

GLOBAL DIGITAL FINANCE: REPORT LAUNCH

MEETING ETHICS AND COMPLIANCE CHALLENGES IN FINANCIAL SERVICES

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Welcome

Rudi Lang
*Global Head of Financial
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DIGITAL FINANCE:

Meeting ethics and compliance challenges in financial services

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The Economist Group

RESEARCH OBJECTIVES

The starting point for this study was the wave of regulation of financial services that followed the 2007-08 financial crisis—particularly the regulations aimed at improving ethical performance through better internal supervision, greater transparency, and more honest risk assessment.

These new requirements, combined with the increased digitisation of the industry, form the background to the central inquiry in this study: **To what extent are financial services firms using digital tools to improve ethical performance?**

The study aims to improve understanding in the following areas:

- Have financial services companies expanded their use of enhanced information technologies, such as data analytics, to comply with new regulations?
- Have financial services companies expanded their use of enhanced information technologies to raise their ethical standards beyond narrow compliance?
- How aware are financial services executives of the issues or problems that enhanced information technologies may raise for their companies' ethical conduct?

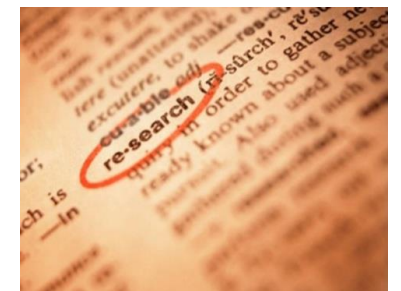


ABOUT THE RESEARCH (1) – ONLINE SURVEY

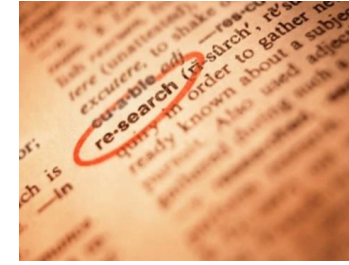
In December 2015 and January 2016, the Economist Intelligence Unit carried out a global online survey of 201 executives of financial services industries.

Survey demographics:

- **Number:** 201
- **Geography:** 60 in Asia-Pacific, 60 in Europe, 61 in North America, 20 from rest of world
- **Function:** 50 IT specialists, 51 risk/compliance specialists, 100 range of other functions
- **Seniority:** Half are C-level and above
- **Company size:** Half represent companies with global annual revenues above US\$500 million



ABOUT THE RESEARCH (2) – IN-DEPTH INTERVIEWS



Also in December 2015 and January 2016, the Economist Intelligence Unit carried out in-depth interviews with six experts in the topic under study.

Participants in interview programme:

- **Dr Thomas Loesler**, Global Chief Compliance Officer, Allianz
- **Andrew White**, CEO, FundApps (a regulation technology company)
- **Ben Hammersley**, Futurist and cybercrime expert
- **James Kennedy**, Applications Delivery Chief Technology Officer, UBS
- **Giancarlo Bruno**, head of financial services industries and member of the management committee, World Economic Forum
- **R. Jesse McWaters**, financial innovation lead, World Economic Forum

KEY FINDINGS: SUMMARY

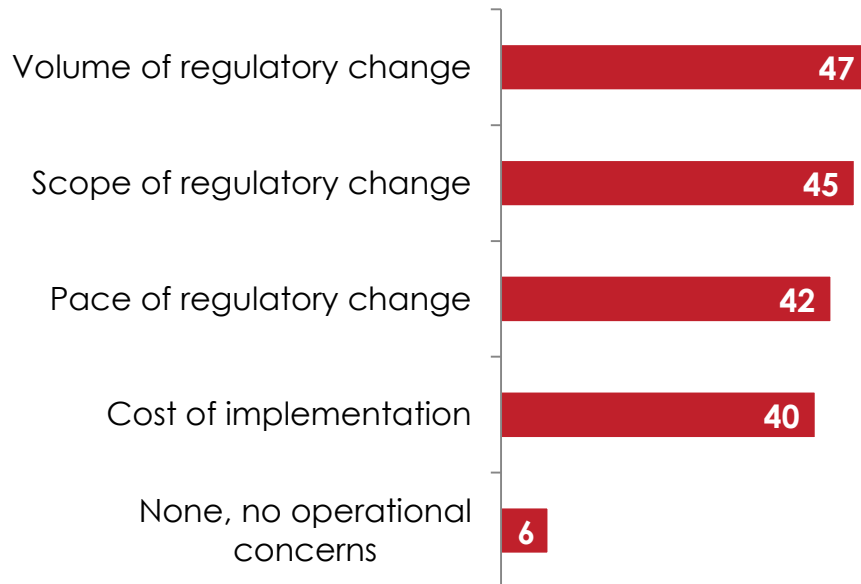


- The wave of regulation, particularly those involving data storage and handling, is causing major operational worries for financial services companies
- While complaining about these regulations, three-quarters of financial companies also claim they are raising their ethical standards beyond regulation requirements—and using digital technologies to do so
- Most financial companies say they have turned ethical compliance into a competitive advantage, particularly by publicising this to enhance their brand image
- At the same time, the financial companies surveyed lag in implementing other changes aimed at embedding ethical compliance, such as better-targeted internal procedures or codes of conduct
- Moreover, three-quarters of companies surveyed say the use of data mining and/or enhanced data analytics raises potential ethical issues of its own, such as a risk of breaching customer privacy; respondents point to the use of third-party analytics providers as particularly risky
- Increased use of digital tools so far has not prompted financial companies to implement corresponding changes in internal procedures or codes of conduct

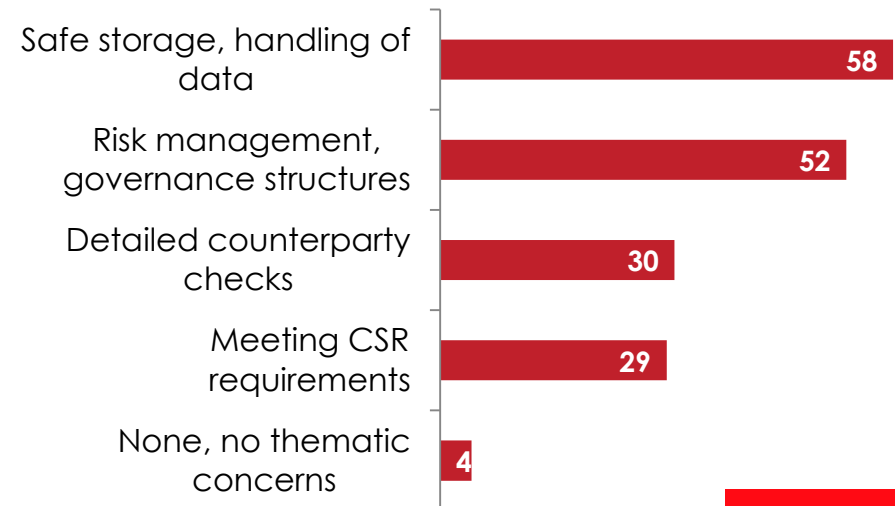
KEY FINDING 1: THE WAVE OF REGULATION, PARTICULARLY THOSE INVOLVING DATA STORAGE AND HANDLING, IS CAUSING MAJOR OPERATIONAL WORRIES FOR FINANCIAL SERVICES COMPANIES

Hit by a wave: The volume and scope of regulation cause the greatest operational worries. The aspects of regulation causing most headaches deal with safe storage and handling of data.

Q: Thinking about the operational requirements imposed by the new regulations, which of the following aspects of regulation, if any, causes the greatest worry for your company? Please select the top two. (% respondents)



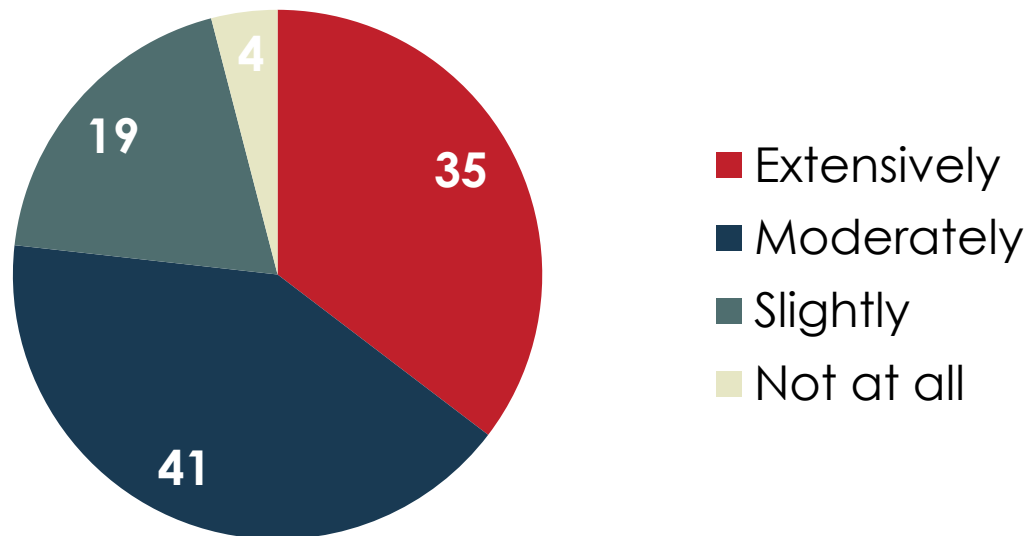
Q: Thinking about the wave of financial services regulations over the past seven years, which of the following regulatory themes, if any, causes the greatest worry for your company? Please select the top two. (% respondents)



KEY FINDING 2: WHILE COMPLAINING ABOUT REGULATION, THREE-QUARTERS OF COMPANIES ALSO CLAIM THAT THEY ARE RAISING THEIR ETHICAL STANDARDS BEYOND THE REQUIREMENTS—AND USING DIGITAL TECHNOLOGIES TO DO SO

In our survey, 76% of respondents say their companies rely on advanced data analytics or data privacy technologies, either extensively or moderately, to raise ethical standards beyond simple compliance

Q: To what extent does your company rely on advanced data analytics and/or data privacy technologies to raise its standard of ethical conduct, beyond simple compliance? (% respondents)



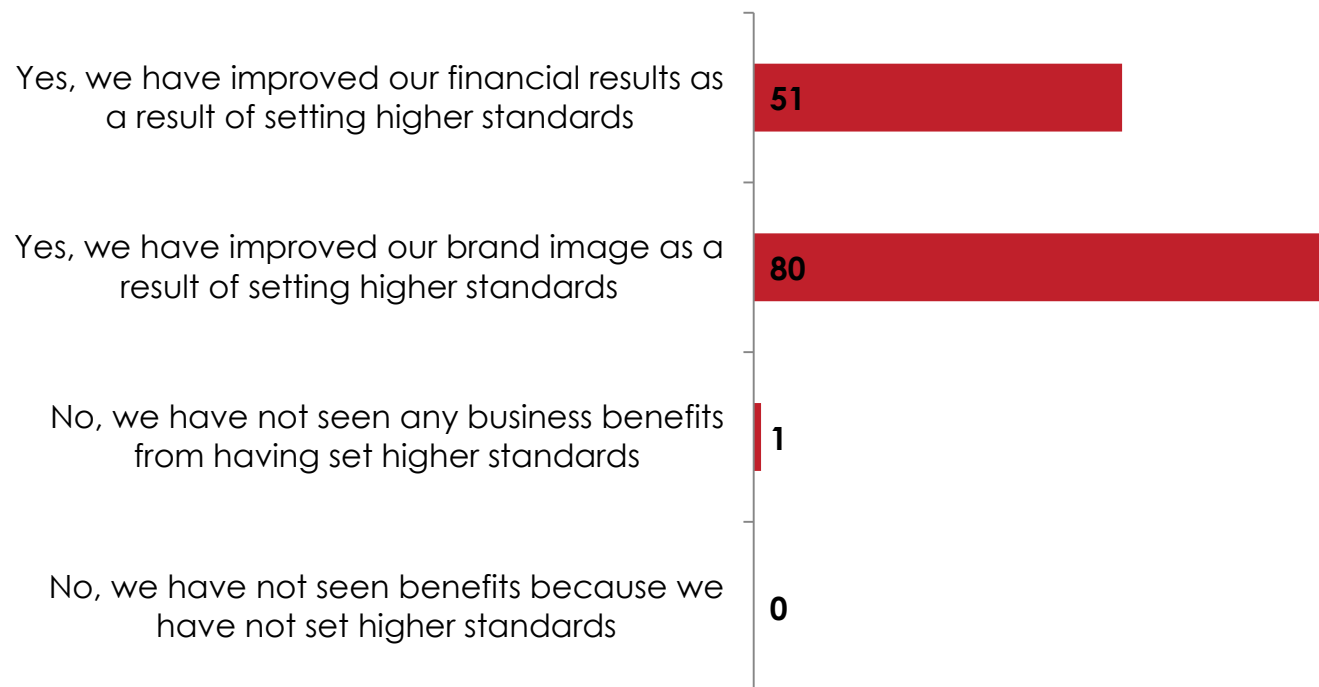
“Ethical situations need to be tested out, placing people in scenarios so that they truly consider the opportunity cost of acting unethically...”

- Association of Chartered Certified Accountants, “Culture vs regulation: What is needed to improve ethics in finance?”, 2014

KEY FINDING 3: MOST FINANCIAL COMPANIES SAY THEY HAVE TURNED ETHICAL COMPLIANCE INTO A COMPETITIVE ADVANTAGE, PARTICULARLY BY PUBLICISING THIS TO ENHANCE THEIR BRAND IMAGE

Respondents say there are good business reasons for going beyond mere compliance.

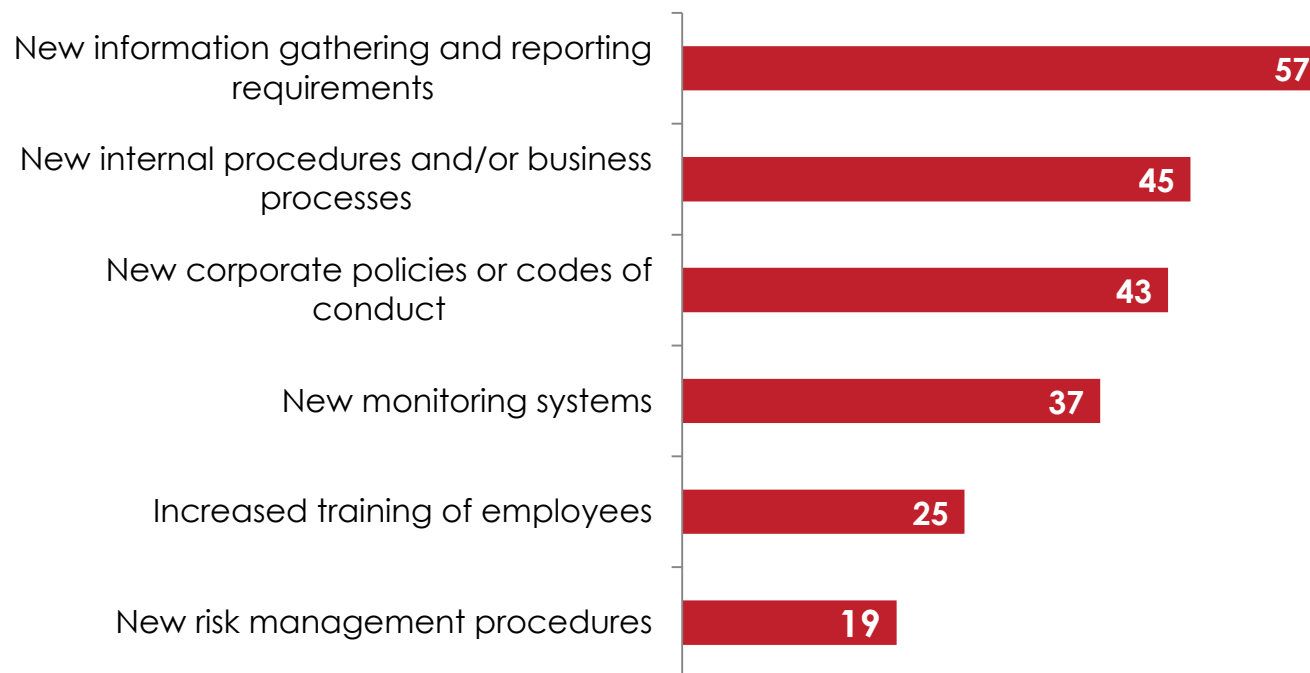
Q: Has your company tried to turn compliance with ethical standards into a competitive advantage?
Select up to two. (% respondents)



KEY FINDING 4: AT THE SAME TIME, FINANCIAL COMPANIES LAG IN IMPLEMENTING OTHER CHANGES AIMED AT EMBEDDING ETHICAL COMPLIANCE, SUCH AS BETTER-TARGETED INTERNAL PROCEDURES OR CODES OF CONDUCT

Survey results show a great deal of activity under way to improve transparency and/or ethical conduct. But the only area of activity involving more than half of respondents is that of information gathering and reporting.

Q: Beyond the use of enhanced digital tools, which additional measures or corporate practices, if any, has your company introduced in recent years to improve transparency and/or ethical conduct? Please select all that apply.
(% respondents)



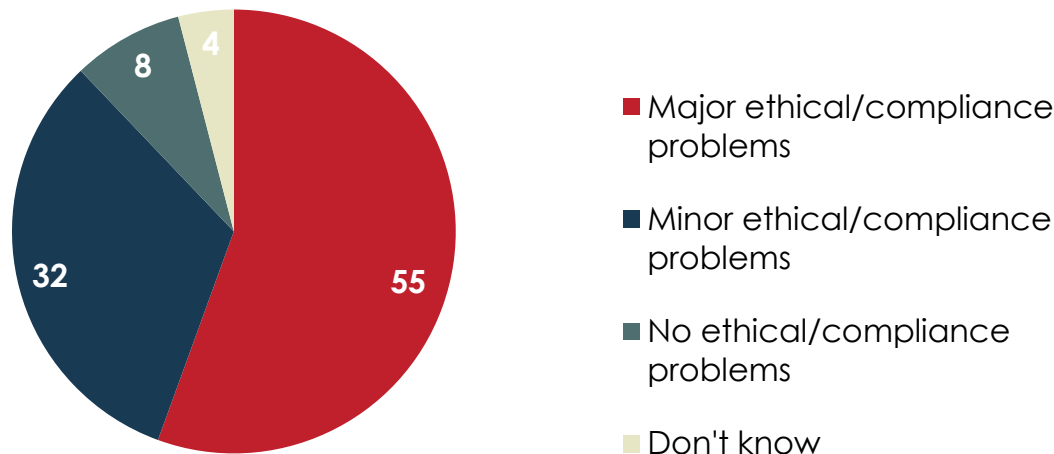
“Compliance is not just a control function to us, it’s an advisory function, which is equally important.”

- Dr. Thomas Loesler, Global Chief Compliance Officer, Allianz, discussing “Allianz Connect”, an internal social media platform

KEY FINDING 5: MOREOVER, THREE-QUARTERS OF RESPONDENTS SAY THE USE OF DATA MINING AND/OR ENHANCED DATA ANALYTICS RAISES POTENTIAL ETHICAL ISSUES OF ITS OWN, SUCH AS A RISK OF BREACHING CUSTOMER PRIVACY

Respondents worry about the rising incidence of cyber-security breaches affecting financial services companies and their customers. A large majority (87%) say that outsourcing data analytics to third-party providers could jeopardise their own ethical compliance.

Q: To what extent does the use of enhanced digital technologies—such as advanced data analytics and data mining—by third parties (eg suppliers or counterparties) create potential ethical or compliance problems for your company? (% responding)



Point - Counterpoint

Third-party IT providers represent “a fundamentally different type of risk. ... As operational risk [is] centralised, that comes with risks to systemic stability”

- Jesse McWaters, Financial innovation lead, World Economic Forum

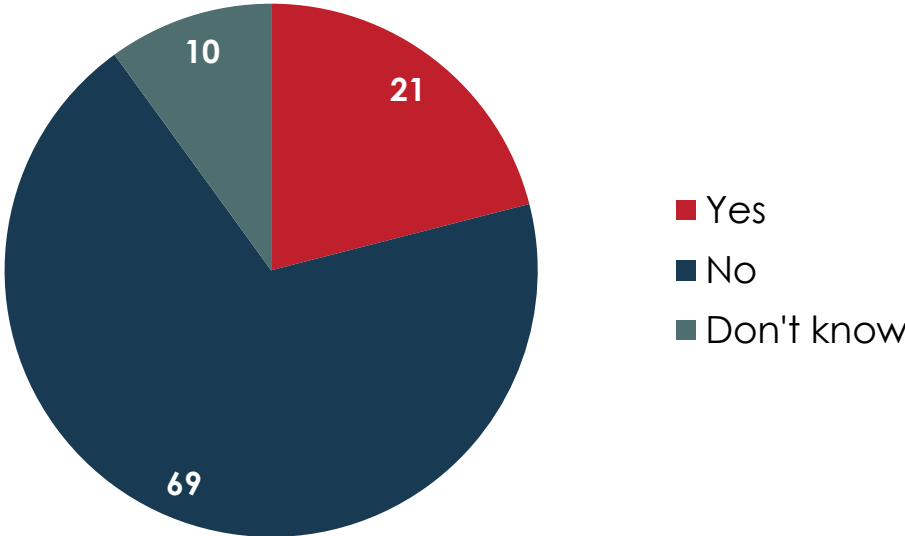
“One of the crucial advantages of the cloud is the ‘strength in numbers’ aspect. For example, every one of our rules has been reviewed and approved by each of our 20 clients.”

- Andrew White, CEO, FundApps

KEY FINDING 6: INCREASED USE OF DIGITAL TOOLS SO FAR HAS NOT PROMPTED FINANCIAL COMPANIES TO IMPLEMENT CORRESPONDING CHANGES IN INTERNAL PROCEDURES OR CODES OF CONDUCT

Internal procedures have been slow to change in response to introduction of new data analytics and cyber security technologies and suppliers.

Q: Has your company changed any of its procedures or codes of conduct in response to the availability of new digital tools? (% responding)



An algorithm “understands only what it is explicitly told.”

- Michael Luca et al, “Algorithms need managers, too”, *Harvard Business Review*, Jan/Feb, 2016

CONCLUSION: FUTURE PRIORITIES

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- The financial industry is responding to the wave of new ethics-oriented regulation despite its worries about operational impacts
- Respondents find cyber-security systems and advanced data analytics technologies most useful in meeting new regulatory requirements for better transparency, risk management, and ethical conduct
- But the industry is weaker on the “softer” measures that help to embed a culture of ethical conduct, such as adopting new internal procedures and new policies or codes of conduct
- The mainly technological fixes adopted so far will prove insufficient to fostering ethics-oriented corporate cultures that go beyond narrow compliance



Thank you.

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Panel session

Chair: **Rudi Lang** - Head of Global Financial Institutions, Mazars

Aviva Freudmann - Research Director, EMEA Thought Leadership, Economist Intelligence Unit

Daryl Wilkinson - DWC Ltd, Strategic Advisor to FCA and a European Digital Financial Services 'Power 50

Kevin Gordon Barrow - CEO/founder of philanthropic Fintech start up MARK Labs