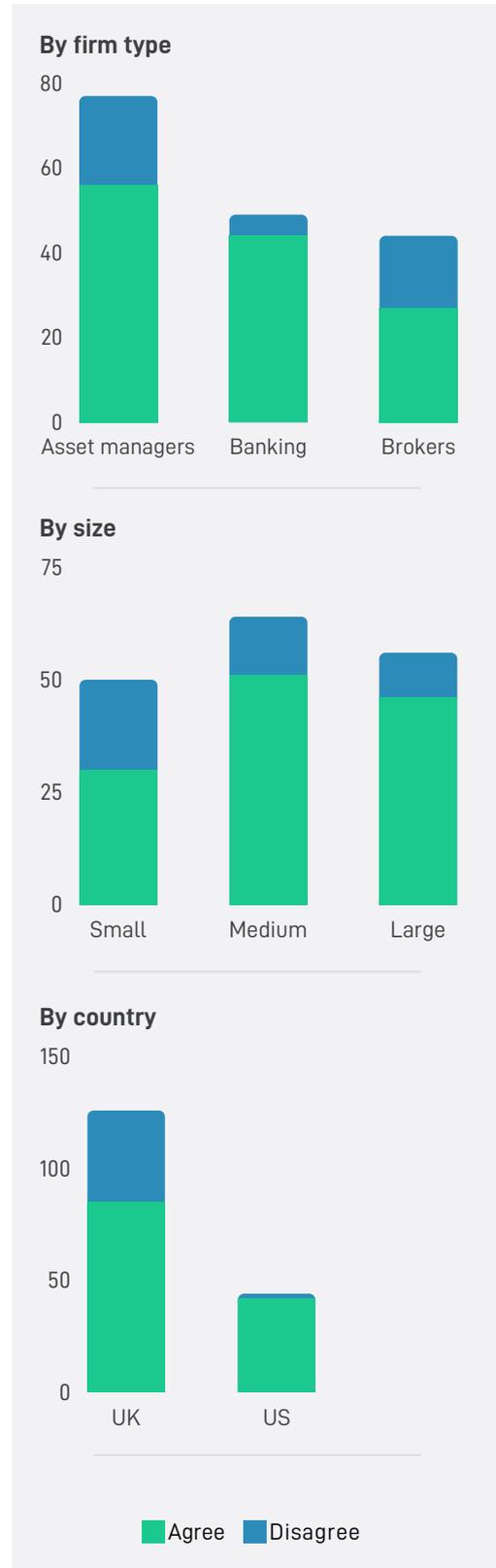
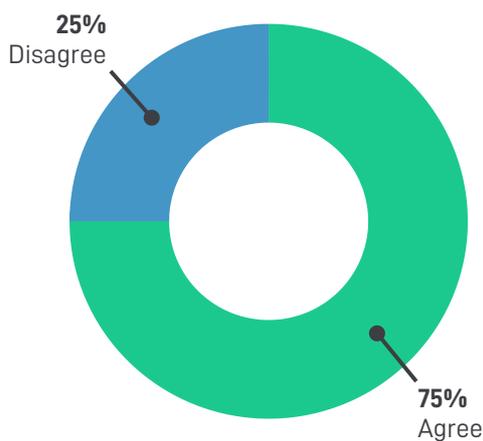
Dealing with the regulator

Some are more optimistic than others

While a majority of respondents (75%) agreed that financial services firms are in a good position to handle more stringent regulations over the next five years while 25% disagreed. Interestingly, only 5% disagreed with this statement in the US. These firms were all small or medium-sized broking firms.

30% of smaller firms don't believe that financial firms are well equipped to handle more stringent rules. When those firms were asked if they think dealing with the regulator is easier or more challenging compared to five years ago, 65% responded "more challenging". This goes hand in hand with the results presented on page 8 which suggest that smaller firms are more impacted by regulatory change. In addition, many small firms struggle with consolidating and normalizing data which impacts firms' ability to handle more stringent regulatory rules in the future.

Do you think financial firms are equipped to handle more stringent regulatory rules over the next 5 years?



2022's Compliance Challenges and Priorities

Future focus - compliance priorities for the year ahead

Data quality: a top priority for many firms

Data quality remains a core priority, with 36% of respondents saying it was key to improving Management Information (MI) and the information being provided to the board, management, and wider business.

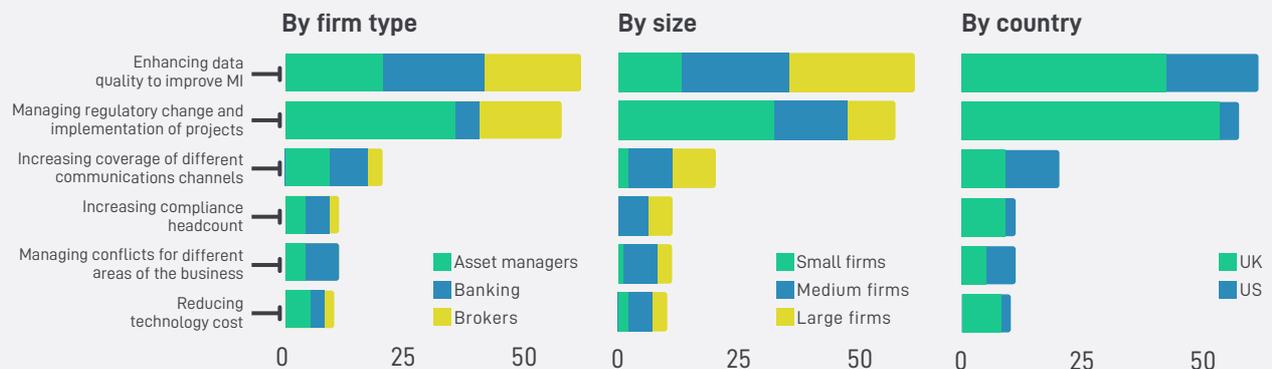
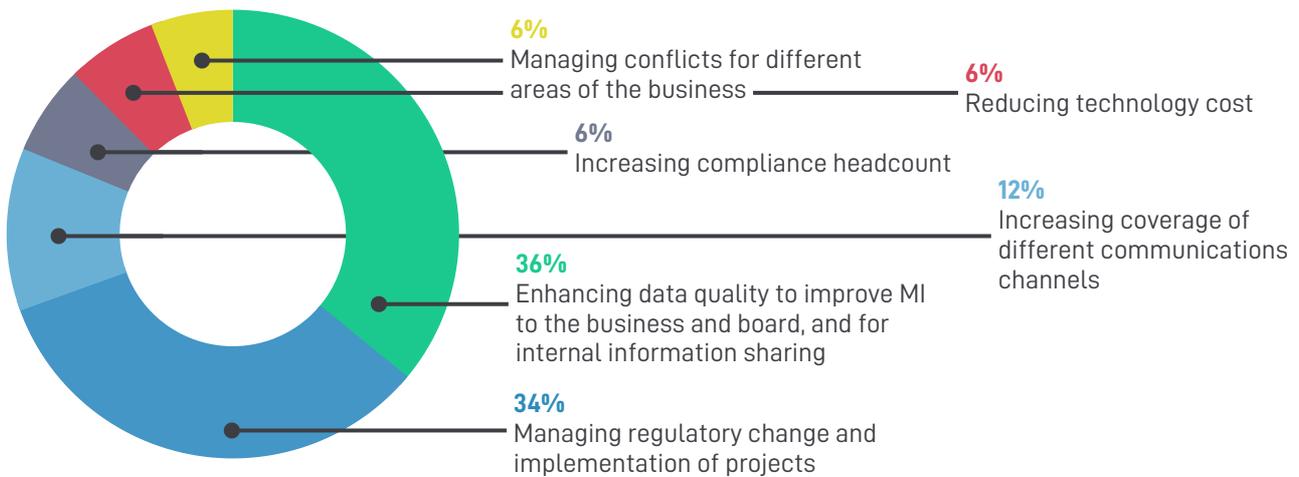
This is particularly true for asset managers and UK firms. In Europe, data quality under regimes like MiFID II has been an ongoing challenge so this is unsurprising. This priority links back to the challenges firms face, where challenges associated with data management were selected by 44% of respondents.

With a proliferation of data, platforms, and systems in use by financial institutions today, it is no surprise that many are focussing on how to bring data together accurately to improve information sharing. Investment in technology, systems, and internal processes has a major role to play in addressing data challenges.

A focus on managing UK regulatory change

The second highest priority - linking back to the challenges - was managing regulatory change and the implementation of regulatory projects, highlighting the impact legislative changes have on compliance teams.

In the next 12 months, what will be your main compliance priority?



2022's Compliance Challenges and Priorities

Navigating a shifting international landscape

In the UK, concerns around continued rule change remain

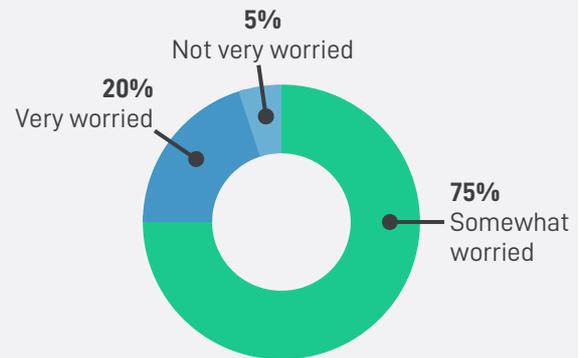
Despite being six years since the Brexit vote and more than two years since the UK formally left the European Union, the true impact on the financial services industry and its regulation remains unclear. 95% of firms said that they are either somewhat worried or very worried about future rules changes as a result of the split, of which 1-in-5 being 'very worried'.

As the UK reshapes its rulebook, one might wonder if this will make it easier for UK firms to meet their regulatory obligations. Certainly, part of the drive for deregulation is to make the UK financial markets more attractive globally. And while many of the UK regulators' changes are welcomed by the financial services industry, these changes do create an additional layer of complexity for firms that operate in both the UK and the EU, in that they now have to comply with two sets of rules that remain complex and are diverging.

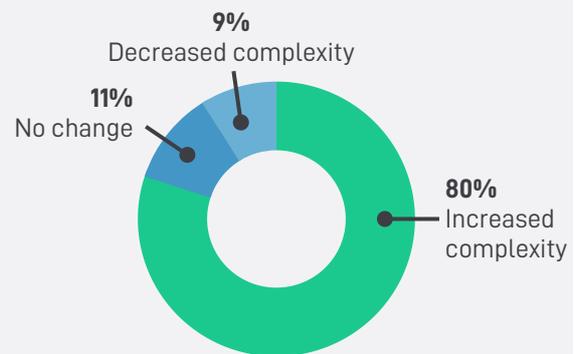
Brexit has spared some and burdened others

Of those firms who said they had already been impacted by Brexit, a majority (71%) said it has increased the costs of their compliance function. Regardless of cost, 80% said the complexity of their compliance operations had increased – an impact that could be increased further in the coming years.

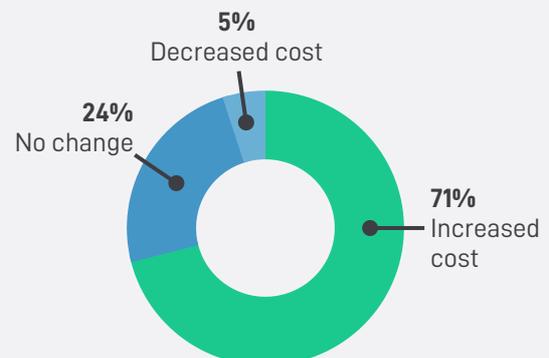
How worried are you about future rule changes post-Brexit?



How has Brexit impacted the complexity of compliance?



How has Brexit impacted the cost of your compliance operations?



Investment and Expenditure

Overview

- **Compliance costs have increased in the last five years**
 - **Technology investment is a key cost driver**
 - **Regulatory reporting, communications monitoring and trade surveillance are key investment areas**
-

KEY FINDINGS



88% of firms said costs have risen in the last five years, some significantly



44% expect to spend more on RegTech in the next 12 months

Investment and Expenditure

Compliance costs have increased in the last five years

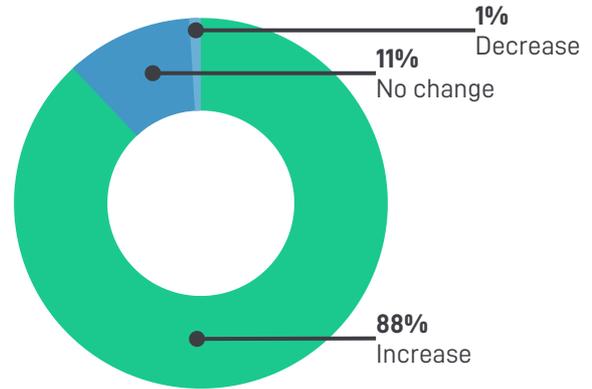
88% say costs are on the rise

The clear message from respondents was that compliance costs are rising, with 1-in-10 saying compliance expenditure has doubled or more over the past five years and just 11% saying it had remained flat. The impact was even higher for larger firms, with 94% reporting increased costs.

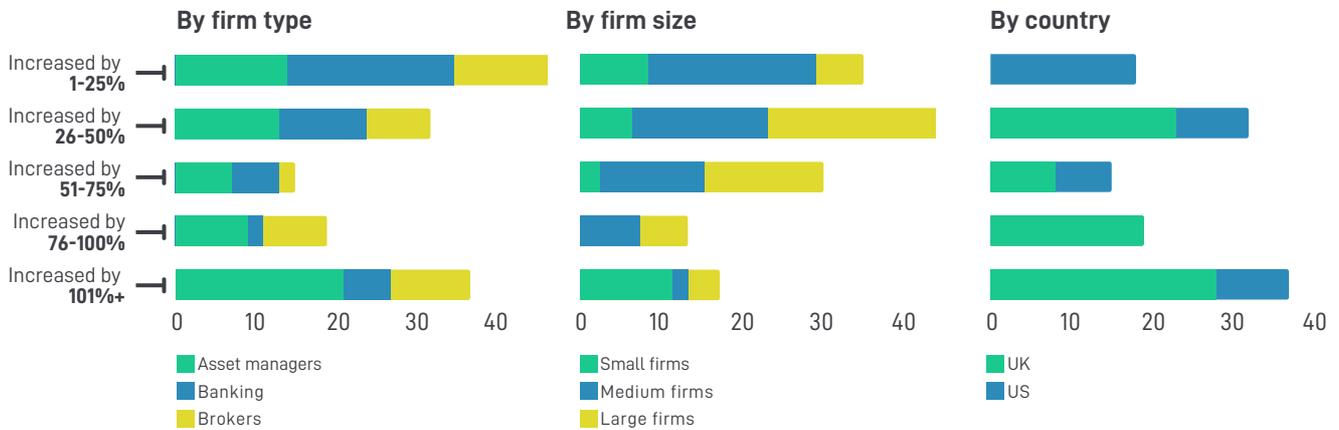
Compliance costs among US-based firms have risen most, with 4-in-5 respondents (77%) reporting increases in compliance expenditure of more than 25% over the last five years.

This compares to 56% in the UK who had seen similar increases in spend. However, this figure increases to 79% of large firms in the UK, reflecting the added complexities post-Brexit over the period.

How has your firm's Compliance expenditure changed over the last 5 years?



How much has your compliance expenditure increased by in the last 5 years (if it increased)?



Investment and Expenditure

Technology investment is a key cost driver

Investments into RegTech are driving costs

Investment in technology was the biggest cost item, according to 45% of firms. This was closely followed by "more regulations to deal with" which was selected by 37% of firms. Hiring and retaining talent followed closely behind at 34%.

There is no doubt that the pandemic has had a notable impact on these factors – with firms being forced to invest in new systems to account for the challenges of hybrid working while adjusting to new and changing regulations. At the same time, the COVID-driven shift in many people who have reassessed their career priorities - leading many people to leave the industry.

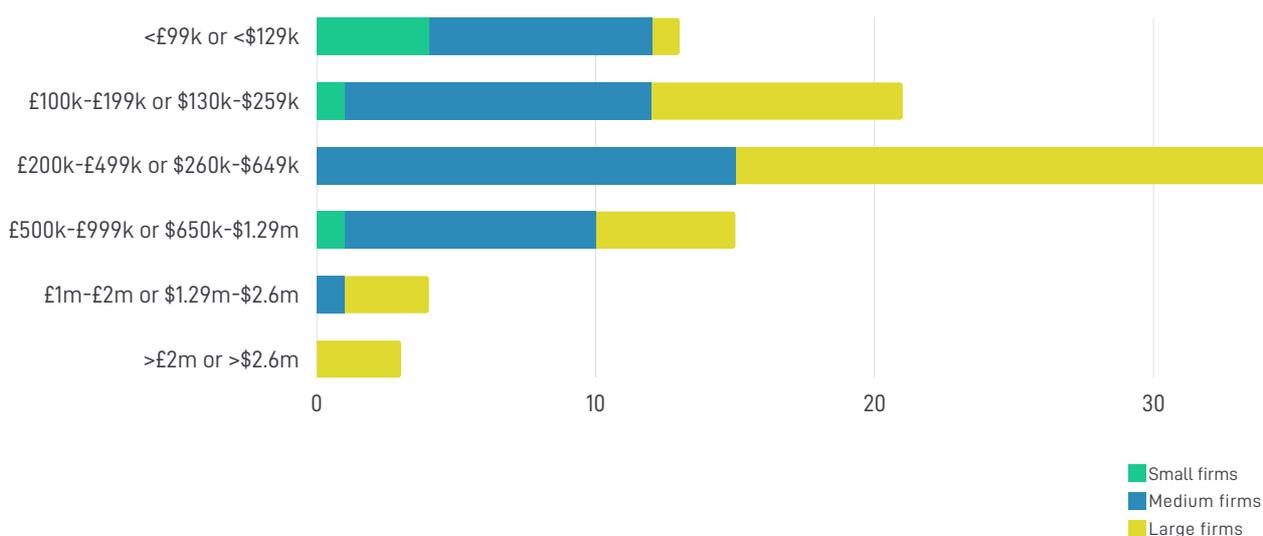
What do you think is driving up these costs? (select all that apply)

- Technology to support day-to-day processes?
45% agree (76 respondents)
- Hiring and keeping the right talent?
34% agree (58 respondents)
- More regulation to comply with?
37% agree (63 respondents)
- Fines?
12% agree (21 respondents)

RegTech spend

RegTech spend is reflective of firm size but varies from firm to firm. Most respondents who answered this question spend between \$260k and \$649k per annum on RegTech. Only a handful of firms spend over \$2.6m on RegTech, all of which were large firms.

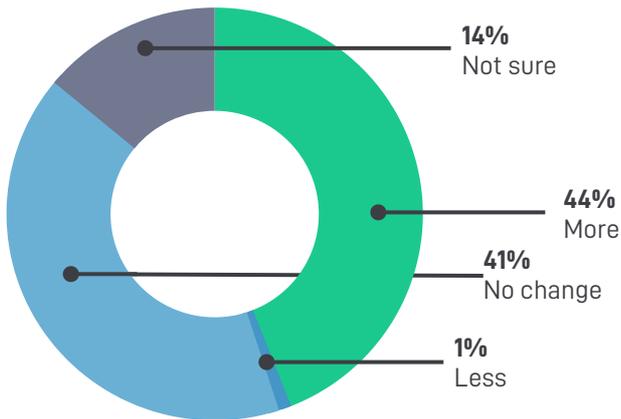
How much did your firm spend on Compliance technology (RegTech) in the last 12 months? (select best match)



Investment and Expenditure

Regulatory reporting, communications monitoring and trade surveillance are key investment areas

Do you expect to invest more or less in RegTech in the next 12 months?



44% of firms expect to invest more in RegTech in the next 12-months

Investment in technology is growing for most firms to support the increasingly challenging regulatory landscape.



Financial firms clearly recognize that sustained or increased investment in RegTech is key to addressing the challenges brought on by today's increasingly complex regulatory landscape.

Carrie Whamond, Founding Partner
AlternitOne

Regulatory reporting and trade surveillance are top priorities overall

When asked about their top two investment priorities, regulatory reporting was the most widely selected priority overall (selected by 86 respondents) followed by trade surveillance (78) and communications surveillance (70).

Holistic surveillance?

Nearly a quarter (24%) of small firms said holistic surveillance was a priority. This compared to just 7% of large firms and 9% among medium-sized firms, pointing to the differences in the execution of compliance strategies between firms of different sizes.

This is not surprising when you consider that compliance within larger firms is often decentralized whereas it tends to be more centralized within smaller firms (see page 25), therefore making holistic surveillance easier to execute.

What are the top investment priorities for your compliance team?

(SELECT UP TO TWO)

	RR	TR	CS	DS + RK	HS	Total
RR	5	25	25	23	8	86 (27%)
TR	25	7	21	16	9	78 (25%)
CS	25	21	7	15	2	70 (22%)
DS + RK	23	16	15	5	2	61 (19%)
HS	8	9	2	2	0	21 (7%)
	86 (27%)	78 (25%)	70 (22%)	61 (19%)	21 (7%)	

RR = regulatory reporting
 TR = trade surveillance
 CS = communications surveillance
 DS+RK = data storage and record keeping
 HS = holistic surveillance

Investment and Expenditure

Regulatory reporting, communications monitoring and trade surveillance are key investment areas

Regional differences and different business types impact priorities

Out of all UK respondents (126 in total), 57% listed regulatory reporting as one of the top two priorities. This was followed by trade surveillance at 49%. Out of the 44 US respondents, 50% listed communications surveillance as one of the top two priorities followed by trade surveillance at 43%.

For large firms, regulatory reporting and communications surveillance were selected as the top two priorities. This was the same among small firms. However, among medium-sized firms, trade surveillance followed by communications surveillance were the two most popular options.

For asset managers, regulatory reporting and communications surveillance were the top priorities.

For banks, communications surveillance was the leading selection followed by regulatory reporting. For small firms this regulatory reporting remained the most popular option followed by communications surveillance.

Communications compliance a focus in the US and for banks

It is unsurprising that communications surveillance was listed as a top priority, especially in the US and among banks given the fact that regulators in US jurisdictions are clamping down hard on communications rules.

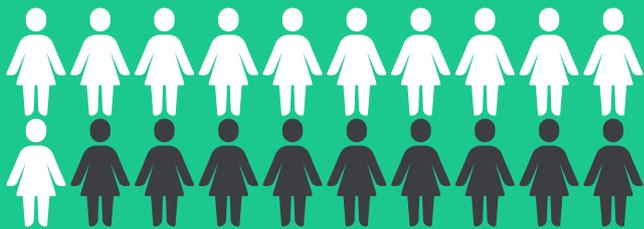
Last year's headline-grabbing \$200 million fine for J.P. Morgan by the Securities and Exchange Commission (SEC) demonstrated the importance of adequate monitoring of employee communications.

		INVESTMENT PRIORITY 1	INVESTMENT PRIORITY 2
By country	UK firms (126)	Regulatory reporting (72)	Trade surveillance (62)
	US firms (44)	Communications surveillance (22)	Trade surveillance (19)
By size	Small firms (50)	Regulatory reporting (21)	Trade surveillance (18)
	Medium firms (64)	Trade surveillance (36)	Communications surveillance (28)
	Large firms (56)	Regulatory reporting (28)	Communications surveillance (25)
By firm type	Asset managers (77)	Regulatory reporting (41)	Trade surveillance (37)
	Banks (49)	Communications surveillance (24)	Regulatory reporting (23)
	Brokers (44)	Trade surveillance (25)	Regulatory reporting (24)

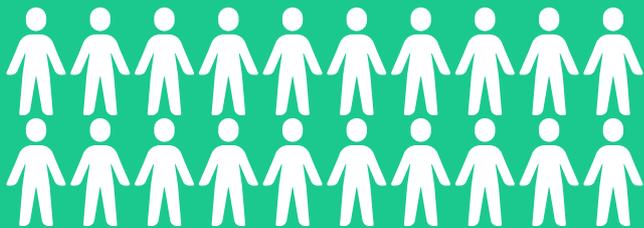
Artificial Intelligence and Machine Learning Overview

- ➔ The majority of firms are investing in AI and ML in compliance
- ➔ Larger firms and US companies are ahead of the curve

KEY FINDINGS



Over half of the respondents said that they have invested in or implemented AI or ML for compliance.

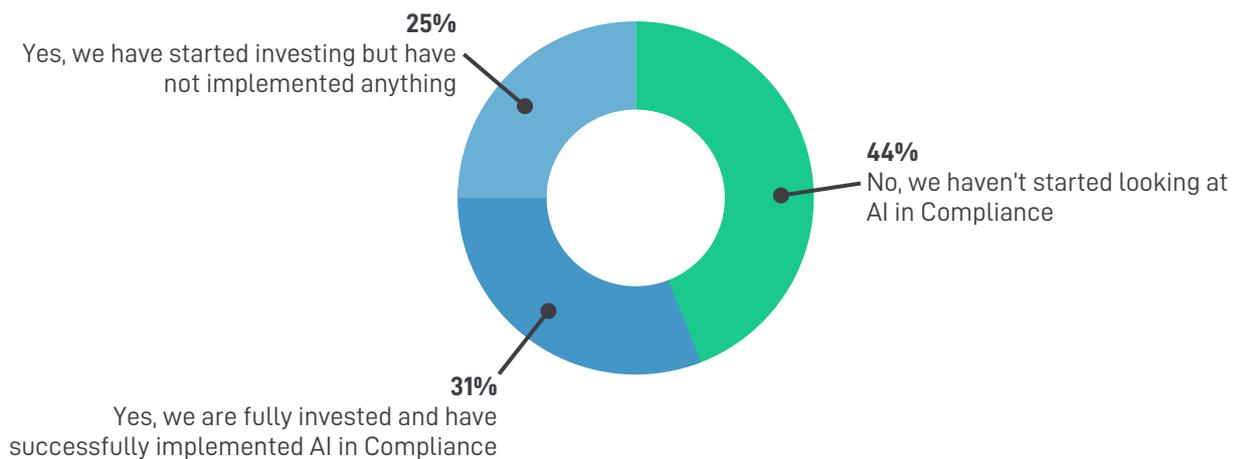


Among the firms that have invested in AI/ML for compliance, 100% have seen an improvement in the quality of ML.

Artificial Intelligence and Machine Learning

The majority of firms are investing in AI and ML in compliance

Have you implemented any Artificial Intelligence / Machine Learning capabilities to improve Compliance processes?



Many compliance teams have not yet realized the value of AI, but those that have are reaping the benefits

Many firms are not yet taking advantage of the potential of AI. Almost half (44%) said they had not even looked at AI's possibilities for compliance. Just over a quarter (25%) said they are investing in the technology, and 31% of firms said they had successfully implemented a degree of AI or ML into their compliance processes.

Those that have implemented AI are reaping the benefits – 100% of those who said they had invested in this area agreed they have seen a marked improvement in the quality of their Management Information.

Since investing into AI / ML for compliance, has your business seen any improvement in the quality of MI?



Artificial Intelligence and Machine Learning

Larger firms and US companies are ahead of the curve

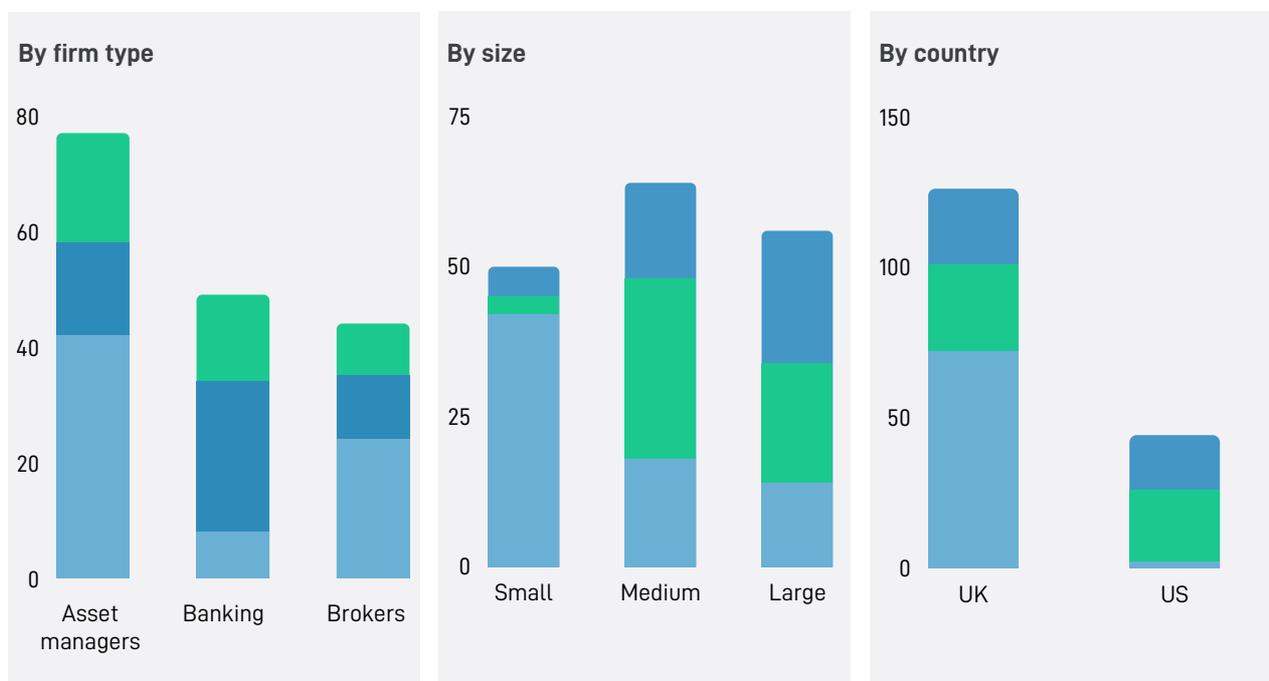
Larger firms are leading the way

Large firms are, perhaps understandably, further along in that journey. Three quarters (75%) have already invested in or fully implemented AI and ML in their compliance processes, in comparison to just 16% of small firms.

US firms are comparatively faster adopters too – with a huge 95% already looking at AI and ML compared to just 53% of UK firms.

One issue with AI and ML deployments is that a strong data foundation is crucial before a business can effectively make sure of these technologies. Without that foundation, AI will almost certainly fail to deliver on its intended purposes. Those organizations that establish a strong base of high-quality, centrally managed data – itself a major challenge for firms, as outlined earlier in this report – will see the greatest benefits from AI implementation.

Have you implemented any Artificial Intelligence / Machine Learning capabilities to improve Compliance processes?



- No, we haven't started looking at AI in Compliance
- Yes, we have started investing but have not implemented anything
- Yes, we are fully invested and have successfully implemented AI in Compliance

The Compliance Team of Today

Overview

- ➔ Administrative and repetitive tasks dominate compliance professionals' work
- ➔ Compliance is responsible for a sizable portion of expenditure
- ➔ Firms favor centralized management of compliance

KEY FINDINGS



Half of respondents said that at least 50% of compliance staff at their firm handle administrative or repetitive tasks.



Three-in-ten compliance teams say that they are responsible for over half of their firm's total expenditure.

The Compliance Team of Today

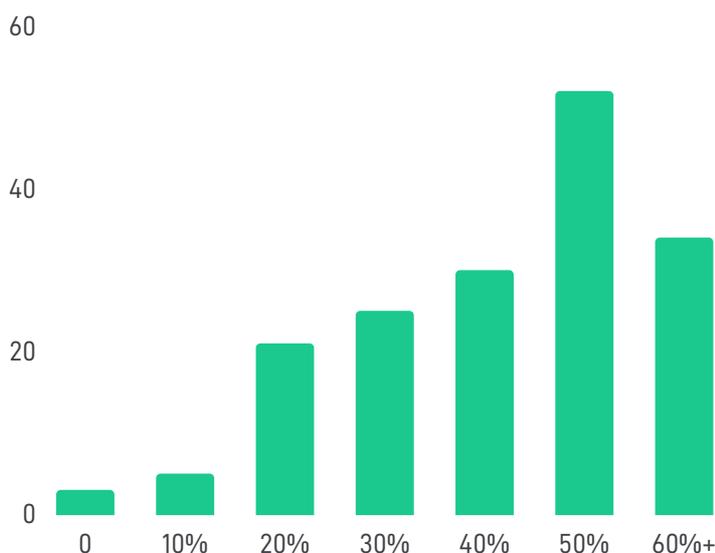
Administrative and repetitive tasks dominate compliance professionals' work

Over half of compliance tasks are administrative/repetitive according to 50% of firms

Despite the quick pace that technology has evolved, many compliance teams are still handling large quantities of repetitive tasks – often a product of some combination of outdated processes, untailored systems and legacy technology.

Half (50%) of respondents said that at least 50% of compliance staff handled repetitive or administrative tasks within their firm, with 20% of respondents saying 60%+ of staff within their team handled work of that nature. It is well understood that the financial services industry as a whole – where innovation has historically lagged behind many other sectors – is yet to fully realize the efficiency gains of digitalization, where technology-led solutions can free-up compliance time so they can focus their efforts elsewhere.

What percentage of Compliance staff do administrative/repetitive tasks at your firm?



“It is unsurprising that repetitive tasks make up such a large proportion of compliance professionals' work today. However, increased investments in RegTech and AI - which many firms are prioritizing - will help teams automate key processes to free up time and resource.”

Carrie Whamond, Founding Partner
AlternitOne

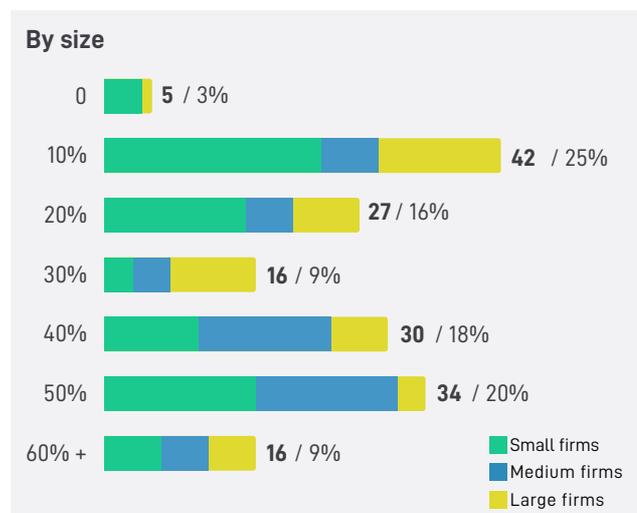
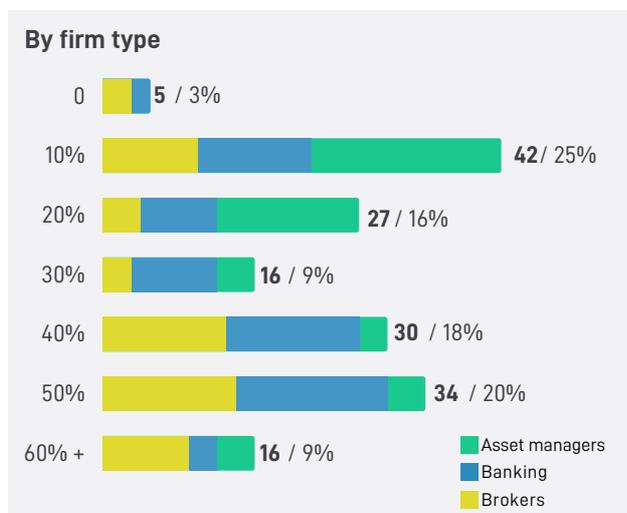
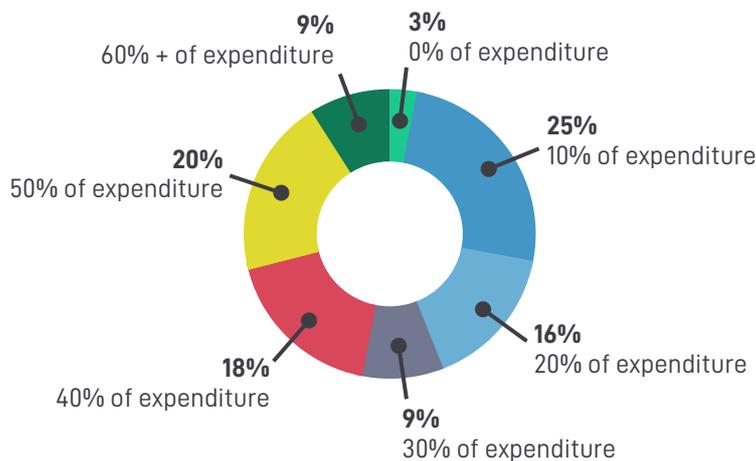
The Compliance Team of Today

Compliance is responsible for a sizable portion of expenditure

Complete compliance demands investment

Nearly a third (29%) of respondents said that compliance was responsible for more than half their firm's total expenditure. For large firms, this goes up to 41%, whereas for small firms it drops to 16%. The results show that banks have the biggest compliance budgets, with 38% of respondents from banking firms saying their team is responsible for half their organization's expenditure, in comparison to 29% of buy-side firms and 20% of brokers.

What percentage of your firm's total expenditure is Compliance responsible for?



The Compliance Team of Today

Firms favor centralized management of compliance

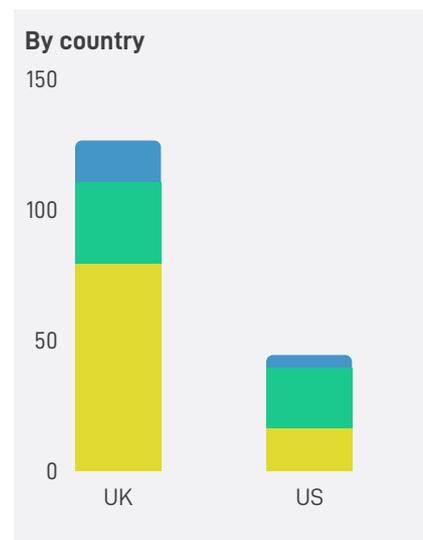
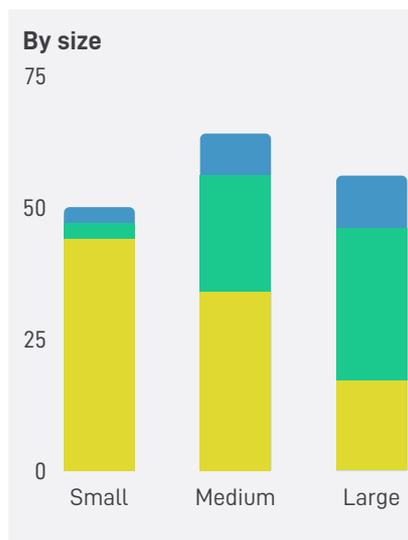
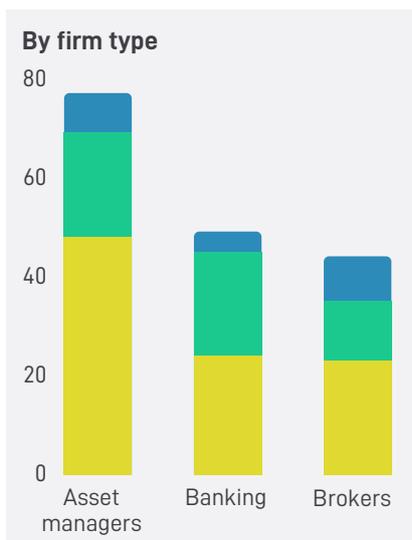
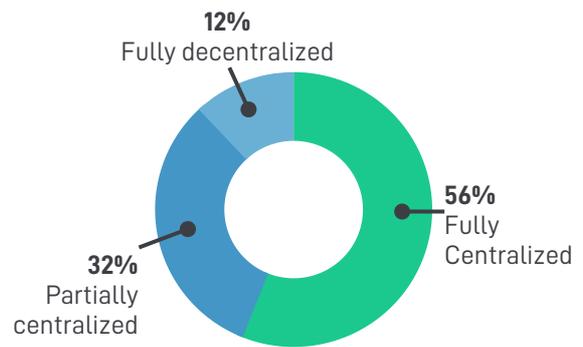
56% of firms have a centralized structure for compliance management

A majority of respondents (56%) maintain a centralized structure for compliance in which one team oversees all branches and regions in which the company operates. This provides a high level of control and consistency, but can also create challenges in dealing with regulatory nuance across different localities.

Meanwhile, just 12% said they deploy a decentralized model where compliance is managed directly within individual jurisdictions. This is understandably more common for large organizations at 18%. In contrast, 88% of small firms' compliance management is fully centralized.

Compliance teams can sometimes be siloed due to differences in local laws and regulations. However, this can naturally lead to problems like data silos or duplicated data points. Centralization of the compliance function can enable businesses to be more strategic and allow for richer learning about operations. However, that hinges on a strong data foundation for the business as a whole, to extract the full value of these learnings.

How does your company manage Compliance?



■ Fully centralized ■ Partially centralized ■ Fully decentralized

Conclusion

The financial compliance landscape is fast-moving and continually evolving. This is driven by the fast rate of change in the industry. We are constantly seeing new asset classes, trading behaviors, communications channels, and ways of working emerge, which regulation needs to incorporate.

Let's not forget that many of the market abuse behaviors firms are required to monitor for today were once genuine trading strategies. So, it is hardly surprising that managing regulatory change is a key challenge for many compliance teams today.

Technology and data are key to establishing future-proofed compliance processes and procedures. By prioritizing how to bring together disparate datasets and make better use of data - be that for MI or internal information sharing - firms can more easily address regulatory change and other compliance challenges that will emerge down the line. It is therefore great to see that a large proportion of firms view the enhancement of data quality as a top priority and that most firms are actively investing in technology.

While there is always room for improvement, particularly in an industry that has traditionally lagged when it comes to digitalization, compliance teams increasingly view technology as a key solution to their compliance challenges. In fact, 85% expect to invest the same amount or more in RegTech in the next 12-months. It is also astonishing that over half of firms that took part in this compliance health check survey have started investing in AI for compliance, with one in three having fully implemented elements of AI.

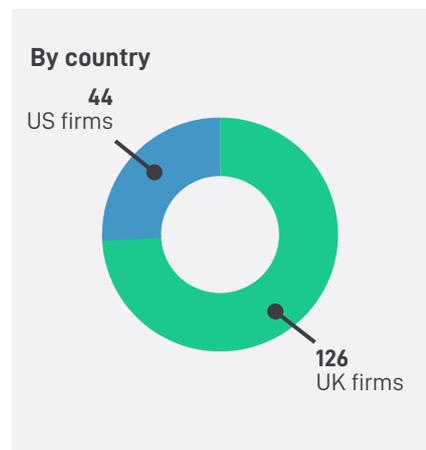
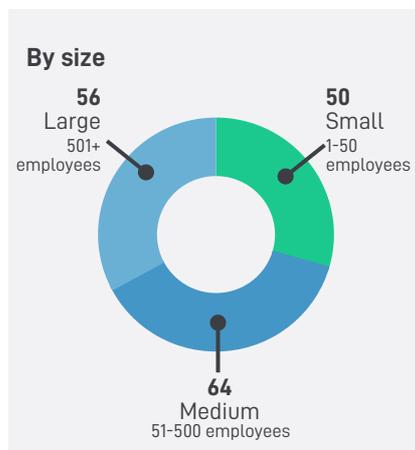
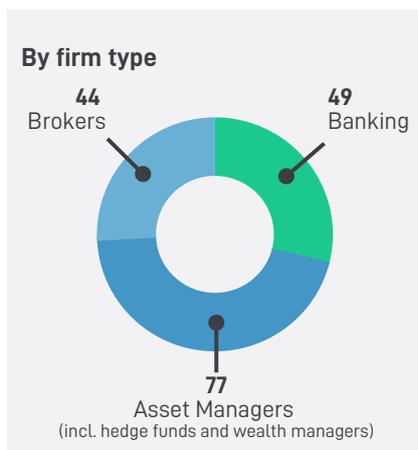
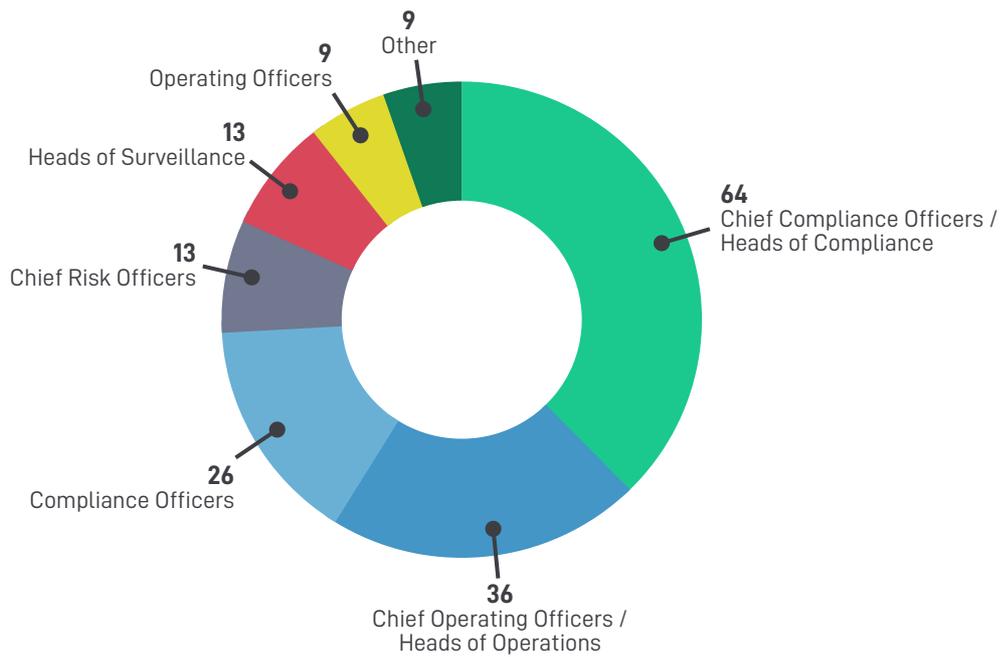
We are hopeful that these investments will enable compliance teams to improve the efficiency of their compliance programs - thereby reducing their reliance on administrative and repetitive tasks. Doing so can enable the compliance function to pivot from reactive investigations and firefighting to a more proactive model for compliance management and risk detection.

Methodology and Definitions

The report has surveyed 170 senior compliance decision-makers in financial services across the UK and US. 80 responses were collected using OnePoll between January and April 2022. 90 responses were collected by SteelEye between October and December 2021. All survey responses were anonymous but have been thoroughly vetted to ensure the authenticity of the research. Below are the splits.

170

respondents





→ Annual Compliance Health Check Report

