ADVICE MATTERS

The CPD Solution For Financial Professionals

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ComplianceServe

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Welcome to the May edition of

ADVICE MATTERS

Can the summer have started off any worse weather wise - apparently only if you live in Iceland? Hopefully now we will continue to get this warmer sunnier weather we like to expect for our summers!

I'm sure for some of you the weather has been the last thing on your mind as the situation with the Woodford fund has unravelled day by day.

If you are reading the 'Woodford coverage' you will not need us to explain how this edition's three articles align nicely to different facets of the case starting with SM&CR implementation, followed by How financial markets work and lastly FinTech, RegTech, artificial intelligence and compliance. If you haven't read anything about the Woodford situation my first question would be "where have you been?" Secondly, I would urge you to do so – a fascinating insight. We believe it might also be another case of some distributors not understanding the underlying assets of the fund which Barclays suffered with when they were fined £7.7 million and ordered to pay circa £60 million to customers for numerous sales of high-risk investment funds to clients with a balanced risk profile (mainly retired clients).

As an additional element, in this month's edition and from now on we will include links after the articles for our relevant open courses should you want to know more. These courses can also be delivered in-house – all of the training we deliver is CPD accredited.

We look forward to delivering another industry relevant Advice Matters to you in July.

All the very best

The Advice Matters Team
at FSTP

ApEx Standards

The learning outcomes and the ApEx Standards can be found at the end of this edition of Advice Matters

Next month

We will focus on:

- What you should expect from compliance
- How financial markets really work
- Only 6 months to go - SMCR

Recognised CPD programme

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Staying on Track

This section will keep you up to date with the changes in market, product, legislation & regulation.

SM&CR implementation – are you awake and smelling the coffee?

They do say that time flies when you're enjoying yourself. That may well be true, but in this writer's experience time also has the nasty habit of flying an awful lot quicker when one has a looming deadline to hit.

As far as the extension of the Senior Managers and Certification Regime (SM&CR) to solo-regulated firms is concerned, never has a deadline loomed so large! If it's not already marked in your diary, now's the time to draw a big red ring around **9 December 2019**.

This is one of the most significant deadlines to hit the industry since the arrival of statutory regulation many moons ago. There's nothing novel in the principles underpinning SM&CR. Individual accountability, effective governance and the cultural, top-down promotion of good conduct are not new concepts; they've been with us forever, it's just that at certain times the industry has failed to provide government and regulators with sufficient reassurance that it understands and can abide by these principles in practice.

Whatever one thinks about all this, we are where we are and 'SM&CR-Day' is almost upon us.

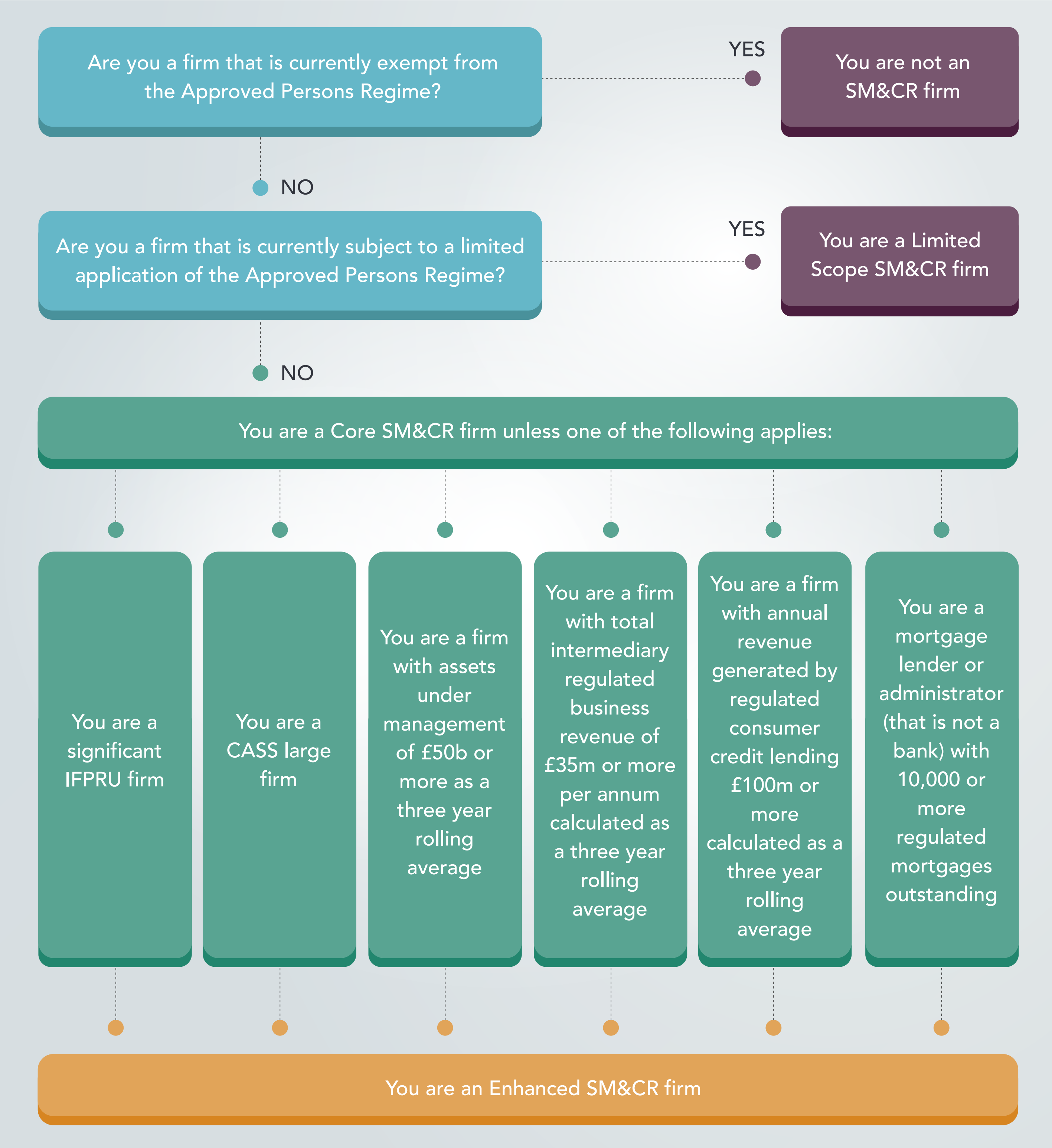
It would be comforting to think that all 47,000 firms becoming subject to SM&CR this December are already well underway with preparing for the new regime. Unfortunately, the noises we are hearing 'off stage' suggest that there are still quite a few firms out there who have either not tuned in to what's happening, or – if they have – don't fully understand what's about to hit them. This is brought into even sharper focus when one remembers that SM&CR is actually made up of three elements – Senior Managers Regime (SMR), Certification Regime (CR) and Conduct Rules, with each one needing particular and close attention to be paid to it.

Important: this article provides you with a general and high-level view of what can be a complicated subject. As with most matters of a regulatory nature, there are quite a few devils lurking in the detail. So, the most important next step – once you've finished reading this article – is to go away and take a closer look at how the new regime will impact you and your firm. The FCA has published some guidance to help you with this and more information can be found here:

https://www.fca.org.uk/publication/policy/guide-for-fca-solo-regulated-firms.pdf

First things first – by now you should have determined what category of firm your business falls into – Limited Scope, Core, or Enhanced.

This flow chart should help you decide where your firm sits in the SM&CR framework:



Source: FCA

The chances are that your firm will fall into the Core category – this is where FCA expects most to sit.

If yours is an Enhanced firm, it will have to fulfil a number of requirements over and above those expected of Core and Limited Scope firms.

There are a number of tasks that must be completed between now and 9 December, although there is a 12-month transitional period which will give firms time to cover-off some of the 'bigger ticket' items that will need to be dealt with. Having said that, there is no time for complacency, so let's consider what needs to happen next…

Your SM&CR pre-implementation checklist:

KEY	
☺	Yes
😐	Maybe/dont' know
☹	No

		☹	😐	☺
1	**Does your firm have its own SM&CR implementation project plan?**			

It's advisable for firms to impose even just some basic project management disciplines on their preparations for SM&CR implementation and to ensure that actions/tasks are identified, allocated to owners and time-bound.

		☹	😐	☺
2	**Have you determined which category of firm your business falls into – Enhanced, Core, or Limited Scope?**			

Very soon, your business should receive a letter from the FCA confirming its categorisation of the firm. It will then be up to your firm either to agree with the FCA's assessment or to push-back accordingly – explaining the reasons for doing so.

		☹	😐	☺
3	**Have you identified your Senior Management Function holders?**			

If it hasn't done so already, your firm must identify who will be its SMF holders (we'll refer to these as 'Senior Managers' from now on). These are the individuals who will need to be pre-approved by the FCA in order to fulfil the SMF role allocated to them in the new regime.

Although there are close parallels to be drawn between SM&CR and the outgoing Approved Persons Regime (APR), this is not a simple like-for-like transition from one regime to the other. For example, certain Controlled Functions (i.e. CF2 Non-Executive Director and CF30 Customer Function) under APR today will – from 9 December – be dispensed with.

The only Non-Executive Directors requiring pre-approval will be those who fill the role of Chair and – in the case of Enhanced firms only – those who are the Senior Independent Director. If you're currently someone who's performing in the capacity of CF30, your role becomes subject to the Certification Regime.

4	**Have you allocated Prescribed Responsibilities (PR)?**

PRs are specific responsibilities, set down by the FCA, which Enhanced and Core firms must allocate to Senior Managers as appropriate (for the record, PRs do not apply to Limited Scope firms). PRs are additional to the inherent responsibilities of a Senior Manager's role and are intended to ensure that accountability for key conduct and prudential risks is properly assigned to named individuals.

5	**Have you prepared Statements of Responsibilities (SoR) for your SMFs?**

The SoR is a single, self-contained document that every Senior Manager will need to have, setting out their role, accountabilities and responsibilities. The SoR should be succinct – no more than 300 words – and clear. The SoR must be submitted to the FCA in support of a firm's application for an employee's pre-approval to be a Senior Manager. SoRs should be reviewed on a regular basis to ensure that they remain accurate and up to date.

6	**Have you identified the individuals who will need to be certified?**

Certification covers specific functions that aren't SMFs but which can have a significant impact on the firm, its customers and/or market integrity. The FCA does not approve these people, but your firm will need to check and confirm (via certification) that the individual is suitable – i.e. fit and proper – to perform the role. This certification must happen whenever someone moves into a Certification Function and at least once a year thereafter.

This means that your firm will need to give sufficient thought to the potential impact this will have on its HR processes, procedures and resources. The amount of work needed should not be underestimated. In order to ensure the robustness of its certification process a firm must review its training and competence (T&C) arrangements – including continuous professional development (CPD), its formal system of performance review/appraisal and the record-keeping associated with these.

It's important to note that fitness and propriety requirements apply to Senior Managers, non-SMF Non-Executives and those performing Certification Functions. This throws into the spotlight – alongside T&C – processes that encompass DBS (i.e. criminal record) and financial checks, along with regulatory references.

7a	**If it falls into the Enhanced category, has your firm prepared the following documents - Responsibilities Map?**

This is a single document that sets out the Enhanced firm's management and governance arrangements. This will include:

- how the PRs have been allocated
- details on who has 'overall responsibility' for the firm's activities
- business areas and management functions
- details of individuals' and committees' reporting lines
- how any responsibilities are shared or divided between different people.

7b	If it falls into the Enhanced category, has your firm prepared the following documents - Handover procedures?	☹	😐	☺

Enhanced firms must take steps to ensure that when someone starts work as a Senior Manager they are provided with all the information and materials they could reasonably expect to have to do their job effectively. One way of achieving this is for their predecessor to prepare a handover note.

The firm itself must have a policy which explains how it complies with this requirement and maintain an adequate record of the steps it has taken to do so.

8	Will all of your firm's Senior Managers and Certification employees have received training on the new Conduct Rules prior to 9 December 2019?	☹	😐	☺

Conduct Rules form the third element of SM&CR. They are a new set of enforceable rules that set basic standards of good personal conduct, against which the FCA can hold people to account. The Conduct Rules can be found in the COCON chapter of the FCA Handbook.

The Conduct Rules apply to employees directly and the FCA's intention is that they should help shape the culture, standards and policies of firms as a whole, whilst improving standards of individual behaviour from the top down and the bottom up.

Two tiers of Conduct Rules apply to all firms.

Tier 1

A general set of five rules that apply to most employees and directors in a firm:

1. You must act with integrity
2. You must act with due care, skill and diligence
3. You must be open and cooperative with the FCA, the PRA and other regulators
4. You must pay due regard to the interests of customers and treat them fairly
5. You must observe proper standards of market conduct

Tier 2

A set of four rules that only apply to Senior Managers, although the fourth rule applies to non-SMF NEDs:

- SC1. You must take reasonable steps to ensure that the business of the firm for which you are responsible is controlled effectively.
- SC2. You must take reasonable steps to ensure that the business of the firm for which you are responsible complies with the relevant requirements and standards of the regulatory system.
- SC3. You must take reasonable steps to ensure that any delegation of your responsibilities is to an appropriate person and that you oversee the discharge of the delegated responsibility effectively.
- SC4. You must disclose appropriately any information of which the FCA or PRA would reasonably expect notice.

So, a Senior Manager will have to comply with Conduct Rules Tiers 1 and 2.

Those employees that fall within the scope of the FCA's definition of 'ancillary staff' will not be subject to the Conduct Rules. This will include the likes of:

- Receptionists
- Property/Facilities Management
- Security Guards
- Audio-Visual Technicians
- Cleaners
- Catering Staff
- Personal Assistants and Secretaries
- IT Support (i.e. Helpdesk)
- HR Administrators/Processors

All of a firm's Senior Managers and Certification employees must have received training on the Conduct Rules, as they apply to the individuals concerned, by 9 December 2019.

9	**Have you established procedures for notifying the FCA of Conduct Rule breaches by your staff?**	☹	😐	☺

A firm must notify the FCA when disciplinary action has been taken against a person for breaching Conduct Rules. Notification is only required if that disciplinary action was because of Conduct Rule breaches.

Disciplinary action' means:

- issuing of a formal written warning
- suspension or dismissal of a person, or
- reduction or recovery of remuneration (clawback).

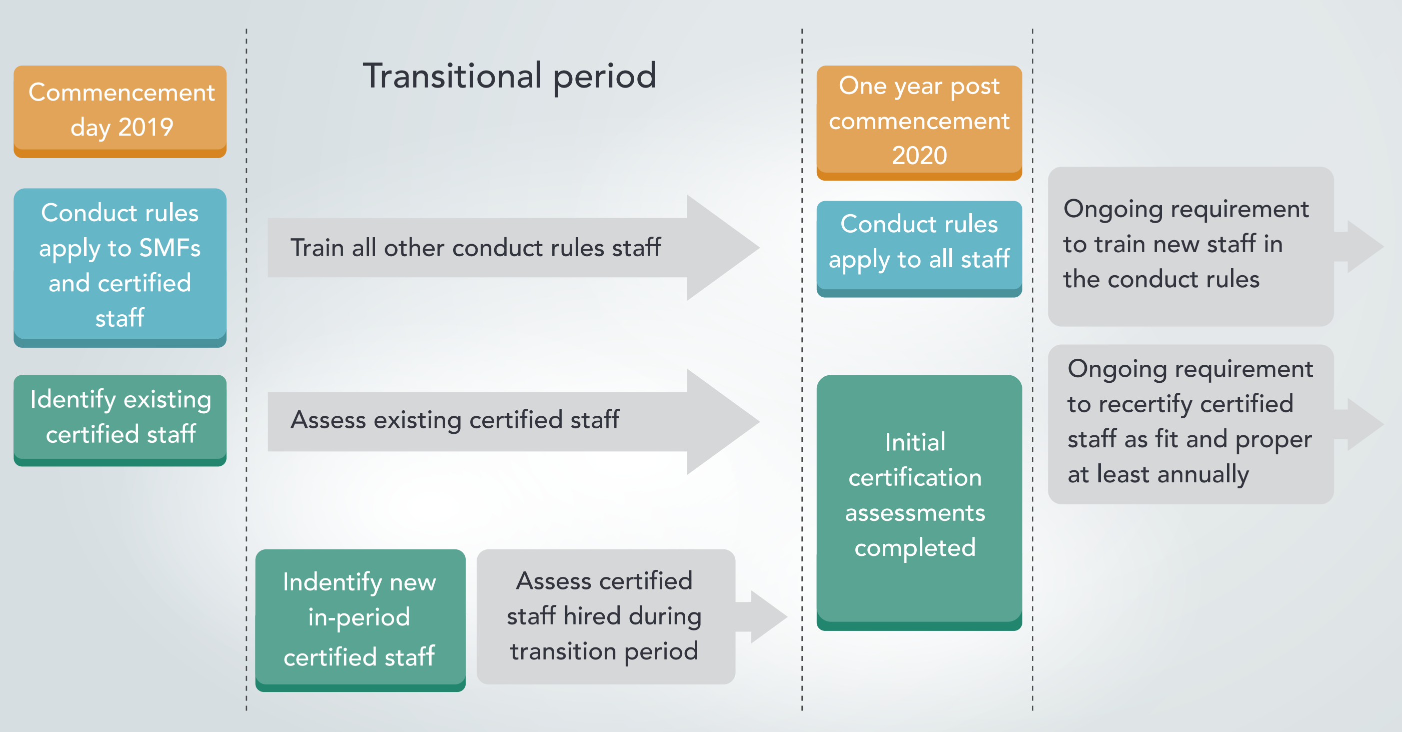
The timing for Conduct Rule breach notification is:

- For Senior Managers: firms must notify the FCA within 7 business days of concluding disciplinary action.
- For other individuals: the FCA requires notification to be made every year via its electronic reporting system, GABRIEL. It's important to note that the annual notification must be made even if there haven't been any breaches (i.e. a 'nil' return).

10	**Do you know what must happen between 9 December 2019 and 8 December 2020?**	☹	😐	☺

There are 2 transitional provisions to help firms move to the new regime:

- Although firms will have to identify their Certification employees by time the new regime starts, they will have 12 months from 9 December 2019 to complete the initial certification process
- Whilst Senior Managers and Certification employees will need to have been identified, trained and abide by the Conduct Rules from the start of the new regime, firms will have 12 months to train their other staff on the Conduct Rules. That training must focus on how Conduct Rules apply in the context of the role the individual is performing.



Source: FCA

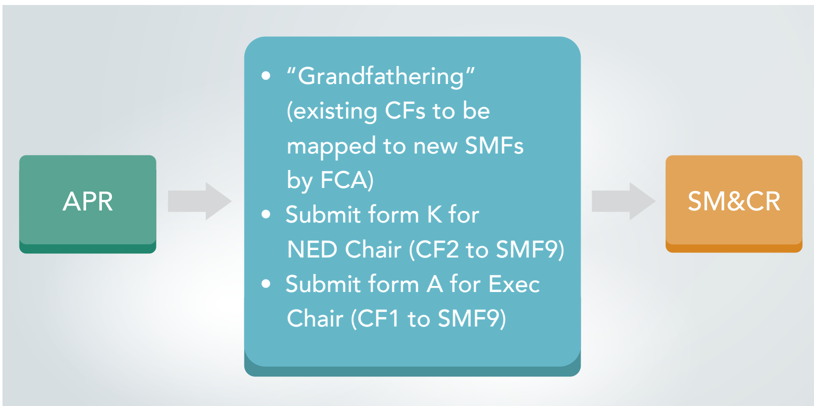
11	**Do you know if you need to submit any forms to the FCA in order to move into SM&CR?**	☹ 😐 ☺

The good news for Core and Limited Scope firms is that their current Approved Persons will be automatically converted to SMFs wherever possible and/or appropriate, with no action required by the firms themselves.

However, firms should consider whether any changes to their approvals are required ahead of SM&CR-day. This will make sure that the move to the new regime is as smooth as possible.

Transition process for non-Enhanced firms

The transition process is more demanding for Enhanced firms. At least one week before 9 December they will have to tell the FCA who they want to assign as Senior Managers, but they won't have to seek re-approval for these people if the proposed SMFs can be mapped directly from the Approved Persons Regime into SM&CR.



There is no need for firms to do extra checks on these individuals when they are converted, as they are already required to make sure that these individuals are, and continue to be, fit and proper.

Enhanced firms will need to submit, as part of a Form K submission:

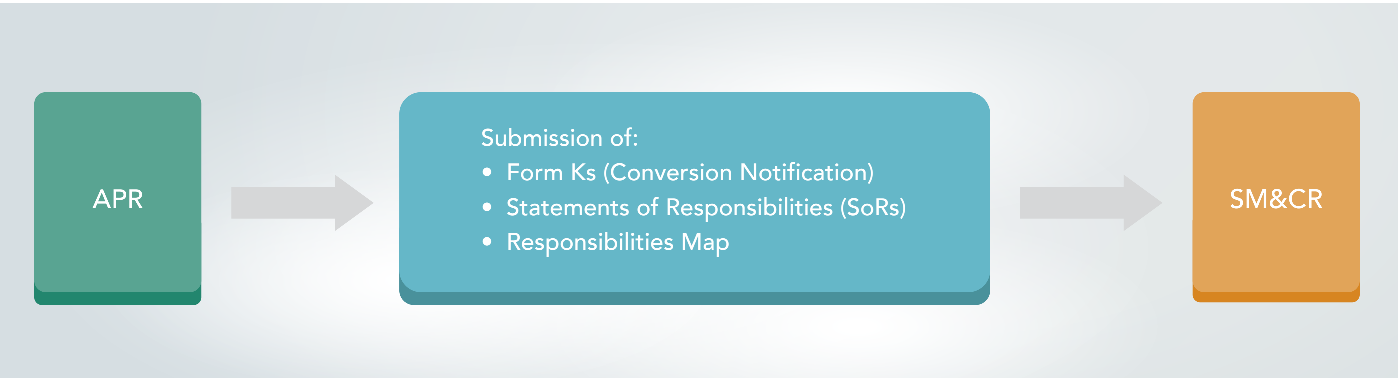
- details of all of the Approved Persons to be converted to SMFs as at 9 December
- statements of Responsibilities for all of the SMFs covered by the Form K
- a Responsibilities Map.

If an Enhanced firm doesn't submit a Form K, it will be in breach of regulatory requirements. Existing Approved Person Regime approvals will lapse and the firm won't have any SMF approvals. As a result, the firm will have no FCA-approved Senior Managers on 9 December and will, therefore, be in breach of the rules.

At that time, the FCA will consider what further regulatory action needs to be taken against the firm and its Senior Managers, including possible enforcement action.

A firm that finds itself in this situation will have to re-apply for approval of individuals through the full SM&CR application process, including mandatory criminal records checks and regulatory references.

Transition process for Enhanced firms



And just one more thing…

12	**Are you comfortable with the state of your preparations for SM&CR?**	☹	😐	☺

Final thoughts

If the majority of boxes you've ticked are Green – that's great. But even if you and your firm are well on the way to preparing for SM&CR's implementation, it's well worth standing back and taking stock for a moment, just to make sure that things are still on track and well positioned for the 'Big Day'.

If you're not so comfortable about the extent of your preparedness (or lack of it!), then it's not too late to get things moving. However, the overriding message is to start now.

Our next open course on the SM&CR – the implications for solo regulated firms is on the 30 July 2019 but we can run in-house courses at a time convenient to you.

Click on the link below to read more details and download a PDF.
https://www.fstp.co.uk/course/the-senior-managers-certification-regime-the-implications-for-fca-solo-regulated-firmsapril19/

Tech Check

In Tech Check we address aspects of technical knowledge that you need to keep abreast of and that will enable you to have better conversations with your clients.

How financial markets work

The cold, hard truth about financial markets is that; "It's all about the money!" So, in starting this article the first point that needs to be understood is "What does money do?"

Money has uses beyond the cash used for small scale transactions. A High Street bank is generally regarded as a safe place to store one's money and hopefully gain a little interest upon it. However, the increasing use of banking "apps" to transfer money from one account to another has meant that the use of notes and coins is declining just as using cheques has. In fact, one starts to sense that money is better thought of as a series of digital entries in the ether.

Money that is deposited in a bank account awaiting use is therefore, not accumulating dust in a vault.

In aggregate it is deployed helping others buy or improve homes or finance a new car via loans. In making such credit available it draws on all the deposit balances so acting as a money exchange to match dormant funds with active needs. The bank will make a charge for such borrowing and the level of the interest charge varies with the borrower's credit rating. A high credit rating, i.e. "AAA/Aaa", secures a low interest charge, whereas a rating that is much lower will require a higher cost of interest be applied.

From the interest charged the bank can reward its depositors and earn a profit from its operations.

What though of the larger markets, for bonds, equities, foreign exchange or derivatives... how do they work?

I will assume the reader knows in principle what is meant by bonds, equities or foreign exchange.

In general, what the borrower does with the capital it has raised is not a concern for the investor, provided the acquired asset is liquid and that the terms of the investment are met in a timely manner.

Markets work because market participants or agents have differing views. At the heart of the market is the price that is quoted by a "market maker". This status means that one is obliged to make a price to a legitimate client when asked... even when the market is fast and volatile.

The "bid" price is that price at which the market maker will buy the asset and the "offer"... sometimes known as the "ask" is where they will sell. The gap between the two is known as the "bid-offer spread" and the more liquid the asset in question then the tighter the bid-offer spread.

One concept that is hard at first to understand is the position of a trading or investment book. If one has no position, one is said to be "flat". On buying an asset, one goes "long". Now, that is quite sensible if one believes an asset will appreciate. By going long, one has bought at a low price and hopes to sell the asset later at a higher price.

There may be a time when one thinks the asset value will decline. If one is long, it would be wise to exit the position before the prices fall too far. However, can one only go back to being flat? If one has no position, must one wait for the asset price to decline before an investment trade can be made?

The answer is an emphatic "No!". One can sell something one does not own or as we say go "short" in the hope that it will decline in value before too long so that one can buy back the asset at a lower price.

The general sentiment is that the real test of liquidity is given by the question "Is there a two-way price?". However, that can overlook the fact that some assets, especially older bonds whose issuer has a low credit rating may be hard to source. Therefore, if a client asks a price, they may be told the asset is "bid only", or the offer is only good in a restricted size. The market maker cannot be expected to offer out the asset if he has no chance of covering the position in the open market.

Consider once again the concept of going short. Say there are two companies, ABC and XYZ who are key competitors in a specific industrial field, maybe car manufacturing or retailing. If one has a gloomy outlook for the economy overall or their specific industry, one may believe the assets will fall in value.

Say one sells shares in ABC when one had no position; one is opening a short. If one is not fully convinced the market will decline the short position is matched by a long position in XYZ. One has in effect "covered" or "hedged" the short so if the market rises instead of falling a loss on buying back ABC's shares can be covered by the profit in selling the shares of XYZ.

However, if one is convinced the market will fall, and the short in ABC is not covered, one is said to be running a "naked short", i.e. it is naked because it is not covered. Put it another way, one is exposed to the market.

I said earlier that the heart of the market was the price. In bonds, by knowing the price and the coupon or regular interest the bond will pay one can calculate the bond's yield. All bond markets have a benchmark and in the largest market, i.e. bonds denominated in US Dollars the benchmark is the US Treasury market.

A new five-year issue by a respected borrower will be evaluated by comparing its yield to that of the five-year US Treasury (T5). The difference in yields is the "yield spread".

The T5 yield (1.876% on June 7th 10:00 BST) is lower as it is the benchmark market. If the new issue carried a yield of 2.500%, then the spread would be given as 2.500% – 1.876% = 0.624% or 62.4 basis points (bps).

If this issuer for five-years would normally trade at a spread of 58 bps, the new issue is cheaper by 4.4 bps and so it can be bought. However, if the usual spread is 66 bps, it is expensive by 3.6 bps and it should be sold. The buying or selling of the bond will bring the spread back to being at its fair value.

Of course, one may not have the room on a trading book to exploit such an opportunity and so just as earlier I considered hedging a short in equities; one could sense the new bond was cheap and so sell the T5 and buy the new bond and simply play the spread as again be exposed to the movement of the bond.

In such a trade the investing client does not want a price as such, instead they want the spread. Many new issues are traded this way and even within the "secondary market" investment portfolios can make small adjustments to the exact percentage of government bonds and high-grade non-government bonds the portfolio holds as they seek to exploit the opportunities in the market. Many spread trades are at the heart of algorithmic or "black-box" programme trades.

Earlier it was suggested that a market maker must quote a price to a reputable client when asked. However, the client may not like the price, or perhaps in a competitive situation a better price is shown by a rival market maker.

There is an exception to the rule and that is when a client asks for a "choice price". That is a price where the market maker will buy and sell the asset. If a client asks for a choice price, they are obliged to trade. It has always been a rarely seen situation, but it does happen.

It all sounds quite straightforward. However, the markets, especially in the 1980s and 1990s were far more prone to abuse. Much of this has been stamped out, but human nature can make the market flawed. Let me consider two forms of abuse and then consider current risks.

Certain players were known as "speculative investors" or "spivs" for short. They would be in touch with the market all the time trying to squeeze tiny margins. They may buy bonds on one phone line from Bank A and instantly sell those bonds on another phone call to Bank B. The bonds went in and straight out for a small margin. This was "backwardation" where one market maker has an offer lower than another's bid. Of course, market makers soon became wary and might make a price to miss.

Spivs were not seen as valued clients although they could be helpful. How so? Market makers would normally deal with one another over the phone or trade anonymously via an inter-dealer broker. This was known as trading on "the street".

Occasionally if they wanted to avoid the street, they could use the spiv to buy or sell for them. This was a practice known as "back dooring". It was not illegal as one could sell or buy bonds with any authorised counterparty. However, it masks transparency. Where there is an opaque market there can be market abuse?

Market abuse arises if financial market investors have been unreasonably disadvantaged directly or indirectly by others who have used information not publicly available or distorted prices or disseminated false and misleading information.

One of the most scandalous forms of abuse is seen in a "market squeeze". A party acting alone or on concert with others can seek to control the market narrative. Cases have been seen in bonds, equities, foreign exchange and LIBOR.

At the heart of such an activity is an agent with significant control over supply and demand of a product who has engaged in behaviour to corner the market with the objective of pushing the price of an asset to a distorted level for personal gain driven by intent to deceive.

The price may be ramped higher or driven lower by creating a false reality that others must chase before they realise what was so obvious.

Markets have changed over the past decade since the financial crisis of 2007/2008. Better levels of regulation have come to the fore although there are still incidents of market manipulation in the differing asset classes. With the rise of algorithmic trading the size and frequency of trading has increased.

The small margins that a spiv looked for appear wide cf. the tiny margins a programme trade may hunt. The process is profitable because of the volumes that are traded.

The risks are magnified given the elevation in transaction size; however also driving the risk is the increasing level of interconnection across the global economy and the instant flow of news and analysis of every data point or comment. There are times when there is too much analysis and one may conclude that words are simply complicated air flow.

What is clear is that all agents must judge the condition of the market carefully to avoid falling for confirmation bias. Ignorance of a fact is now no excuse. In the context of investing, one must accept nothing, believe nothing but consider everything.

Be aware, as "Caveat Emptor" tells us... but be aware of one's responsibilities to behaving properly and making the markets effective, efficient and transparent.

Click on the link below to read more details and download a PDF.
https://www.fstp.co.uk/course/an-introduction-to-financial-markets19/

Skills & Expertise

Personal development is often forgotten or neglected, as it is not seen as important as the other areas of CPD. In reality it can be the aspect that makes the real difference to your clients and your earning capacity. In each edition of Advice Matters we will discuss potential development areas and ensure any regulator focus that aligns to this area is covered in a very timely manner.

FinTech, RegTech, artificial intelligence and compliance

If you work in financial services compliance, especially if you hold the CF10 / SMF16 as Chief Compliance Officer, understanding how artificial intelligence can be used to support compliance as a business enabler rather than a disabler could save your firm time and money.

This article is not about eliminating the human element of compliance but working hand in glove with the technological advancement that is happening in our industry – advancement that we should not ignore.

Not so long ago, the use of computers, the internet and therefore data was not as mainstream. With the birth of Google, Facebook, other giant internet-based databases and the innovation that is happening in companies such as Microsoft, the collection of data has become a focus and an advantage. However, at the same time, it can bring its own problems. Well managed data can make compliance more effective than it has ever been, but it has dependencies, one of them being the quality, experience and knowledge of the human interaction.

Using technology to advance and enhance financial services is the simplest way of referring to the term 'FinTech'. However, a payment services company facilitating international payments for consumers and SME businesses that require an online form to be completed in order to "on-board" with that firm is not necessarily an example of 'game changing' FinTech. The innovative and disruptive side of technology is the really influential part of FinTech – advancing in ways we haven't experienced before when for example we are designing new product and services.

So where did the terminology 'RegTech' come from?

> "In simple terms RegTech uses technological advancements to make the application of regulation for the financial services sector more effective."

Over recent years the number of new FinTech companies would have not been so numerous if it was not for the benefits RegTech offers financial services. The revolution of digital wallets and digital currencies and many other changes would not have been possible if the concept of big data by FinTech firms was not digested and utilised.

Using simple terms again, artificial intelligence or AI, as it is now commonly referred to, is viewed as the next level up, programming a 'machine' in a way that operates better than the human brain. The term 'machine learning' is also another way of referring to the same concept.

> Why is this necessary for financial services?

Let's look at the doctor analogy as we like to do in financial services. In the world of medicine and science, an AI capable computer could facilitate a more accurate and appropriate diagnosis for a patient with less limitation compared to a doctor, who perhaps only has so much knowledge about a certain illness at that moment in time given his personal individual experience and exposure to that illness. The human mind, despite all its intelligence, has limitations that perhaps a machine can overcome and escalate to new levels.

Let's take this into our world – the same machine-driven intelligence could assist in combating financial crime and the prevention of money laundering. If it can predict and understand criminal activity and behaviour and create mitigating actions that work one step ahead of that activity and behaviour, we should see a significant decrease in positive outcomes for the criminal fraternity.

The inter-connection of the global financial sector has made it absolutely necessary for risk management and decision making to be supported differently. Financial services, similar to many other sectors, have been enhanced by the advice provided by AI, specifically in the areas of:

- lending
- risk management
- fraud prevention
- trading
- personalised banking.

Lending

The aim of integrating AI into the traditional methodologies used in lending decisions is to achieve a more accurate assessment of a potential borrower, at less cost, accounting for a wider variety of factors, which leads to a better-informed, data-backed decision. Unlike the human mind, this way of decision making ensures there is no bias in the process.

Risk management

For risk management, the cognitive computing allows a vast amount of data to be processed in a short space of time which can then be used to produce meaningful MI that can significantly assist with risk identification and subsequent mitigation. In addition, algorithms analyse the history of risky scenarios and can alert early signs of potential issues for current and future cases.

The accurate predictions and detailed forecasts that AI can provide are based on multiple variables that usually come from the design of a 'risk-based approach' that an organisation has created. So by design an AI advice mechanism can be fed the rules based on the risk appetite of the business and then the same principles and factors can be applied to large volumes of transactions and user activities. In this case, the business can be assured that it is achieving its defined risk management criteria without worrying about scale, human error and blind spots.

Fraud prevention

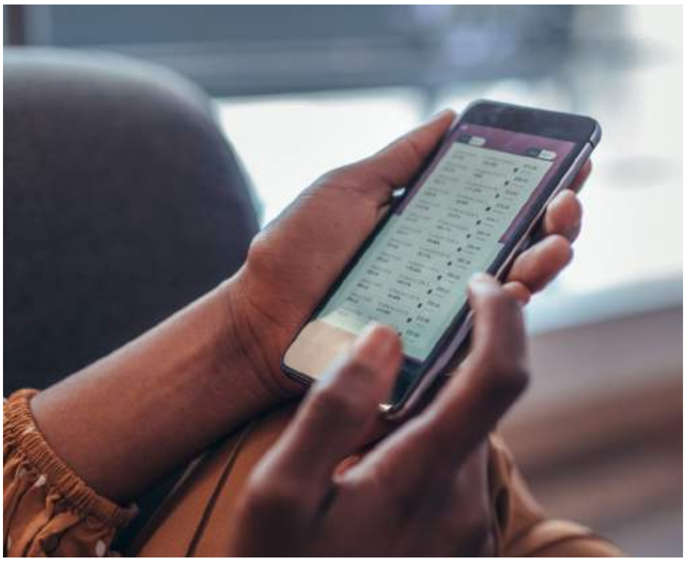
As mentioned previously, in fraud prevention, as machine learning is catching up with the criminals, advice produced through AI is becoming a key player in combating another element of financial crime. AI has proven significant impact on credit card fraud reduction, which is an evolving, on going problem the industry has had to contend with for years. As the more digital, dealing with money and the identities of people behind the money, has become, the more sophisticated the criminal has become in areas such as impersonation fraud.

Trading and investments

In the trading world and investments, AI has assisted hugely with the predictions for stock performance which are far more accurate than any human can predict - algorithms can test trading systems based on past data and bring the validation process to a whole new level before pushing it live. Some global financial institutions trust AI to a point where they manage a number of offered portfolios.

Banking

Banking has become less formal and more customer friendly with the help of AI advice. The majority of the online banking apps, from both the major players and new starters in the market, are making their products more attractive by personalising them based on a user's behaviour. Artificial intelligence programmes can then process these behaviour patterns to tailor the rest of their experience making it more personal and practical – influencing customer retention and producing data that positively impacts on the marketing activities of the organisation.



And … as part of compliance

To ensure there is not unnecessary conflict between the strategical and commercial plans of a firm compared to its compliance agendas and priorities, the compliance function within any company should play an active part in shaping and forming its activities and appetite for risk with the right level of autonomy and influence over business decisions. This will become harder as practical compliance experience retires from financial services.

The intended benefit of AI and the automatic data analysis, especially on a live basis, can reduce the cost of compliance to financial services firms. An analysis carried out by a machine within seconds is both scalable and its costs do not increase based on head count. More importantly it can help to avoid human errors and biases.

In conclusion the AI phenomenon takes the 'what if' scenarios and enables predicted future outcomes with an acceptable level of reliability which become more reliable as more data is collected and analysed – just think where we might end up!

Click on the link below to read more details and download a PDF.
https://www.fstp.co.uk/course/cryptocurrency-and-digital-asset-complianceseptember19/

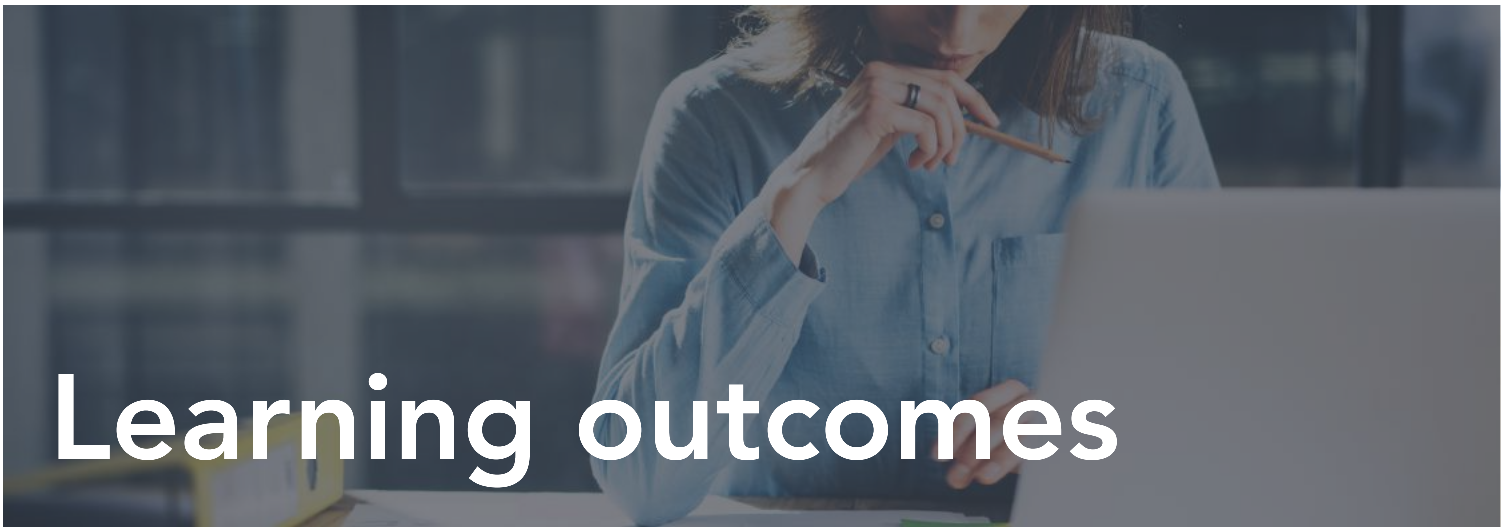
Links to FCA documents

June 2019

Relevant Consultation Papers (CP), Policy Statements (PS), Guidance Consultations, Finalised Guidance and Discussion Papers

Reference	Title	Link
Press Release	FCA confirms the extension of the Temporary Permissions Regime	https://www.fca.org.uk/news/press-releases/fca-confirms-extension-temporary-permission-regime-deadline
Press Release	FCA & PRA jointly fine Raphaels Bank for outsourcing failings	https://www.fca.org.uk/news/press-releases/fca-and-pra-jointly-fine-raphaels-bank-1-89-million-outsourcing-failings
Press Release	FCA appoints new chair for FOS	https://www.fca.org.uk/news/press-releases/fca-appoints-new-chair-financial-ombudsman-service
Press Release	FCA hosts an event for British Steel Pension Scheme Members	https://www.fca.org.uk/news/press-releases/fca-host-events-british-steel-pension-scheme-members
Press Release	FCA confirms biggest shake up in the overdraft market	https://www.fca.org.uk/news/press-releases/fca-confirms-biggest-shake-up-overdraft-market
Statement	Update on the Woodford equity income fund	https://www.fca.org.uk/news/statements/update-lf-woodford-equity-income-fund
Speech	From Innovation Hub to Innovation Culture	https://www.fca.org.uk/news/speeches/innovation-hub-innovation-culture
Speech	Diversity – delivering excellence in the future	https://www.fca.org.uk/news/speeches/diversity-delivering-excellence-future
Press Release	FCA publishes final report on RBS	https://www.fca.org.uk/news/press-releases/fca-publishes-final-report-relation-rbs-grg

Reference	Title	Link
Press Release	FCA publishes final rules on Buy Now Pay Later products	https://www.fca.org.uk/news/press-releases/fca-publishes-final-rules-buy-now-pay-later-products
Press Release	FCA calls consumers to act now re PPI complaints as deadline pressure builds	https://www.fca.org.uk/news/press-releases/fca-calls-consumer-act-now-ppi-complaints-deadline-pressure-builds
Press Release	FCA and CSRC announce their support for Shanghai-London stock connect scheme	https://www.fca.org.uk/news/press-releases/fca-and-csrc-announce-their-support-shanghai-london-stock-connect-scheme
Press Release	FCA publishes first annual report on the perimeter	https://www.fca.org.uk/news/press-releases/fca-publishes-first-annual-report-perimeter
Press Release	FCA announces further action on defined benefit transfers	https://www.fca.org.uk/news/press-releases/fca-announces-further-action-defined-benefit-transfers
Statement	Letter to Nicky Morgan, Chair of the Treasury Select Committee on the Woodford equity income fund	https://www.fca.org.uk/news/statements/letter-nicky-morgan-mp-chair-tsc-lf-woodford-equity-income-fund
Statement	Joint statement on the opportunistic strategies in the credit derivative market	https://www.fca.org.uk/news/statements/joint-statement-opportunistic-strategies-credit-derivatives-markets
Press Release	FCA fines Bank of Scotland for failing to report suspicious fraud	https://www.fca.org.uk/news/press-releases/fca-fines-bank-scotland-failing-report-suspicions-fraud
News Story	Citizens Advice supercomplaint update	https://www.fca.org.uk/news/news-stories/citizens-advice-supercomplaint-cma-update



Learning outcomes

By reading this edition of Advice Matters and applying the learning you will be able to:

Understand the implications of the fast approaching deadline date for implementing the extended SM&CR regime for FCA solo regulated firms
Be aware of the different categories that could be applicable to your firm
Discuss different questions to highlight where your firm is in their SM&CR implementation plan
Clarify how bonds, equities, foreign exchange and derivatives work
Confirm your understanding of what is required for your firm to implement the SM&CR requirements compliantly
State the difference between bid and offer spread
Understand the importance of the test for liquidity
Be aware of how a firm/individual could commit market abuse
Establish the different between FinTech and RegTech
Consider how AI supports the financial services industry and why it is necessary
Verify the part that compliance should play

The ApEx standards

The ApEx standards addressed in this edition of Advice Matters are:

Core or specialist subject	Learning outcome	Indicative content
FSRE	FCA's responsibilities and approach to regulation	The FCA's statutory objectives and the regulatory processes
FSRE	Principles and rules as set out in the regulatory framework	Rules and practices of anti-money laundering and proceeds of crime obligations
FSRE	Different types of risk and how they relate to institutions and individuals	Options for mitigating, eliminating or managing risk
FSRE	How the retail consumer is served by the financial services industry	Industry obligations towards consumers
IP&R	Macro-economic environment and its impact on asset classes	• Economic and financial cycles • The relevance of money, inflation, deflation, interest rates and exchange rates • Role of financial investment in the economy
IP&R	Main characteristics and behaviours of asset classes	• Main types and features of cash and cash equivalents • Main types and features of equities • Concepts of pricing, liquidity and fair value
IP&R	The nature and impact of the main types of risk on investment performance	• Risks relating to liquidity and access • Inflation and interest rates risks
IP&R	Understand the performance of investments	• Portfolio performance

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