Meeting the challenges
Compliance and obligations across regulatory regimes

bobs guide

IN ASSOCIATION WITH

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Intelligent Automation
Meeting the challenges: Compliance and obligations across regulatory regimes

Foreword
Over the past decade, financial markets have been shaped and defined by two key trends.

Firstly, the post-global financial crises reforms instigated by the G20 have seen a variety of different types of regime arise in markets small and large across the world. Well documented, these regulatory forces have – in some instances deliberately, and in others less directly – forced not only systematic changes but also altered beyond recognition how firms operate, across a number of asset classes. The result has been laborious compliance and reporting obligations, made all the more onerous when firms operate across borders. Secondly, markets have been driven by technological advances.

The rate of progress within the fintech ecosystem has been never before seen, with few markets benefiting as much from technological developments as financial services.

Fortunately these two main drivers have gone hand in hand, with regulatory technology growing in sophistication and prominence in order to lighten the burden of compliance requirements weighing heavily on the shoulders of market participants. But the struggle continues, with new rules adding to the existing regulatory infrastructure continuously.

This year, in partnership with Inforalgo, bobsguide conducted a survey to find out the key compliance burdens facing market participants within some of the most prominent regulatory regimes, and how they’re dealing with them. Some clear trends have surfaced in our research: concerns are rife not just about regulatory regimes the market is currently waiting for – they also exist for those regimes already in play. A range of data management issues exist, and concerns are raised by our survey respondents about how their technology stacks help them to comply.

These points and more point to a changing dynamic for firms between their technological capabilities and regulatory requirements. Read on to get a clearer picture of where things stand across various regimes.

Michael McCaw
Editor
bobsguide

Key takeaways

1. Timelines to prepare for regulations – such as the impending CAT requirements – are putting firms under pressure

2. Data consolidation from a range of sources is a key concern for market participants for complying with various regimes

3. Market participants are wary of connectivity – with other sources and regulatory systems – to fulfil compliance requirements

4. Real-time reporting obligations are a strain for the market, with many respondents facing resource issues

5. A significant portion of the market is still grappling to understand many rule sets, with concerns over fines and reprimands a major threat

6. Firms continue to look for third party and inhouse tech options to help reduce compliance burdens
Real time reporting required

Many of the rules enforced on market participants over the past few years come with the additional challenge of requiring firms to report transaction data in real-time, or close to it. Under Europe’s MiFid II, for instance, trading venues and certain categories of investment firms must publish volume and price within fifteen minutes of a completed trade of equity or similar products. In the US, broker-dealers facing CAT are looking for solutions that capture and manage data in real-time, to ensure reports are made according to the rules’ tight timeframes. Drastically reducing the amount of time a firm has between execution and filing reports, significant pressure has been put on the market in terms of internal resource – as well as finding the right regtech solution to ensure compliance.

New, restrictive and onerous requirements have been reflected in our survey: asked what the most important real-time regulatory reporting functions market participants look for in a solution, more than 50 percent selected data insight or analytics, front end UI/UX for operations and compliance teams, and real time reconciliation, respectively. Clearly, firms looking to comply with real-time reporting obligations require precision in order to trust their real-time data and transparent systems that allow for fast and insightful analytics as stipulated by regulators.
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Operational efficiency a top priority (op risk and fines/punishments)
On a scale of one to ten – with ten being most concern, one being no concern at all, nearly 35 percent of respondents placed operational cost and risk for compliance as an eight.

The extensive challenges firms face to comply with regulatory rules are many, and getting operations in order is crucial. Operational and compliance managers are all too familiar with trying to orchestrate the requirements built into regulatory complexities. Europe’s Emir Refit represents significant changes on a micro level to the existing regime, while many firms are still grappling with MiFid II – with reports of a number of firms rushing to backdate trade data. The Order Audit Trail System (OATS), long considered a difficult and obtuse system, may well be missed when CAT finally gets rolled out. FINRA’s new system has been referred to as “OATS on steroids”, with a host of new substantial data requirements, such as options data, allocations, and customer data.

Our respondents’ concerns are well founded with non-compliance fines stretching into significant portions of a breaching firm’s annual turnover, in some regimes. And they are well aware of it, with 100 percent of respondents at least partially concerned about the threat of fine or reputational damage.

Resource strains
A serious concern for the market is the cost of compliance, and with due concern: preparation for MiFid II itself was estimated to hit around $2.1bn, with direct and indirect costs of Dodd Frank to the top eight US banks hitting earnings by around $12bn per year. Merely connecting to CAT could cost firms around $7,600, annually – and that doesn’t include the infrastructure required to comply. Market participants are wide awake to the resource drain they face: on a scale of one to ten – with ten being most concern, one being no concern at all, around 75 percent selected resources required for compliance as between five and ten on the scale.

On SFTR, it has been estimated that 40 percent of the fields will be difficult to obtain. That’s been reflected in our survey, with more than 50 percent of respondents selecting nine or ten regarding SFTR in our ten point scale, with ten signalling the greatest concern. For FINRA TRACE, 100 percent selected five or above, and with the regulator said to be refining its algorithms, more resource pressure may be placed on those that come into its reach.

Connectivity for ease of data utilisation becoming increasingly vital
As the volume of cogs in the supply chain grows for each firm, interconnectivity between those organisations has become a crucial component to fulfil compliance requirements. More than 50 percent of our survey respondents ranked connectivity methods and protocols as a vital concern when considering the regimes they face.

Of the reporting obligations established in the past decade, many have been created in order to infuse transparency into markets, with both Europe’s Emir Refit and MiFid II seeking to establish the different cogs that led to each trade. Similarly, the impending CAT requirements in the US require broker-dealers and proprietary trading firms to connect with CAT, meaning connectivity, data ingestion, consolidation, mapping, submissions and exceptions management must all be of the highest order. Our survey respondents recognise that, with 100 percent listing connectivity with CAT as a very real concern. For many of the broker-dealers and trading firms subject to CAT, automating a number of processes to fulfil the regulatory requirements in a centralised network will be paramount.
Results

Obligations
This year’s survey was designed to highlight the challenges key regulations have raised among market participants, and which regimes have been the greatest disruptors. The results show some interesting insights, with firms dealing with established rules, but also suggest many are spending a great deal of resource preparing for regimes currently in the pipeline.

Perhaps unsurprisingly, almost 70 percent of those surveyed told us Europe’s second Markets in financial instruments directive (MiFid II) – launched in January 2018 - has posed the greatest impact to their firm over the last 12 months.

The European Commission’s Securities Financing Transactions Regulation (SFTR) ranked second with around 35 percent of respondents highlighting the impending ruleset as a critical focus this year. One in four respondents named the European Markets Infrastructure Regulation (Emir) Refit, which came into force in June, as an critical area of attention in recent months.

Just under 20 percent of respondents pointed to the Financial Industry Regulatory Authority (FINRA)’s Trade Reporting and Compliance Engine regime, with the same number pointing to the Securities and Exchange Commission (SEC)’s Consolidated Audit Trail (CAT), due to come into force next year, and 15 percent highlighted the ever-evolving Dodd Frank Act as a top regulatory hurdle.

Almost 40 percent of those surveyed ultimately named a host of ‘other’ regulations when asked what was posing the greatest impact to their respective firms. The Fundamental Review of the Trading Book (FRTB), the EU’s second Payment Services Directive (PSD2), the General Data Protection Regulation (GDPR) and new capital requirements being introduced by Canada’s Office of the Superintendent of Financial Institutions (OSFI) were all named as areas of concern within compliance departments.

Time to comply
When considering compliance to any regulatory regime, often firms will look first at the timeframe within which they must get their houses in order. We asked firms how much of a concern timelines were in terms of how much pressure they feel to comply, with one being of no concern, 10 being a great concern. Overall, firms are showing signs of extreme concern with regards to their ability to comply with regimes ahead, with the majority of responses coming in at the higher end of the scale.

When broken down by framework, the regulatory timelines attached to FINRA Trace emerged as an area of major concern: nearly one in five of those most concerned about the regime said they are extremely worried about the timeline.

Meanwhile, over 80 percent ranked the EU’s Emir Refit a seven or eight out of ten. Although the bulk of requirements came into effect in June 2019, reporting obligations on certain delayed provisions will come into force from June next year.

Our survey also revealed a mixed level of concern surrounding the Dodd Frank Act. In October, a major update to the Act’s so-called Volcker Rule received its final seal of approval. It will come into effect from January 2020, with a mandatory compliance deadline of January 1, 2021.
A third of respondents suggested they were less concerned about the timeframe, but the rest said it is causing anxiety in compliance departments.

**Pointing to the (right) data**

**Data consolidation**

When asked to rate their level of concern surrounding data consolidation from disparate data sources, almost a third of those surveyed suggested this is causing compliance headaches. This high level of concern amongst practitioners is spearheaded by concerns in relation to MiFid II requirements.

When segmented by top regulatory area of concern, almost 40 percent rated data consolidation from disparate sources at the very top end of the scale in relation to MiFid II.

Data consolidation is also a critical concern around Dodd Frank. Two-thirds of survey respondents rated consolidation from disparate sources with an eight or a nine as a prime concern, which makes sense given the broad range of data required in order to meet the Act’s all-encompassing reporting requirements.

Around 40 percent of practitioners concerned about FINRA Trace ranked data consolidation as a major issue. This likely stems from the phasing out of the legacy CTCI tool many firms commonly used for electronic Trace and ORF reporting, which will be unsupported by February next year.

Those practitioners facing business disruption from the Emir Refit expressed concerns around data consolidation, with around a fifth ranking it as their most serious reporting concern.

**Data volumes**

In addition to the compatibility of various data strands, the sheer volume and size of transaction data was revealed to be a serious area of concern for those facing compliance obligations. A third of respondents rated the volume of transactions or data reporting required at the very top of the scale and as a primary hurdle to compliance.

Concerns are particularly high in relation to MiFid II requirements. Almost
half rated data size as at the very top of the scale in terms of a concern. This is hardly surprising given the huge scope of the directive in terms of data on pre-trade, trade and post-trade activities across the various asset classes.

Other segments generated a mixed response. In terms of Dodd Frank, a third scored data volumes a major concern in terms of their worry level. By contrast, two-thirds said they were relatively comfortable in dealing with the requirements.

Survey respondents gave us a similar picture in terms of mixed concerns when it came to the CAT, Emir, FINRA and SFTR obligations. Practitioners focused on addressing MAS or OATS compliance obligations expressed little-to-no concerns in this area.

Data connectivity
Our survey found data connectivity to be a high area of concern for most organisations, with just over a third rating connectivity a major concern. A further third scored connectivity as a medium-level concern while the remainder or practitioners indicated it was a non-issue.

When broken down by framework, those dealing with Emir Refit pointed to connectivity as a major concern. The response among practitioners focused on Mifid II and Dodd Frank was similarly alarming, with a third scoring connectivity as a seven out of ten for the former and 30 percent scoring it an eight out of ten for the latter.

Data fragmentation
This year’s survey found data fragmentation to be another key area of focus, with a third scoring data fragmentation as the single most concerning hurdle to compliance.

CAT emerged as highest area of concern, with 60 percent rating fragmentation a major area of concern. This anxiety is likely generated from the large amounts of data the SEC is requesting as part of required reporting on executed trade orders. Likewise, 60 percent scored data fragmentation a major area of concern in relation to FINRA Trace.

Our survey revealed a mixed level of concern surrounding the Dodd Frank Act. In October, a major update to the Act’s so-called Volcker Rule received its final seal of approval. It will come into effect from January 2020, with a mandatory compliance deadline of January 1, 2021.
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Transaction reporting
Over a third of respondents rated the real-time nature of transaction reporting at the top end of the scale.

Practitioners told us they were most concerned about the real-time nature of transaction reporting in relation to Mifid II. Around 50 percent scored real-time reporting at the very top of the scale.

A third of respondents scored real-time reporting as a major concern in relation to Dodd Frank obligations, and of those respondents facing FINRA and CAT obligations, two fifths suggested real-time reporting as a concern.

How much of a concern are real-time transaction reporting obligations?

Operational cost and risk
Over half of the respondents in this year’s survey rated operational cost and risk for compliance a serious concern. By contrast, not a single practitioner rated this area as a non-issue.

That response rate mirrors those respondents facing Mifid II obligations, while 40 percent of those facing CAT highlighted the regime’s operational cost and risk as a major concern.

Likewise, a third scored operational cost and risk as a prime concern in terms of Dodd Frank requirements, 80 percent scored it as serious concern in relation to the Emir Refit and 45 percent of those facing SFTR ranked operational cost and risk for compliance as a top concern for conforming with the rules.

In terms of compliance, 100 percent of those practitioners who’d indicated OATS was the single greatest regulatory disrupter to their business scored cost and risk at the very top of the scale.

Regulatory violations
Violations and disclosure have the power to decimate an organisation in terms of heavy fines or reputational damage – which is why just under half of our respondents scored these concerns as a major concern.

When asked about their concern levels, two-thirds of respondents facing Dodd Frank obligations ranked violations and disclosure threats as a very real threat.

That’s unsurprising given the SEC’s tiered
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A bobsguide report in association with Inforalgo

How much of a concern is the interpretation of eligibility and determination rules?

Over a third of Mifid II obliging respondents said violations and disclosures are a very real threat, which suggests firms are still struggling to conform with the rules.

Eligibility and determination rules
Our survey found practitioners held varied views around the interpretation of eligibility and determination rules. A third suggested this area is a prime concern, with 50 percent indicating it as a medium concern and very few downplaying the concern as being of insignificant relevance.

Reading the rules

Business rules
Many of the new regulatory frameworks that have impacted firms over recent years haven’t just been large in scope – they’re also large in size, often with vagaries which lead to variations in terms of interpretation. Over forty percent of respondents to our survey said interpreting the rules was an area of serious concern.

Over 80 percent of those complying with the Emir Refit rated interpreting the rules sufficiently as a major concern in terms of the significance of the concern. SFTR also ranked highly, with around 55 percent of respondents suggesting this as a primary concern.

Practitioners indicated they were relatively relaxed in terms of their interpretations of Dodd Frank, MAS requirements and OATS, while just over a third of Mifid II impacted firms ranked the interpretation of rules as a very real concern.

Are you struggling with the rules?

Over a third of Mifid II obliging respondents said violations and disclosures are a very real threat, which suggests firms are still struggling to conform with the rules.
Just under half of SFTR and, separately, Emir Refit-impacted respondents rated interpretation as a primary concern, suggesting worries over the interpretations of both rule sets.

Similarly, 35 percent of those who’d identified Mifid II as a top concern rated interpretation as a very real problem. By contrast, respondents indicated they were relatively unconcerned with their interpretation of eligibility rules in terms of Dodd Frank and CAT.

Ambiguity surrounding the rules can make life incredibly difficult for compliance managers. That’s why a third of respondents rated ambiguity highly on our scale.

When broken down by regime, practitioners expressed particular concern around ambiguity as it relates to Mifid II. Almost 40 percent of respondents impacted by the regime rated ambiguity around the rules as a very real concern. Likewise, 40 percent of respondents who’d expressed a focus on SFTR scored ambiguity around its requirements at the top end of the scale. The same proportion of CAT-impacted practitioners rated ambiguity of the rules as a major concern.

**Tech assistance**

**Technology stack used**
Across the compliance infrastructure, firms rely on modern tech systems to take up large parts of the burdens they face. However, our survey respondents raised concerns about how they assist with compliance.

Asked where their technology stack sits in terms of a hurdle to compliance, a third selected it between eight and ten – at the very top of the scale. Almost 40 percent scored the technology stack their organisation is using in the midrange (between four and six).

Over 40 percent of Mifid II-impacted firms rated their tech stacks at the top end of the spectrum (eight to ten) as a compliance concern. This was of equal concern to those respondents focused on SFTR, with 40 percent scoring technological concerns prominently.

Tech stacks used in relation to CAT requirements were also a top area for
This year’s survey revealed functional or systematic changes to be a relatively high area of concern. Over a third of respondents scored functional or systematic changes at the highest end of the scale.

Are you worried about the resources required to comply from development and operations?

Concern, with 60 percent scoring at the top end of the scale.

By contrast, our survey found lower levels of concern in this area in relation to the Emir Refit. Just under half of respondents who’d indicated this regime was their organisation’s top regulatory hurdle scored tech stacks either a ‘2’, ‘4’ or ‘5’.

By contrast, our Emir Refir obligations do not seem to contradict the rules’ requirements, with just less than half of respondents selecting the concern as being on the lower end of the scale (between one and five) as a matter of concern.

Functional or systematic changes
This year’s survey revealed functional or systematic changes to be a relatively high area of concern. Over a third of respondents scored functional or systematic changes the highest end of the scale.

When broken down by regime, functional or systematic changes were of the greatest concern to those organisations experiencing adverse impacts from predicted CAT requirements. Four out of five rated functional changes at the top end of the scale.

Practitioners impacted by MiFid II, Emir Refit and SFTR also indicated relatively high levels of concern in this area. Around 40 percent rated systematic changes at the top end of the scale.

Required resources
The resource required to comply with regulatory obligations has been a substantial area for concern recently. Almost half of the survey’s respondents scored the resources required to comply from development and operations between eight and ten – at the top end of the scale. Just over 40 percent rated this area a seven out of ten. Not a single respondent indicated it was not a concern.

80 percent highlighted this as a top area for concern in relation to CAT requirements, while just over half of MiFid II-impacted firms scored resourcing at the highest point in the scale. Likewise, 45 percent of SFTR-impacted firms scored resources highest in terms of raising concerns.
Improving regulatory workflows
When asked which regtech solutions they would consider, 48 percent told us they favoured extending their organisation’s in-house reporting functions, while 30 percent said they would look to outsourcing to multiple vendors for a single solution.

By contrast, 15 percent indicated they would prefer to outsource to a single vendor for multiple solutions. Just seven percent said they’d consider a new in-house solution.

These priorities changed when segmented by particular regimes.

In terms of Dodd Frank, 75 percent said they would consider an existing in-house reporting function. Likewise, two-thirds of Emir Reft impacted firms said their solution of choice would be to extend in-house reporting function. This was also the favoured method amongst those focused on CAT requirements, SFTR obligations and Mifid II.

For new regulatory reporting workflows which of the following regtech solutions would you consider?

- Extending existing in house reporting function 48%
- Outsource to multiple vendors for single solutions 30%
- Outsource to single vendors for multiple solutions 15%
- A new in house solution 7%

Areas for discussion
When asked about the most discussed about areas within their organisations, 39 percent said they spent the most time mulling over the creation of a ‘golden source’ of data that can increase both confidence and performance in meeting ongoing regulatory reporting and compliance challenges.

This was followed by discussions around existing gaps between regulatory rules and organisations’ processes and controls (35 percent), and the cost of compliance weighed against regulatory fines and reputational damage (19 percent).

There was an even split in relation to Dodd Frank between those whose top areas for discussion were the cost of compliance, creation of a ‘golden source’ of data and existing gaps between regulatory rules. But in terms of those practitioners focused on CAT, OATS and FINRA Trace requirements, the creation of a ‘golden source’ of data was overwhelming named the number one area for discussion within firms.

Concerning regulations, which of the following is the most discussed topic in your firm?

- The creation of a ‘golden source’ of data which can increase both confidence and performance in meeting ongoing regulatory reporting and compliance challenges 39%
- The cost of compliance weighed against regulatory fines and reputational damage 19%
- Existing gaps between regulatory rules, and organisations’ processes and controls 35%
- The impact and uncertainty the UK’s exit from Europe (Brexit) may have on regulators 4%
- Potentially contradictory interpretation and application of regulations 4%
When asked about the functions they prioritise in relation to real-time regulatory reporting, just over half of respondents told us their most important considerations were front end UI/UX for operations and compliance teams, as well as data insight or analytics.

Real-time reconciliation followed closely as a top priority among those firms considering new regtech solutions – while just under half highlighted the ingestion of source data in real-time. Exception management was the least sought-after function, with just over a third indicating this was a key consideration.

Front end UI-UX for operations and compliance teams was most prevalent for those impacted by Dodd Frank, with 100 percent highlighting this as a key consideration. Likewise, 100 percent of respondents said control of data mappings and workflow (without code changes) was a top consideration. The requirement for data analytics or insights was most prominent in relation to CAT requirements – with 100 percent naming it a top consideration. This was also the top consideration in terms of FINRA obligations, with 80 percent telling us the data insights, control of data mappings and ingestion of source data in real-time were all top considerations.

Finally, reporting timeframe was more likely to be named a key consideration among those who indicated high levels of concern over Mifid II obligations. In terms of enrichment using reference data, 75 percent of those surveyed who’d identified the Emir Refit as their firm’s greatest regulatory disruptor indicated this was a top priority.

100 percent of respondents said control of data mappings and workflow (without code changes) was a top consideration.
About this survey
This survey was conducted between September and November 2019. The primary aim of the survey was to identify and evaluate the concerns financial market participants face in complying with regulatory hurdles.

50 percent of our respondents were based in Europe, nearly 30 percent in North America, eight percent based in Africa and just over two percent in Asia.

The survey and the report were conducted by bobsguide in partnership with Inforalgo.