

"Clarify economic and financial news to better anticipate and control risks"

A Roadmap to Compliance Framework and Methodology Creation

- ❖ Changes in the regulatory landscape challenge compliance function efficiency and impose that they constantly review their operative model and processes. Hence the need to construct a fit-for-purpose framework, which can provide longevity to a range of applications, both in terms of cost and maintenance.

Compliance risk is broadly summarised as the threat posed to the organisation from a financial, organisational or reputational standpoint resulting in legal infringements, regulatory perspective, codes of conduct or a failure of internal organisational standards.

In order to fully understand the risk exposure which is present, there is a requirement for institutions to formulate a coherent and comprehensive risk assessment process, in order to correctly identify, assess, design and implement controls which mitigate against these inherent risks.

This paper outlines the framework, methodology and process for being able to complete a risk mapping and control plan creation exercise at an enterprise compliance function level within a financial institution.

Framework and Methodology

There are a multitude of potential compliance risks which are inherent within an institution. Therefore, any robust assessment and effective risk map and control plan requires a framework and methodology to rely upon. The framework acts as a visualisation and map of the compliance risk landscape and categorises them by theme, whilst the methodology takes into consideration the objective and subjective methods to assess those categorised risks within the framework.

The process in which a framework is constructed must take into account the eventual use case for the framework, how fungible it needs to be and the number of lenses which are to be applied to it. This paper focuses on the creation of the enterprise framework methodology, which is a generic risk framework, which enables multiple applications across functions and product/business lines, dependent on the lens utilised.

The framework proposed in this paper operates much like a target operating model, in that at the core of the model there is the application of the fundamental rules unique to each organisation of ethics and compliance.

Surrounding this core set of fundamental rules is the first layer of the framework (the elements). These elements are **people, process and technology**, which are broadly categories created by the active fundamentals of actions taken within the compliance department. These fundamentals include, but are not limited to activities such as risk assessments, due diligence exercises, risk mitigation activities, continuous compliance improvement and case management and investigations.

The fundamentals of the first layer of the framework then lead into the second layer of the framework, which encompasses the assessment, design and implementation of these activities. Beyond this level are then the various themes of compliance from a technical perspective, such as security, privacy, fraud and general non-compliance.

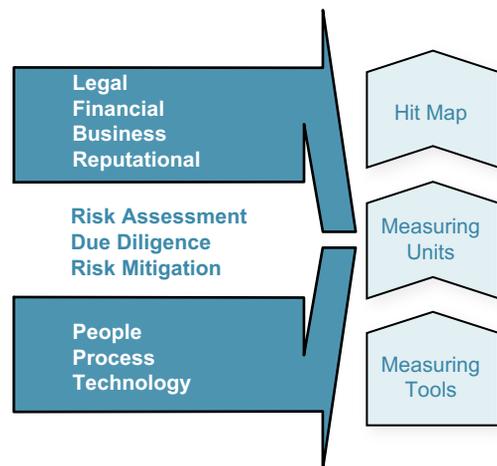


Figure 1 : Framework construction (source 99 Advisory)

Methodology

The methodology is effectively the implementation and application of the framework required within a financial institution. The methodology takes into consideration the potential impact of each risk which allows the organisation to measure the likelihood of an event happening.

Once the likelihood of an event is identified, its impact is measured as an "inherent" risk (a risk that exists in the absence of controls or mitigation plans, therefore creating a baseline or worst-case scenario event).

Commonly, the risk drivers are measured against four categories. These categories are legal, financial, business and reputational. These drivers are not equal in weight, and are custom to each financial institution, because of the variation in risk tolerance both across the organisation, and between different organisations.

The drivers outlined above rely on a system of measurement which is both qualitative and quantitative and as a result, measurement can only be an estimate, albeit based on accurate inputs.

Workshops and interviews from a cross-functional team

There is a requirement for the participation of those individuals who understand not only the risks but also the likelihood of an event occurring in different business lines. Usually, these individuals will be SMEs in their area and are those who are immersed in the business on a day-to-day basis. It is important to get a blend of individuals, critically across various geographies, as the impact and likelihood of an event occurring can vary across geographies quite widely.

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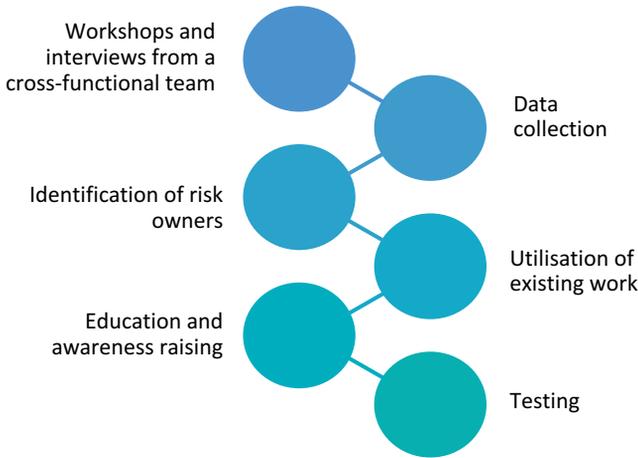


Figure 2 : Process of framework and methodology creation (source 99 Advisory)

Data collection

There will be a requirement to analyse and report on data (both structured and unstructured) on order to test the framework and methodology. Depending on the volume and complexity of data from events such as audit reports, transaction records and compliance exception reports, the data can be used to refine the creation of the framework and methodology appropriately, whilst ensuring it is fit for purpose.

Identify risk owners

With risks, always comes accountability. As a result, it is very important to identify not only those individuals who own the risk should an event occur, but also there should be a clearly documented escalation pathway with defined SLAs as agreed and harmonised within the business unit. This provides a clear level of transparency for both the business at the management level but also to the regulatory bodies, who would expect this to be in place.

Utilise existing work

The leveraging of existing material is a way to both accelerate the time it takes to establish the required controls and framework, but also acts as a harmonisation activity across the various business areas, to ensure that there is synergy and continuity across the policies which exist. Creating a framework in isolation will not appropriately deal with the risks which may present themselves.

Educate and raise awareness

Effectiveness of a framework and methodology only exists if those individuals who operate within it are aware of it fully, along with the knowledge of who risk owners are, escalation points and how to escalate appropriately.

Testing

The testing of the framework along with the methodology is important not only at the outset, but continuously to ensure that they remain fit for purpose and appropriate to a changing business. A repeatable process also demonstrates the variation between repeat tests of the increase or decrease of the likelihood of a risk occurring, its impact to the business and whether or not the mitigation activities remain effective.

Conclusion

Regulatory compliance has affected financial institutions, increasing the cost of compliance and resulting in the delivery of the core compliance elements more challenging, often falling short of requirements both internally and that of regulatory bodies.

As the regulatory landscape constantly changes there is the potential for the compliance function to gain a competitive advantage by successfully navigating this environment, through implementing systematic changes to its operating model and processes, therefore driving more effective oversight and increasing its efficiency. Institutions that are able to perform these changes and successfully make this transition will benefit from a competitive advantage in the future, through being able to deliver better service internally and externally and significantly de-risk their operational positions.

It is clear that is no one size fits all 'template' to compliance exists. However, the framework and methodology outlined in this paper provides the ability to making it possible to structure the approach and components required to construct a fit-for-purpose framework, which can provide longevity to a range of applications, both in terms of cost and maintenance.