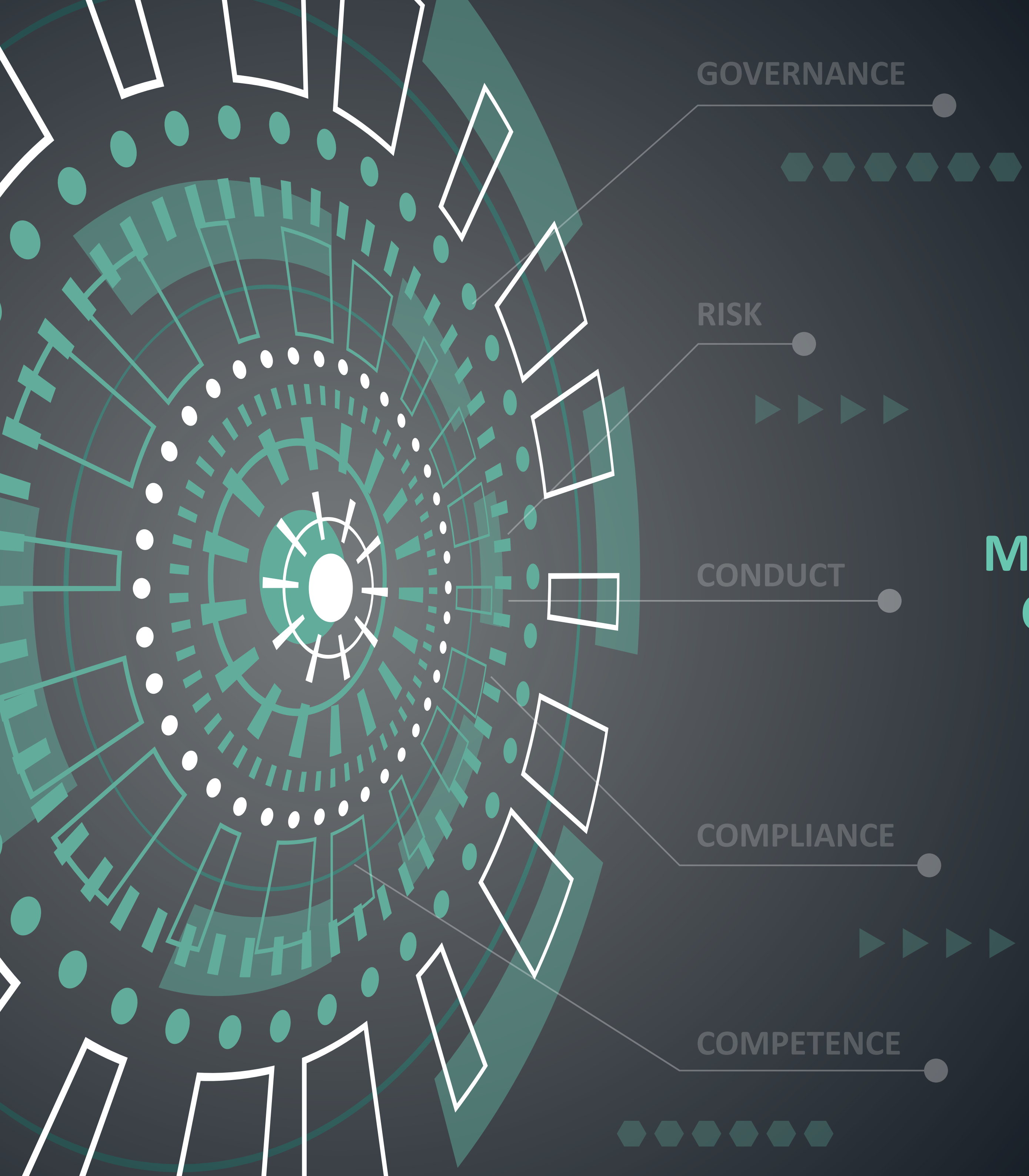


MODELOFFICE
compliance · alignment · sustainability

Model Office-MO® Cost of Compliance Survey 2022

www.model-office.co.uk

Contents

The FCA: a data led regulator

'The FCA will become a different type of regulator...our regtech systems monitor transactions and spot outliers that could suggest fraudulent behaviour. We are already working on automated systems for our threshold permissions. And our organisation has moved to the Cloud and revolutionised the ease with which we can access vital data to prevent financial crime and protect consumers. We have migrated more than 52,000 firms and 120,000 users to our RegData platform, which grants access to flexible and scalable data collections....Regulators will have to ensure that firms can show not just how data was gathered or stored or used, but why it was decided it was important in the first place and how they avoid it being used to discriminate against minorities and people with other protected characteristics.'

Nikhil Rathi, FCA Chief Executive

1. Introduction

Model Office-MO® has conducted its latest annual survey across retail investment advice (RIA) firms' key compliance concerns, challenges and opportunities. This survey generated responses across 70 firms who are engaged with Model Office RegTech and a further 50 who are not. The survey questions were designed to produce a comprehensive view on where RIA firms are post pandemic and how their recovery is taking shape, and if they view adoption of RegTech as not only supporting their ongoing governance, risk and compliance (GRC) challenges, but also supporting new hybrid working which is forcing firms to reassess their approach to GRC.

Survey trends and themes

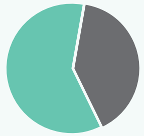
Regulatory challenges

1 in 3 firms are concerned about attracting the right skilled resources to the compliance department/ function

1 in 3 are concerned about regulatory enforcement

1 in 4 are concerned about the speed of regulatory change and lack of RegTech awareness/adoption

100% are concerned about the implementation and impact of the Consumer Duty, with only 1 in 4 confident that the October 31st deadline has been met



More than **50%** are concerned about a demonstrable compliance culture

ESG and climate change is a concern with more than **70%** of firms unsure how to expand suitability requirements to incorporate client sustainability preferences

When asked what the regulatory challenges are, our survey said...

Automation and standardisation
Financial crime and sanctions compliance
Geopolitical risk
Anti-money laundering compliance and supervision
Growing regulatory expectations
Financial crime and sanctions compliance
Legacy software development
Availability of skilled resources
KYC and digital onboarding
Accelerated digital transformation
Operational resilience
Compliance training
Consumer duty
Strategic review of existing compliance programmes
Tax compliance
Investment in technological solutions
Remote capabilities
Strategic review of existing compliance programmes
Conduct risk
Lack of budget and resources
Culture
Business growth
Cyber resilience
Crytocurrencies and digital assets
Volume and implementation of regulatory change
Increase in products and services offered
Effective compliance monitoring
Employee burnout
Data security
ESG and climate risk management
Meeting customer expectations
Senior management buy-in
Increasing cost
Balancing compliance and business needs
Remote capabilities

	Compliance time	Compliance cost: Direct as % of revenue	Compliance cost: Indirect as % of revenue
RIAs with **1-10 RIs**	*Spend* **4-6 Hours** per week	*Spend* **2-5%**	*Spend* **2-4%**
RIAs with **11-20 RIs**	*Spend* **8-13 Hours** per week	*Spend* **6-8%**	*Spend* **7-9%**
RIAs with **20+ RIs**	*Spend* **15+ Hours** per week	*Spend* **10-13%**	*Spend* **9-10%**

Reasons for costs

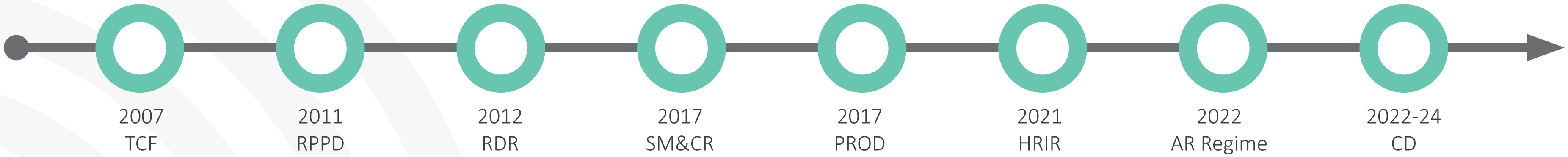
70% say it's professional indemnity insurance

1 in 2 feel compliance officers and staff contribute significantly

1 in 3 point to paraplanning, administration and third-party support

2. Increasing demand for compliance risk oversight

Consumer protection regulations



The regulatory direction of travel is clear for all to see. Prior to and since the financial crisis of 2008/9, there has been a steady flow of big impact regulatory directives to raise the bar in consumer protection, starting with 2007 Financial Services Authority (FSA) **Treating Customers Fairly (TCF) and culture** and then 2011 **FSA Responsibilities of Product Providers and Distributers (RPPD)** which stipulated firms should design advice services to generate good outcomes, **the 2012 Retail Distribution Review (RDR)** heightening professional standards across qualifications and remuneration, then the 2017/20 **Senior Managers and Certification Regime (SM&CR)** spotlight on a move to individual compliance responsibility and accountability, 2017 **Product Governance rules (PROD)** requiring firms to manufacture and distribute products and services around client good outcomes, the 2021 high **risk investment review** strengthening financial promotion rules, 2022 **Environmental, Social and Governance (ESG) focus** on disclosure, greenwashing and client sustainability preferences, the **new Appointed Representative (AR) Regime** ensuring principals and their (AR) member firms significantly improve their governance oversight, conduct and competence, plus the operational resilience rules ensuring good practice for systems and controls, and now the 2022/23 **Consumer Duty** clamping down across the distribution chain to ensure harmonisation of information, disclosure and protecting client good outcomes.

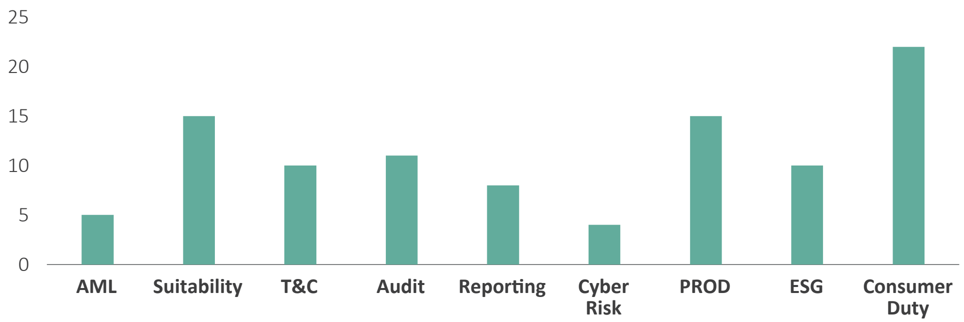
The pandemic has highlighted the need for firms to adopt technology as an enabler to support home and hybrid working, and ensure clients are serviced comprehensively and firms gain quality management information (MI) and data analytics on all business services and operations including compliance.

So with such a pace of regulatory change upon us, there is no doubt that the data our survey shows around regulatory changes, illustrates firms are now looking at how they can better identify, manage and monitor regulatory and access quality data and MI across their businesses.

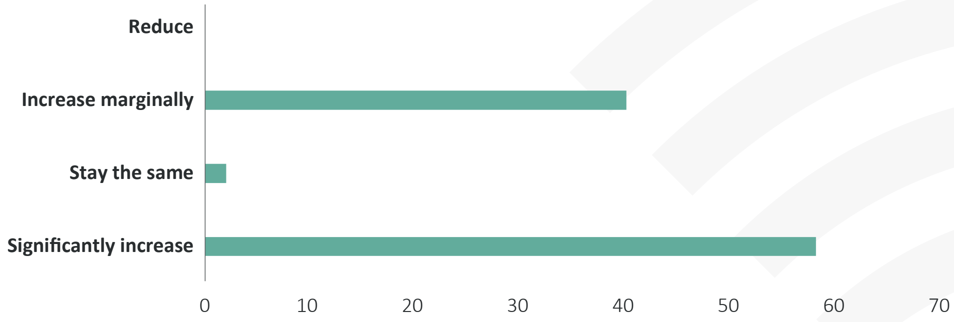
"If you haven't got the data, it didn't happen and if you do, it better have happened".

Chris Davies Founder, Model Office

What are your biggest compliance challenges over the next 12 months?

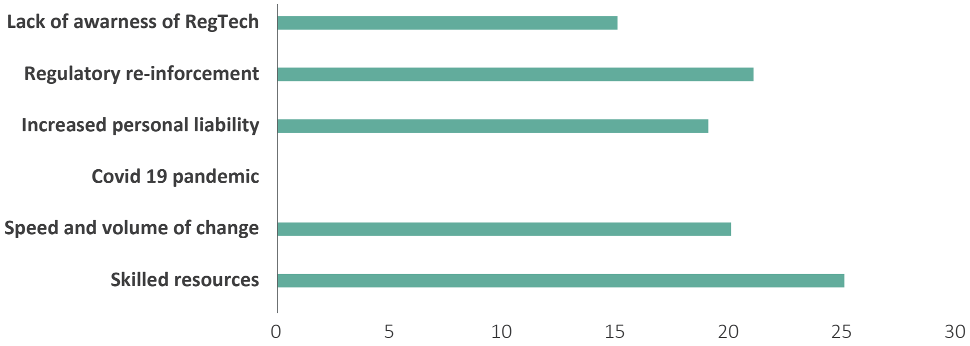


Over the next 12 months, do you expect regulatory directives too?



It is plain to see RIAs are under no false impression that regulatory directives will still be coming thick and fast. It has long been observed, since the financial crises, that it is raining regulations. Yet, it will be those firms which are pro-active, and employ the right people and technology, that can keep abreast of regulatory change and ensure they continue to comply and compete in their markets.

What are the compliance areas within your business that keep you up at night?



The chart showcases that firms are now on the lookout for skilled compliance professionals and resources that will support then maintain their compliance with regulatory directives and protect their clients' needs and good outcomes.

The good news is firms are no longer seeing the pandemic as a challenge as hybrid working becomes the new normal. RIAs are concerned at the lack of technology applied to their compliance supports, particularly with the perceived regulatory enforcement challenge. This is reinforced with RIAs' belief that regulatory directives will increase significantly over the next 12 months.

Summary

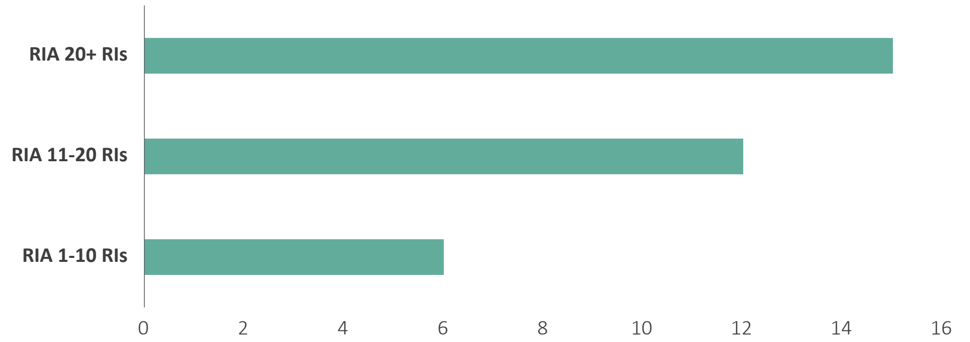
The data in this section shows RIAs are under no illusion that they need to move fast to adopt systems, controls, skilled resources and technologies that can help them keep abreast and ensure they comply with an ever-changing and challenging regulatory environment. This means that firms need to adopt a comprehensive research and due diligence and recruitment strategy to ensure they have the right people in the right place with the right skills and responsibilities, communications are clear and understood, evidence-based practice is at the heart of all they do and the right technology is implemented to increase quality data and MI on all governance, risk and compliance activities.

3. The costs of compliance

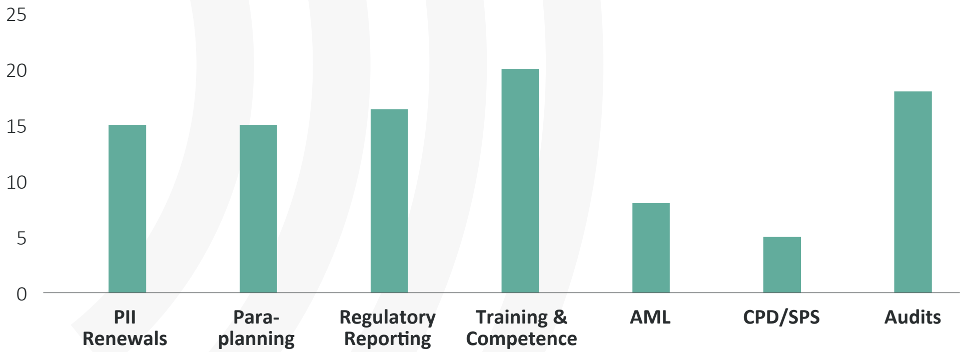
Time

The survey results are clear in this area, that firms are spending an increasing amount of time on compliance activities within their business. This increases dependent on the size of business yet is still proportional to a sizeable chunk of time no matter how big or small the RIA is. It gets really interesting when we look at the compliance activities the firm is taking time to execute.

How much time do you spend each week on compliance?



Which compliance activities take more time?



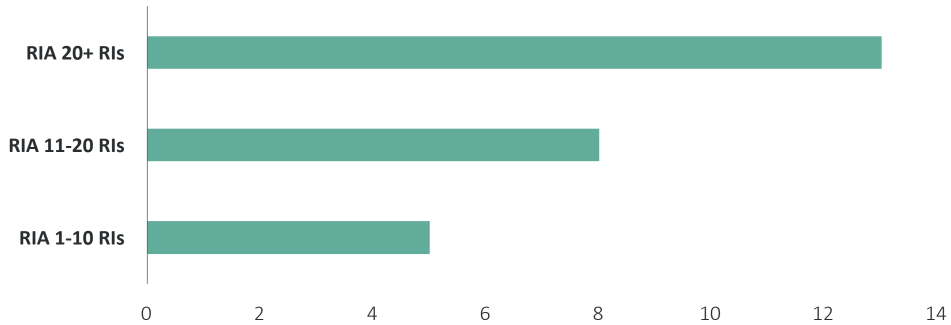
This chart shows a distinct increase in training and competence time from our previous research in this area, which is surely down to key regulatory directives such as the SM&CR. Regarding paraplanning activities, this highlights the rise in this activity being regarded as integral to ensuring suitable advice and compliant services and products are in place, which is a huge positive, yet has a demand on ensuring the right skilled professionals and/or services are recruited and retained. The fact that audits, PII renewals, AML and regulatory reporting are still showing as concerns is interesting when there are already RegTech solutions and services that can significantly reduce the time and associated costs across these particular compliance reporting activities.

Rate how much time is taken across business v compliance activities

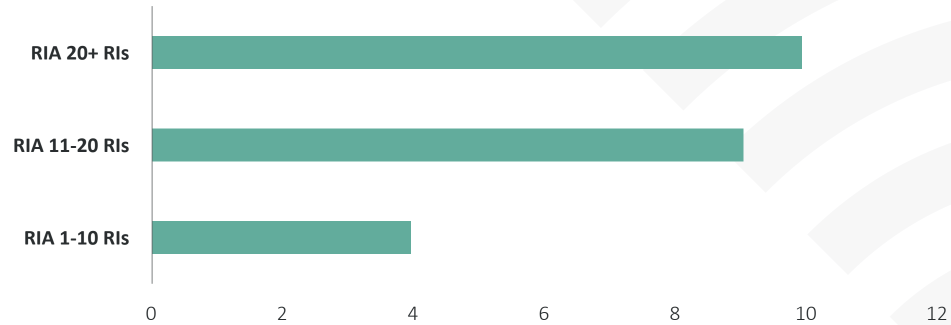
When asked about time cost regarding business and compliance activities, with only 35% of time spent with clients, too many advisers/planners seem to be bogged down in time on and in the business management activities rather than spending the time required to nurture trusted partnership client relationships. This can cause risk in not playing to strengths and thus employing technology and building a diversified team with the right skills is required so time spent on client meetings increases and business operations, systems and controls are expertly managed.

Monetary

How much is the direct compliance cost as a % of your annual revenue (eg. PII levies/fees/licences)?



How much is the indirect compliance cost as a % of your annual revenue (eg. training, recruitment, compliance support, audit)?



The totals across the above RIA firms' direct and indirect compliance costs illustrate a telling trend. It is costing firms more and more money, squeezing margins and will no doubt affect their ability to remain in business against the current cost of living crisis. One of the key concerns we have with the Consumer Duty is the implementation cost. There is no doubt, RIAs will have to invest in more business strategy, T&C, audit and oversight activities to ensure they comply. Generally, this means that some or all of this cost may well be passed on to the clients, an unintended consequence maybe, but a significant self-defeating consequence if this happens.

Summary

What are the biggest reasons for costs of compliance?

The survey results are indicating a worrying trend that the costs of compliance are climbing against an economic outlook for an imminent recession and a political and social backdrop of instability and a European war contributing to a cost-of-living crisis.

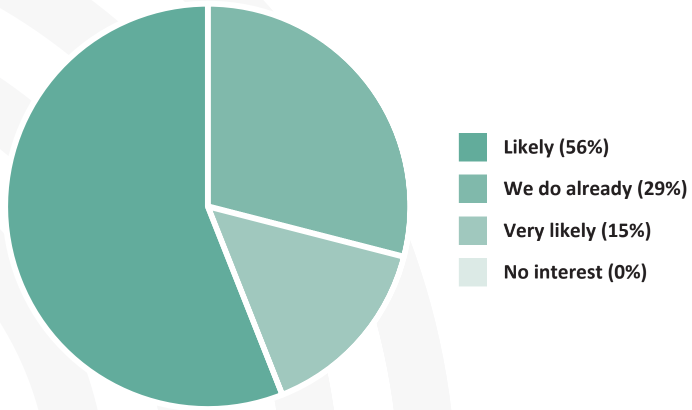
The total direct and indirect compliance costs are very telling:
1.RIA 1–10% 10% revenues. 2. RIA 10–20 17% revenues. 3.RIA 20+ 23% revenues

RIA firms have been suffering a hard professional indemnity insurance (PII) market for some time and the data shows us this is not getting any better as the largest contributory factor to compliance costs. Audits are now demanding data led reporting and granular information on increasing regulatory demands the FCA are imposing across key directives such as the Consumer Duty.

It is clear that something has to give and we hope it is not the firm's resilience! As section 4 will illustrate, RegTech provides a great opportunity for RIAs to adopt technology that will enable them to gain quality and focused data and MI across the plethora of regulatory directives they are having to manage and monitor, plus save them significant costs and time across GRC activities which will help boost performance and ensure clients are served and good outcomes are maintained.

4. RegTech adoption

How likely are you to adopt RegTech over the next 12 months?

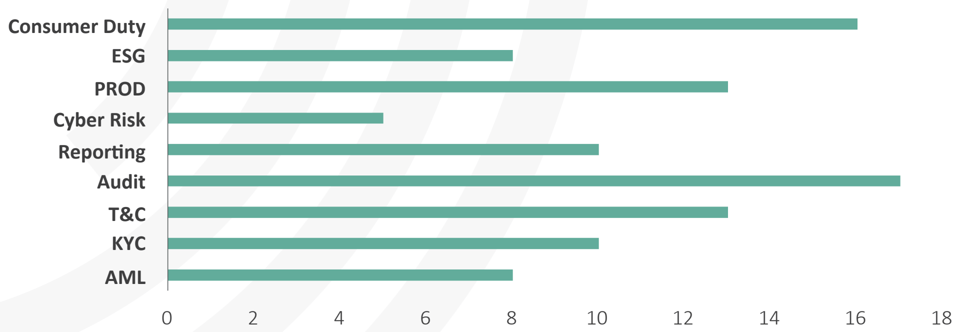


It is encouraging to see that 1 in 3 firms are already engaged and adopting some form of RegTech. This is certainly an improvement since our 2021 benchmark report. It is also good to see that RegTech is now coming into its own with more than 50% RIAs stipulating it is likely they will adopt RegTech into their compliance and business practice.

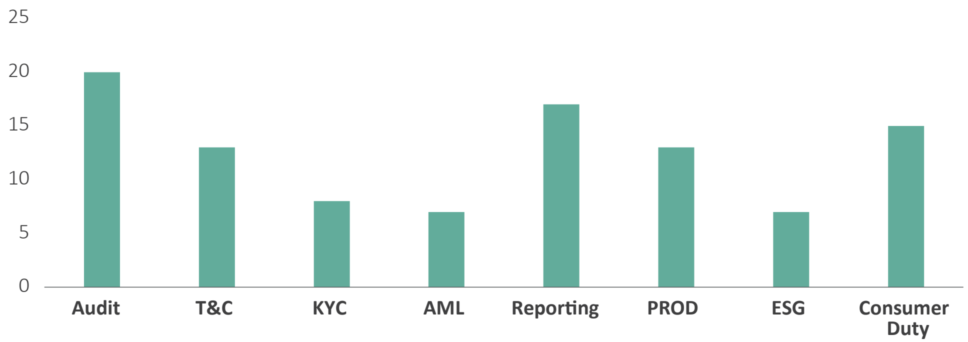
What will the future compliance function look like?

RIAs are also welcoming tech and data into the world of compliance, if they have confidence it will save them costs and time.

In which areas will you adopt a technology solution?



In which areas is RegTech saving you costs?



Both the above bar charts showcase that firms are already contemplating adopting tech across regulatory directives and those who are already engaging RegTech are saving costs. As RegTech can act as a third line of defence and provide granular regulatory intelligence, this means firms are able to make informed decisions on how to develop the business services on a compliant and cost-effective basis going forward.

Summary

As this report shows, compliance teams are still spending a large percentage of time on compliance tasks. On average, firms are spending too much time on business management and compliance tasks and they need to free up ‘dead’ time by employing technology across their client servicing and compliance activities.

Cutting GRC tasks dead time

We have identified that there is a certain amount of ‘dead’ time firms can cut from GRC activities which will allow them to spend more quality time with ongoing client and business strategy needs. By applying RegTech to automate audit client file reviews, compliance policy document and compliance audits and report writing, and streamline regulatory reports, firms can currently save 30%+ of time and associated costs plus ensure they gain higher quality MI and data in real time.

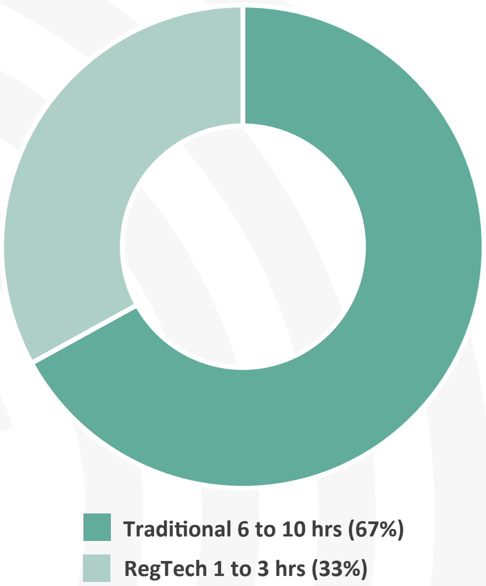
RegTech and alleviated GRC dead time

	Periodic Audit review data gathering	Periodic client file audit	Compliance document audit	Client outcomes, T&C & regulation audit	Audit data and report output	Audit & regulatory report review & analysis
Traditional: Manual, face to face	2 hours	1-2 hours	2-3 hours	3-5 hours	1-2 hours	3-4 hours
Hybrid: ‘cyber compliance’ RegTech	30 mins - 1 hour	30 mins	30 mins	2 hours	60 secs	2 hours

Applied correctly RegTech can cut out compliance ‘dead time’ across travel, onsite/virtual audit fact finding, manual client file, compliance document reviews and audit report writing, presentation and related actions and strategy. As we can see above, dependent on the RIAs business model RegTech can save 50%+ of time and associated compliance costs. This does not mean replacing compliance professionals with technology, it means RegTech enables them to work more effectively and efficiently.

5. Conclusion

How much time do you spend each week on GRC tasks with/without RegTech?



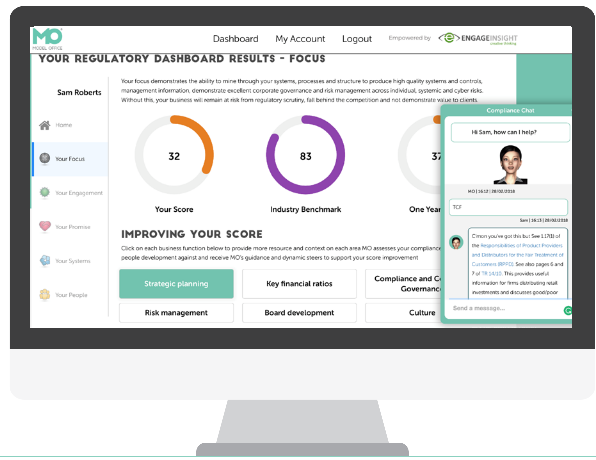
Model Office-MO® is now providing demonstrable time and cost savings both for networks and support services, their member firms and also individual firms.

This applies across all regulatory permissions and the new Appointed Representative regime overhaul where RegTech will provide greater MI and data across new and more rigorous oversight and governance requirements.

The fact that regulatory diagnostic, gap-analysis and audit report phases are all automated, means firms gain on average 6 hours a week back to spend on quality client time. Given the Consumer Duty is now demanding more time spent on supporting the client journey and attaining and maintaining those good outcomes, this surely means that CEOs, compliance officers and client facing teams should embrace RegTech as an integral part of their tech stacks.

As the data illustrates in this report, compliance officers, networks and support services are having to juggle a heap of competing priorities. Whether it is budgets, resources, oversight requirements, risks and controls, prioritising different elements of the governance, risk and compliance role will be a big key to success for any compliance function.

As we can see (despite the majority still using traditional compliance tools), those firms who apply RegTech actually spend less time having to monitor GRC tasks than those who do not. The fact that data driven GRC technology can deliver significant cost and time savings across areas such as PII renewals, client file reviews, audits, regulatory and board reporting and enhance business and client communications, understanding, duty of care and much more means RIAs can gain a RegTech line of defence as they move into a time of increasing uncertainty.



MODELOFFICE

compliance · alignment · sustainability

www.model-office.co.uk

Success by Design