RegTech for Asset Managers:
Unleashing the Pent-Up Demand to Automate

February 2017

The regulatory shift toward heightened management of systemic risk has dramatically increased reporting obligations for asset managers in recent years. Requirements such as the EU's Alternative Investment Fund Managers Directive (AIFMD), U.S. Money Market Fund Reform and last year's SEC Investment Company Reporting Modernization Rule (SEC Mod) are all designed to give regulators the data necessary to provide deeper visibility into systemic risk.

The increased regulatory pressures have many buy-side firms turning to a new breed of solutions, collectively known as RegTech, which use advanced data analytics and artificial intelligence to monitor risk, help firms stay ahead of regulatory compliance requirements and improve operational efficiencies and cost effectiveness in the back office.

In this whitepaper, Confluence discusses the historical landscape leading up to the introduction of RegTech, defines RegTech and discusses its implications for transforming the asset management back office.

The Tipping Point for Change

Across the industry, asset managers are feeling the impact of increased regulatory scrutiny, with many now reporting hundreds of disclosures to regulators and statistical data collectors, not to mention investors and internal clients. As the reporting burden has increased, deadlines have also become much more stringent, placing tremendous time and cost pressures on asset managers.

Historically, regulatory compliance was seen as a must-have and treated as a tactical burden, carried out piecemeal with little overarching strategy. Responsibilities have been spread across various internal legal, risk and accounting teams and possibly external fund administrators, with each of these groups using their own systems with bespoke data integration approaches and processes. Regulatory reporting has been a complex, fragmented, costly and time-consuming endeavor, offering little to the business in the way of strategic insight to date.

To manage their reporting obligations more holistically and strategically, asset managers need to invest in automating and streamlining their back-office processes—a long-sought goal.

In a Confluence survey of asset management industry professionals conducted in the second half of 2016, 61 percent of respondents cited automating back-office processes as their top goal for the coming year. In fact, this has been the top priority in four consecutive surveys Confluence has conducted in the past eight years.

Why now? With the regulatory burden intensifying for asset managers and their service providers, Confluence believes the pent-up demand for change and automation in the back office has reached a tipping point. That sense of urgency, along with regulator support for new technology adoption, are the drivers for adopting RegTech in asset management.

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Origins of RegTech

RegTech refers to the creation, development and adoption of new technologies that facilitate compliance with regulatory requirements and obligations. The emerging global industry is projected to grow to $120 billion by 2020, according to Reuters.

The term RegTech was first used in conjunction with the UK Financial Conduct Authority (FCA)'s Project Innovate. Recognizing that asset managers and other financial services firms are overwhelmed with their reporting responsibilities, the UK regulator sought to create an environment where firms, vendors and FinTech startups could test out new ideas and technologies in a so-called regulatory sandbox.

The FCA has also issued guidelines to the regulated community on how to assess, compare and deploy cloud-based solutions. "The FCA guidance provides firms with a greater level of comfort in deploying cloud technology, and is fostering a more positive environment for innovation," says Nicola Le Brocq, Regulatory & Compliance Market Analyst at Confluence.

Reuters also reported that other international regulators have followed suit and are offering similar support to the budding RegTech industry. The Hong Kong Monetary Authority and Securities and Futures Commission (SFC) both recently said that they see major opportunities for technology to help financial firms meet growing regulatory requirements. In September, the SFC announced plans to launch a pilot project with 20 banks to monitor and detect systemic risk using RegTech.

Regulatory bodies in Australia, Canada, Japan and Singapore have also begun to engage with RegTech. In October, the SEC proposed an Office of Data Strategy, part of a broader vision for the regulator to find new, innovative ways to keep up with data's growing role in regulating the markets. The RegTech initiative put in motion by UK regulators will no doubt continue to spread globally as firms turn to disruptive technologies to manage new regulatory requirements.

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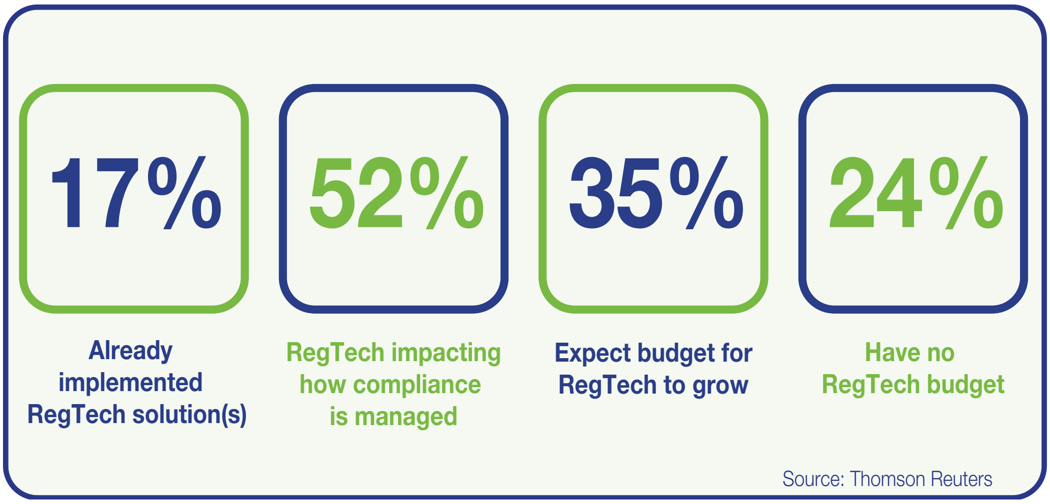
In a recent Thomson Reuters survey of more than 500 financial services compliance and risk professionals, entitled *FinTech, RegTech and the Role of Compliance*, 17 percent of respondents said they had already implemented one or more RegTech solutions, while 52%reported that RegTech solutions are impacting how they manage compliance in their firm. Some 35% of respondents expected their budget for RegTech solutions to grow in 2017, but almost a quarter (24%) had no RegTech budget, signifying a potential divide in the industry between firms that are embracing new technologies and those that aren't.



So What Is RegTech?

RegTech solutions leverage advanced data automation and information management technologies, and are often delivered on a Software-as-a-Service (SaaS) or Cloud-based model. They include powerful analytics that enable fast vetting of transactions and client data, effective management of data, quick and standardized digital reporting and real-time compliance monitoring. This type of application delivery offers many advantages including fast deployment, flexibility and scalability. SaaS or Cloud deployment also reduces infrastructure requirements on the clients' end, enabling firms to be up and running fast and allowing for seamless upgrades.

Regulatory requirements have the potential to change rapidly, with regulatory bodies frequently issuing revisions and releasing additional FAQs. With traditional application deployments, rewriting software to take new requirements into account has been particularly time consuming and costly. When a regulation is amended, firms using traditional installed applications must go through painful upgrades in order to receive the modifications made by their software providers to meet the amendments. That process is both resource-intensive and risk-prone. Today, firms are seeking solutions that are flexible and offer built-in agility to adapt to changing requirements. Cloud-based and SaaS-enabled RegTech applications can be updated quickly and cost-effectively by the vendor, and deployed immediately to all users, enabling firms to quickly respond to new requirements and vastly reduce their technology burden and cost.

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RegTech for Asset Managers

Asset managers must report hundreds of disclosures to multiple different entities. At the same time, they want to reduce the number of systems they rely on for regulatory reporting. They need a scalable solution that can handle a broad range of requirements, facilitate the consolidation of reporting platforms and deliver a holistic approach to compliance management.

In addition, because reporting deadlines often converge at the end of a month, quarter, or year, firms need systems that can handle multiple reporting deadlines at once. RegTech solutions are beginning to deliver that type of functionality. Leveraging the power of Cloud computing, RegTech solutions also provide the necessary elasticity to dial up or down the processing power needed to produce multiple reports at once, and distributed processing helps ensure critical uptime and availability during reporting cycles.

The advanced data analytics and systems integration offered by RegTech solutions also speed up the reporting process. Condensed reporting timeframes have been especially challenging for buy-side firms operating under an outdated reporting model. With RegTech, those challenges can be dramatically reduced, and firms receive the added benefit of getting a clearer picture of their business risk, a function that the back office has not traditionally been able to support. In fact, some asset management firms have said they intend to use RegTech solutions to reduce their reporting timeframes well beyond required regulatory deadlines in order to improve their business performance. This was not the case even 12 months ago—it is a positive and dramatic development that is unfolding at this very moment.

RegTech Will Transform the Asset Management Industry

Asset management firms are demonstrating a sense of urgency to transform their back offices through automation. There is a palpable sense that this goal is no longer a nice-to-have but a need-to-have. This sense of urgency has led to a number of firms allocating more budget to invest in transformation projects leveraging RegTech capabilities. This has already begun to create efficiencies for the firms who have been proactive. They've been able to drive down costs, mitigate regulatory risk and better understand business risk.

RegTech is providing asset managers with an opportunity to review and revamp their business, from the back office to the front. Rather than simply tacking on new single-point applications to an outdated and overgrown platform, asset managers are adopting new and innovative ways to solve regulatory and business challenges. That is ultimately the value that RegTech is providing today—and this is only the tip of the iceberg.

"The back office of the future will be entirely straight-through-processing (STP), with employees focused on exceptions processing only," says Tom Pfister, Global Head of Regulatory Reporting Solutions at Confluence. Rather than being bogged down in the mundane efforts of matching and reconciliations, staff will be freed up to add value, carry out more investigative work in order to reduce risk and ensure clients are receiving the right level of support. Back-office teams will be smaller, with greater levels of expertise.

Ultimately, a more efficient back office will benefit the front office and the business as a whole. Firms will be able to leverage their back-office intelligence to make operational decisions and manage risk in real time.

Improving back-office processing also offers a clear competitive advantage for attracting investor allocations, as institutional investors are increasingly demanding that asset managers demonstrate robust risk management and regulatory processing capabilities.

While the benefits of automation are clear, many asset management firms do not have the time or budget to stay on top of regulatory mandates themselves. Third-party providers, such as vendors and fund administrators, who have the scale and technology expertise to pursue innovative solutions to the industry's challenges, will therefore play an important role in driving the shift toward automation.

Real transformation will not occur overnight. But the long-term trend is towards the increased digitalization of the asset management industry. RegTech is the first real symbol of that transformation. Firms that actively embrace RegTech both for solving their regulatory challenges and for improving their overall business operating model will be better positioned for the era of digitalization, while firms that do not take the long-term view of technology's role in the industry will increasingly struggle.

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About Confluence

As a global leader in data-driven solutions for efficiency and control, Confluence solves tough data management and automation challenges for the asset management industry including performance and analytics, regulatory reporting, investor communications and fund expense management.

Recently launched, the Unity NXT™ Regulatory Reporting platform is a pioneering RegTech solution. The platform's strength lies in its ability to support the entire reporting process for post-trade regulatory filings from one data-centric platform, eliminating the need to use multiple disparate systems. It was built on the foundation of data aggregation and reuse across multiple filings and regions, simplifying and expediting the regulatory filing lifecycle for asset managers and their service providers. As a result, it supports the condensed time frames to meet compliance deadlines that have become the norm for regulatory reporting. The platform delivers speed and flexibility utilizing straight-through-processing with automated exception-based analysis.

All Confluence solutions enable asset managers and third-party administrators to consolidate and leverage data across business operations, which lowers costs, reduces risk, decreases reporting turnaround times and provides Confluence clients the scalability to automate more processes without additional resources.

Our solutions support a wide array of fund types—including mutual funds, ETFs, alternative investments, institutional portfolios and UCITS funds. Seven of the top 10 global service providers license Confluence products and eight of the top 10 global asset managers have business processes automated through Confluence.

Headquartered in Pittsburgh, PA, Confluence serves the international fund industry with locations in Brussels, Dublin, Ho Chi Minh City, London, Luxembourg and San Francisco.

For more information, visit www.confluence.com.