

From cost to opportunity: Holistic regulatory change management

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ABSTRACT

Regulations and regulatory change management (RCM) are critical for safeguarding organisations and the overall economy by providing operating guardrails for managing risks. This paper discusses the purpose of regulations, the role of regulators and the need for proactive adoption of a robust RCM framework. It provides a practitioner's perspective for establishing in-house RCM operations, outlining opportunities for adopting regulatory technology to support efficient compliance and organisational growth needs.

Keywords: regulations, regulators, regulatory change management, RCM,

compliance, risk, RegTech, rule analysis, regulatory library, requirements inventory, target operating model

INTRODUCTION

Banks and financial institutions are operating in a regulatory landscape that is evolving at a significant pace, as are the consequences of facing penalties and reputational damage for delays or lapses in adherence. The new era of regulatory changes is presenting both opportunities and challenges for these institutions. Compliance with regulations remains a top priority and these institutions have an opportunity to adopt a proactive approach that may lead to competitive advantage through improved financial performance while meeting heightened customer and investor expectations. It is important to explore and evaluate newer business models and innovative ways firms may collaborate with supervisory bodies to ensure constant evolution of their role as responsible stakeholders in the economic system that deliver sustainable returns.

One critical component of a reimagined future will be a very strong regulatory governance, which is foundational for assuring ongoing monitoring of changes issued by regulators, applicable interpretations and timely implementation, leading to efficient and effective compliance across an organisation. The selection of a suitable regulatory change management (RCM) framework for an organisation depends on its circumstances, growth plans, supervisory guidance, mandatory compliance expectations, process



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and technology maturity and most importantly, budget considerations. Due attention must be paid to immediate regulatory commitments, if any, as well as to existing legacy RCM capabilities prior to embarking on the transformative journey.

This paper presents a view of RCM implementation from a practitioner's perspective and provides one of many possible approaches from concept to operation, addressing the most common considerations along the way. The primary focus is on providing practical guidance for the realisation of an effective RCM function and not on addressing actual regulations.

BACKGROUND

The global financial crisis of 2008–9 ushered in a new era of regulatory change transformation in various banks and financial institutions. Global regulating bodies identified inconsistencies in implementation of similar regulations across jurisdictions, chose to focus on consumer protections, and then introduced new regulations to build consistency. The after-effects of the financial market crisis and the global changes to regulatory frameworks forced financial institutions to rethink their approach to regulatory compliance. This meant that the financial institutions had to reconfigure their compliance infrastructure to satisfy the new directives.

The simultaneous evolution of technology to handle large volumes of data, workflows, improvements in artificial intelligence (AI) to support interpretive capabilities and the fintech evolution made the industry evaluate its approach to solving the problems at hand. The increased regulatory scrutiny and reduced profitability provided an opportunity for financial institutions to scale up their regulatory compliance activities while expanding their business operations amid expectations to do more with less. Since then, the regulatory expectations have

increased with a regular cadence of new compliance requirements.

Also, with the boundaries between financial institutions and technology companies becoming increasingly blurred, the innovations in the space have become an area of focus for regulators worldwide. The lack of formalised regulatory frameworks in the fintech space has led to volatility and forced the authorities to act swiftly to bring order and structure. Regulators worldwide are collaborating and learning from each other about how to establish a stable ecosystem that promotes innovation and allows it to be governed in an effective way to avoid systemic disruption.

THE ROLE OF REGULATORS

The role of a regulatory body is to perform key foundational functions to facilitate an organised financial marketplace. The effective operation of a country's economy, the interests of investors, and the welfare of the general public all depend on a successful regulatory regime that closely manages systemic risks.

The primary goals of these organisations include:

- Ensuring a stable financial system that minimises and manages inherent systemic risks through active monitoring, policy and engagement with the industry;
- Promoting the safety and soundness of individual financial institutions and monitoring their impact on the financial system as a whole;
- Enabling consumer protection and facilitating sustainability;
- Enforcing compliance through supervision and examination.

In the recent past, regulators worldwide have turned their attention to the effective use of technology to conduct their supervisory activities, while simultaneously encouraging

the financial system on the responsible adoption of these technologies for regulatory compliance. As a supplementary process to support the adoption, they have been issuing guidance on the risks associated with technology and suggesting mitigation frameworks to navigate them.

As quoted by the Federal Reserve in the US in its Supervision and Regulation Report,¹ over the past four years there has been an active dialogue among financial regulators and the public on the risks and benefits created by the increasing use of technology by financial institutions. Regulatory agencies have issued guidance to the financial industry on a wide range of topics to address these risks. These topics include operational resilience, third-party relationship risk management, system authentication and access management and due diligence on prospective relationships with fintech companies.

In Asia, as the volume, variety and rate of changes accelerate in the digital economy, the Monetary Authority of Singapore (MAS) and the financial institutions governed by it use supervisory technology (SupTech) and regulatory technology (RegTech), respectively, to enhance regulatory change management. The MAS and financial institutions are investigating and collaborating on opportunities to harness technology to manage tedious tasks and direct the focus and resources to address real problems.

In Europe, the European Banking Authority (EBA) Founding Regulation (EU) No. 1093/2010 mandates the EBA to promote supervisory convergence and facilitate entry into the market of actors or products relying on technological innovation, through the exchange of information and best practices. The aim of this mandate is to contribute to the establishment of a common European approach towards technological innovation. The adoption of technology in the financial sector continues at a fast pace. RegTech, defined as any

range of applications of technology-enabled innovation for regulatory, compliance and reporting requirements implemented by a regulated institution (with or without the assistance of a RegTech provider), has the potential to make compliance more effective in the European financial sector.

Regulators across the world are investing in and experimenting with technology choices for an integrated digital infrastructure to promote more innovation and collaboration. The advancements in: (i) digital currency propelling the world towards a cashless economy with the tipping point being the global COVID-19 pandemic; (ii) expansion of distributed ledger technology (DLT, more commonly known as blockchain) usage in cross-border settlements, clearing and settlement, digital identity and recordkeeping; and (iii) the use of regulatory sandboxes² to develop responsible innovations, all portend significant developments in the coming years related to laws, rules and regulations that govern them. With the blurring of boundaries between traditional banks and fintech firms, regulatory supervision will continue to evolve, leading to more regulatory changes in the near future as regulators seek to advance a digitised regulatory landscape.

Questions remain with respect to how much influence regulations have on financial markets and the avoidance of financial crises, and some economists suggest that innovation is stifled when governments overly regulate the financial services sector. Although the ongoing debate about the optimal amount of regulation continues, there is no doubt that a stable economic system requires a strong regulatory governance framework to manage financial and operational risks.

REGULATORY CHANGE MANAGEMENT CHALLENGES

Companies are dealing with regulation that is expanding rapidly in response to constant

change and transformation fuelled by progress in financial and technological innovation, the changing focus on consumer privacy, stronger calls for a responsible and stable economy through environmental, social and corporate governance (ESG), and better risk management by financial institutions. But not every piece of regulatory news is going to affect an organisation's business and regulatory obligations. Companies need a way to quickly and easily identify, understand and track regulatory changes and obligations to focus on the areas that are most relevant to their business. A formalised RCM framework provides regulatory horizon scanning, applicability determination and adherence capability to enable compliance.

Managing change is the single greatest challenge for organisations in the context of governance, risk management and compliance (GRC). Keeping up with the dynamic and intricate nature of change and how it cascades to the entire organisation is an intense and involved process. Establishing a line of sight through traceability from regulatory change to policy and controls is often a manual and labour-intensive process. Achieving the desired results is frequently challenged by shortfalls in change management, which leads to organisational disruptions of critical risk and compliance activities that enable effective governance. Key factors that accentuate the challenges are:

- *Frequency of regulatory changes:* Since the global financial crisis, regulatory expectations have increased, with a large number of compliance requirements coming at a high frequency. Financial institutions are working with tens of thousands of changes every single year and thus have the unenviable task of evaluating their applicability to the company;
- *Complexity of regulatory changes:* A tremendous challenge of regulatory change is the fact that regulations in one country may affect compliance in many other nations

as well. The cross-border impact of regulations according to the global compliance standards consistently applied across many organisational businesses has increased the complexity of implementations;

- *Sourcing regulatory change information:* The amount of data associated with regulatory changes is massive. Although advancements in databases have made the storage of such data relatively inexpensive, organisations recognise that the handling of this data by overworked change management professionals will be a challenge. As such, the process of sourcing, organising and analysing this tremendous volume of data calls for additional technology support;
- *Implementing the change:* The process of implementation involves the determination of applicability and evaluating the promulgated amendments or newly issued rules in relation to a company's existing obligations. Regulators during their supervisory evaluations not only focus on actual implementation but also on a demonstrable, repeatable process to consistently perform these activities with the changes reconciled within the company's controls, policies and procedures. Manual processes based on siloed pockets of tribal knowledge across an organisation leave the business vulnerable to human error;
- *Budget/resources:* Unfortunately, in many organisations during times of economic downturns, regulatory change management is one of the areas that is expected to do more with less. It is counterintuitive considering that the function operates as the North Star in enabling organisations to navigate risky pitfalls and guide them to a safe harbour. Lately, organisations have started looking at RCM as a competitive advantage — an investment that avoids costly mistakes. But there are ways to go before the full potential is realised through commensurate budget allocations;
- *Sustainable business as usual (BAU) transition:* Companies often develop an RCM

framework, but without focusing on commissioning a good post-deployment plan. The lack of a solid operations readiness plan with clearly identified roles and responsibilities handicaps sustainable compliance through the transition to a well-thought-out BAU process.

With the rapid pace at which regulatory changes are being propagated and technology developments are occurring in RegTech, especially around machine-readable regulatory formats, natural language processing (NLP) and AI, financial institutions should be exploring improved change management frameworks, ably supported by new-age automation infrastructures and innovative vendor service models to optimise operations without exponentially increasing the cost of compliance.

ORGANISATIONAL MINDSET AND A RISK-BASED APPROACH TO RCM

Until recently, many organisations adopted an informal, reactive approach to regulatory change. By definition, a reactive approach occurs when an organisation does the bare minimum to get it up and running and performs regulatory change management as a response to an internal audit, an exam finding or major industry-wide regulatory changes. The company in question is not actively monitoring the developments in the regulatory landscape and often relies heavily on outside counsel for guidance. While this continues to be the preferred approach for smaller companies, it risks leaving mid-sized and larger companies out of compliance and opens them up to financial, legal, environmental, reputational and safety risks. The alternative is a proactive change management approach through the creation of an interpretive office³ and a formalised RCM process.

A common practice in many organisations is to adopt a risk-based approach to

managing regulatory change by considering the highest areas of organisational risk for a primary set of regulators in their jurisdiction. Risk assessments are the most logical starting points for building an effective RCM programme. Taking into consideration the unique set of risk parameters applicable to them, organisations should develop their own target operating models, impact assessment methodology and rubrics for quantification of risks and integrate these within the organisation's GRC strategy.

CONSIDERATIONS FOR A HOLISTIC REGULATORY CHANGE MANAGEMENT PROGRAMME

Once the risks are identified, organisations should meticulously evaluate key external and internal factors and the regulatory environment that influence these risks while establishing a holistic RCM programme. Due consideration should be provided to upcoming regulatory changes, speed of expected response, ability of the current target operating model to support the upcoming changes and if a new target operating model is required, and a solid roadmap to facilitate the transition from the legacy operations.

Often, the reactive mandate provided to the regulatory change function within many financial organisations acts as an impediment to securing appropriate budgets for establishing a holistic RCM programme. But with regulators expecting demonstration of more responsible actions and governance reporting from the board, chief officers of various organisational functions (CxOs) and other members of senior management, due attention is being provided by organisations to make these programmes strategic from a risk and compliance perspective.

Companies should consider key external risks, such as market, geopolitical, societal, competitive, industry and technological forces that are constantly shifting in nature,

impact, frequency, scope and velocity of change. Looking within, an organisation must stay on top of changing business environments that introduce a range of operational risks, such as those involving employees, third-party relationships, mergers and acquisitions (M&A), processes, strategy and technology. Regulatory environments governing organisations are a constant shifting sea of requirements at local, regional and international levels. The effect of thousands of changing laws, regulations, enforcement actions, administrative decisions, rulemaking and more will test an organisation's ability to stay compliant (see Figure 1).

The failure of RCM programmes or their inability to achieve the level of success that was targeted at programme initiation is largely a function of their failure to adapt to the evolution of the various factors discussed above. In a sense, such organisations fail to set a well-thought-out long-term vision for these functions. Many companies may have a well-defined near-term goal, such as the implementation of the London Inter-Bank Offered Rate (LIBOR) transitions or Markets in Financial Instruments Directive (MiFiD), which, when achieved, is considered the completion of the mandate that was

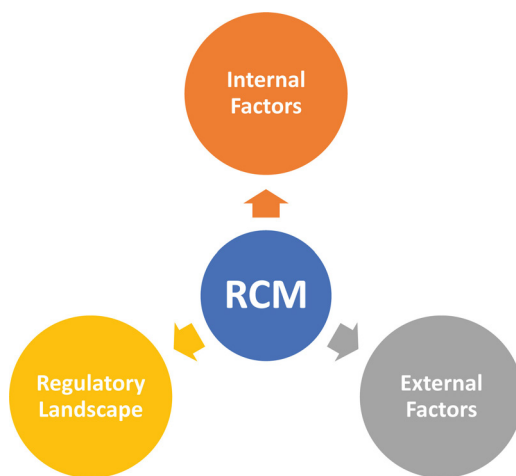


Figure 1 RCM factors

set out, after which point the organisation lacks clarity on next steps.

Figure 2 shows the components necessary to establish a sustainable long-term operation when setting up an RCM programme/function.

The execution of a holistic RCM programme should always be done in phases. Organisations should refrain from trying to address too many objectives at once. This often is the key reason that many regulatory programmes fail. A realistic multi-phase execution roadmap should be developed with specific milestones and measurable outcomes. While there is no right way to break down these phases, care must be taken to ensure that each phase is a logical sub-function or achieves a defined jurisdictional scope that allows incremental improvements to the function.

One preferred way to phase out execution is to consider a regulatory library with a limited, well-defined scope categorised by organisational risk taxonomy, defined jurisdiction, optimal level of granularity and critical issuance types that include only final laws, rules, regulations and guidance. Considering that each of these components could heavily influence the level of organisational regulatory compliance, attention should be paid to ring-fence these decision criteria and formalise the scope through appropriate documentation. Once the scope of the library is formalised, a target operating model to service the scope and keep it current and relevant can be established. After the baseline RCM services are established successfully, the model can be continually expanded across the different components to provide increased coverage throughout the organisation.

In addition to expanding the predefined components, new objectives may be added to progressively build traceability between the regulatory library and policies and procedures, organisational controls, risk assessment frameworks and ultimately,

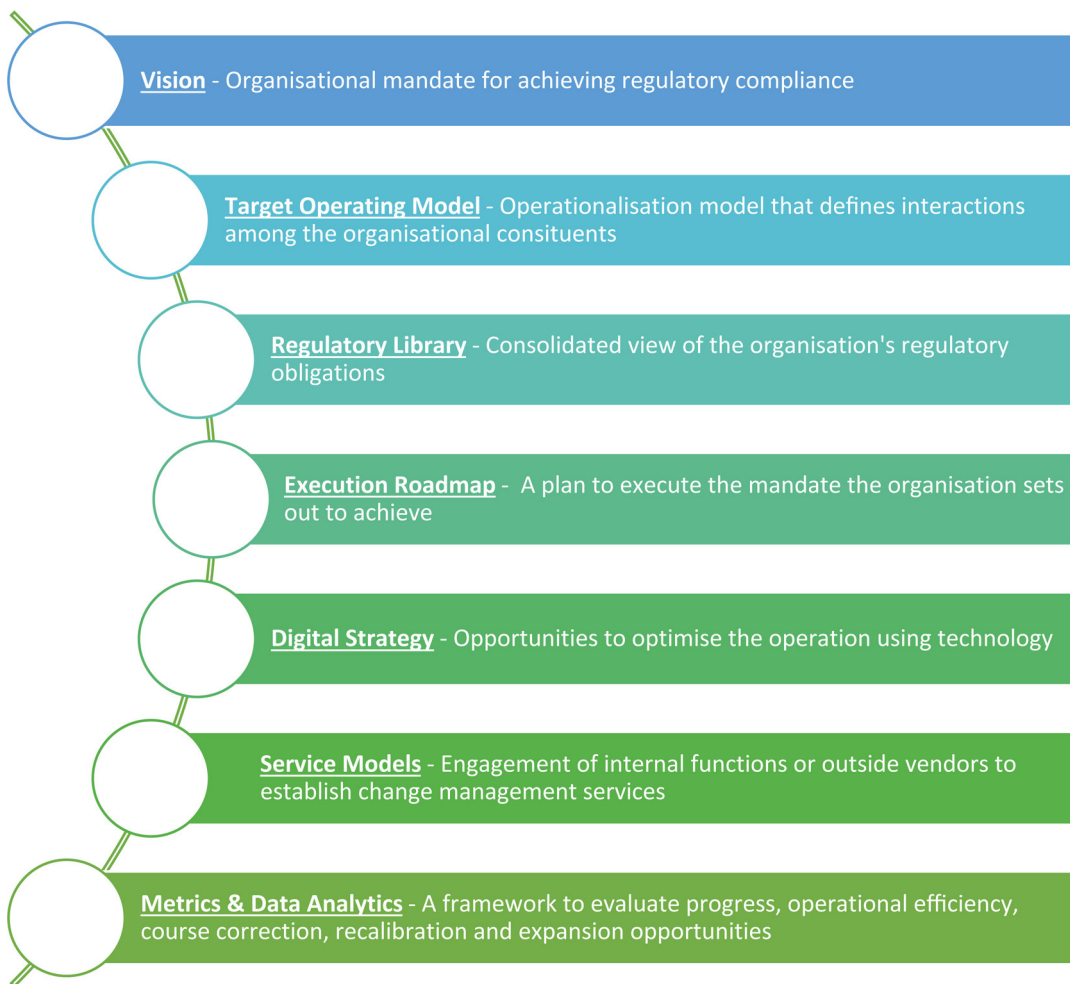


Figure 2 Setting up a RCM programme

to products and services offered by the business units. Establishing this lineage by linking regulatory changes to the systemic risk components of the organisation and the business operations transforms RCM from being a mandatory reactive process to a competitive advantage. It allows companies to comprehensively understand the impact of upcoming regulatory changes on their risk landscape and product offerings. It also promotes the swift evaluation of organisational changes that is rooted in a well-informed cost-benefit analysis and development of an organisational position to

navigate the change with optimal resource consumption.

WHY USE REGTECH TOOLS?

For perspective, the JWG Group,⁴ a London-based think tank, estimated that by the year 2020 some 300m pages of regulatory documents, full of dense language and crucial but often subtle implications, had been published worldwide. And this volume has increased since the pandemic. Extracting the regulatory obligations from these texts and mapping them to organisations has

historically required many hours of manual work.

Regulatory technology, or RegTech, improves this process by:

- Collecting regulatory content in one place and eliminating silos, making it easier to monitor the regulatory landscape while reducing reliance on e-mail/ mailing lists;
- Surfacing/ filtering regulatory changes that apply to a specific company, narrowing the universe to be considered for evaluation;
- Helping RCM professionals organise and triage regulatory changes by mapping them onto the company’s risk and business taxonomy, policies and controls, thereby streamlining the process of assessing impact;
- Updating a company’s regulatory library in near real time;
- Providing continuous insights and data visualisation capabilities.

The implementation of RegTech tools can support multiple stages of the RCM process. At a very high level, the target business architecture for digitisation of RCM is shown in Figure 3. The three key components include capabilities to: (1) harness regulatory data; (2) manage regulatory change; and (3) develop regulatory intelligence, all of which are supported through a strong workflow, analytics and reporting infrastructure along with data storage capabilities.

Any end-to-end RCM life cycle involves an interpretive or evaluation component and a workflow backbone. The interpretation of a newly issued or changed regulations, often referred to as rule analysis (RA), is an intrinsic element of any RCM function with a goal of harnessing regulatory data. It provides an objective analysis of the effects of the rule or change on the organisation through a comprehensive consideration of internal and external factors. A standardised

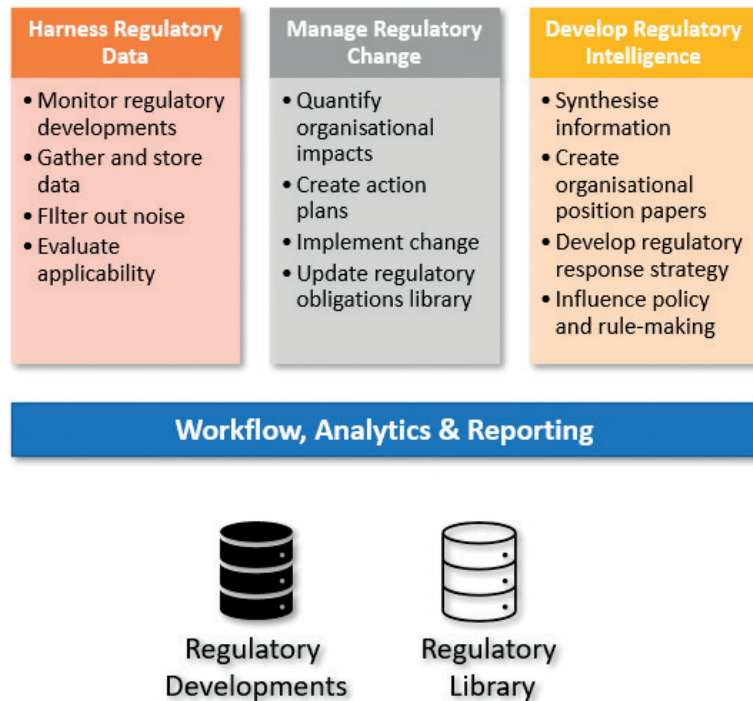


Figure 3 Regulatory change management: business architecture

RA framework is necessary for developing consistent and repeatable interpretive outputs that are unbiased. Guidance on interpretive factors and standardised scoring mechanisms to be considered during the RA should be developed with a focus on benefits and costs of compliance along with other policy options that do not consider implementing the change. This will help the stakeholders clearly understand the economic and reputational risk of not complying with the regulatory change. In addition, a good RA provides evidence of a well-informed decision-making process with a record of the data, assumptions and analyses.

While it is very difficult to automate the interpretive aspects of the RCM process, automating the corresponding workflow may yield significant productivity gains. The key here is to have a clear programme scope without which the programme will not be able to demonstrate sustainable benefits. Key steps in achieving the desired outcomes include:

- Well-thought-out separation of interpretive and workflow tasks of RCM;
- Productivity enabling the interpretive components for faster decision making by providing the necessary tools to the decision makers and making the process consistent and repeatable. For instance, defining an impact assessment framework built on specific factors and introduction of standardised rubrics for the measurement. But there should be scope for professional judgment in the evaluation of impact;
- Automating the workflow processes to speed up the activities;
- Identifying clear roles and responsibilities, and introducing service-level agreements (SLAs) to keep everyone accountable;
- A mechanism for monitoring the change implementation progress through an action planning and status reporting feature;

- Actively involving all stakeholders in the implementation and operationalisation of the RegTech tool;
- Ensuring sustainability is built through active stakeholder engagement after the operationalisation and developing robust metrics to track sustainability.

To again quote the JWG Group,

‘Firms should therefore continue to consider investment in technology, and in the supporting IT infrastructure and associated skillsets, although any such investment needs careful planning. Firms need to be certain that fintech and RegTech will deliver the stated benefits. A well-resourced, highly skilled RCM function will be invaluable in successfully navigating the optimal use of digital solutions.’⁵

RECENT TRENDS AND THE FUTURE OF REGTECH

With the rate at which changes are happening, technology will continue to be a key component in regulatory compliance for most organisations. Regulatory change management is a very involved and resource-intensive process and financial services companies have been adopting technology as a tool to support innovative service models that deploy in-house and vendor capabilities to scale up operations. And in the coming months and years, due to economic uncertainties, most RCM teams will be expected to do more with less.

A recently published forward-looking article, ‘Fintech, RegTech and the role of Compliance in 2023’⁶ by Thomson Reuters Regulatory Intelligence, provides useful insights into what to expect in 2023. The paper published trends based on responses from financial companies that were surveyed and then pooled the responses from Global Systemically Important Banks (G-SIBs),

which are seen as leaders in this space. While RegTech investment slowed down in 2021–2, resulting in a flat year-over-year performance, the time frame covered is still considered a transitional period. Looking forward, the article notes,

‘There remain huge benefits to be gained from the successful deployment of technology, including the development of better risk management tools, the automation of processing, improved tracking of regulatory change as well as the streamlining of data governance, all of which should free up time for more compliance value-add tasks.’⁷

As shown in Figure 4, the positive trend on the perceived benefits of RegTech continues, with most of the respondents feeling extremely positive or mostly positive with better percentages across G-SIBs.

Also, the responses indicate that the boards of financial services companies were

more actively engaged and consulted about RegTech matters, a shortcoming that was also highlighted in previous reports.

The engagement of risk, compliance and other organisational functions in the company’s approach to RegTech has increased; while 72 per cent participated in their company’s approach to RegTech, 27 per cent were fully engaged and consulted (versus 68 per cent and 30 per cent in 2021, respectively). In the G-SIB community, there was a notable increase in the fully engaged and consulted category from 26 per cent to 57 per cent. Additionally, outputs produced by RegTech solutions have continuously gained acceptance for use outside the typical GRC spaces, becoming a trusted source of management information used for strategic decision making.

Finally, there is a consensus among financial services companies not only that RegTech will increase the effectiveness and efficiency of regulatory adherence through

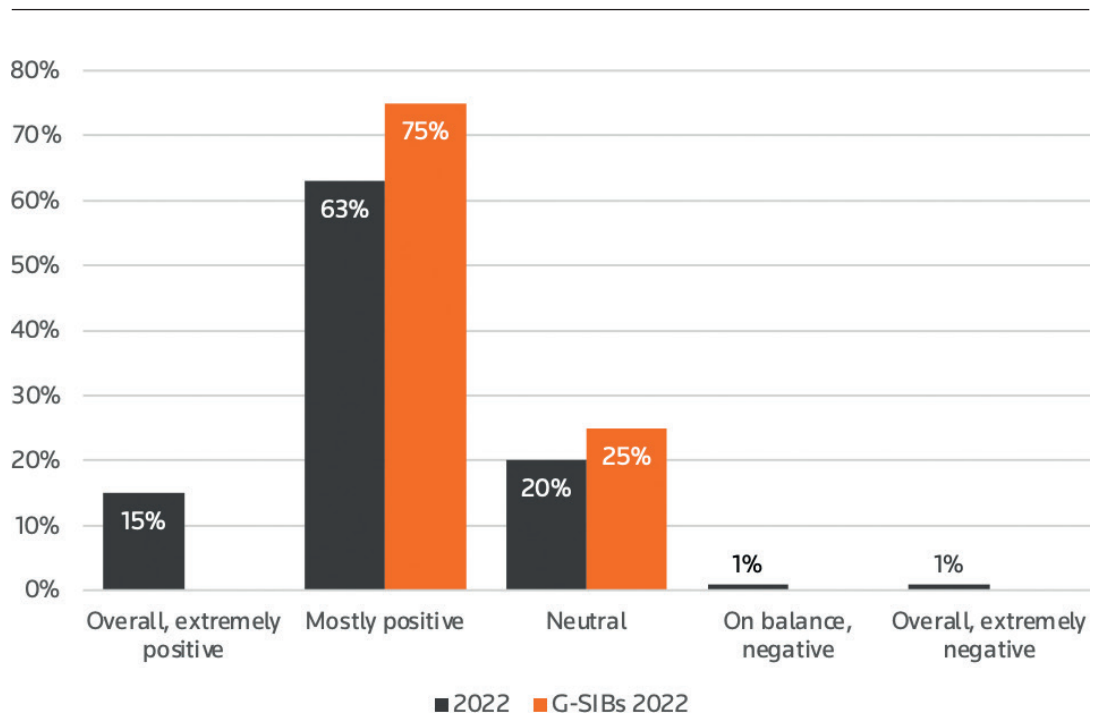


Figure 4 RegTech: What is your view of innovation and digital disruption?

digitisation and automation, but that it also creates issues in terms of investments and the skilled resources required to completely realise and harness the potential of these solutions. As such, companies should focus on ensuring that a sound infrastructure is developed through careful, focused investments alongside the appropriate broadening of existing skillsets to handle the future state as essential components of their regulatory charter to be well positioned for successful operations going forward.

CONCLUSION

A dynamic and holistic RCM framework may be achieved through a comprehensive process to facilitate the real-time, continuous identification and evaluation of global regulatory changes supported by a skilled team of subject-matter professionals. A forward-looking approach that incorporates sustainable and scalable technology solutions will continue to serve organisations well. Care must be taken to proactively establish an interoperable process that traces regulatory requirements (and other change triggers) all the way to the most suitable company operating model, processes and related risk and control framework elements. Companies must take a long-term perspective by anticipating change as a frequently occurring event and not just prepare for transitions caused by major regulatory shifts. Even small events, such as a new interpretation of an existing law, or guidance issued for handling cyber security, may have ripple effects. And these changes also come with great risk. Failure to appropriately address them could result in issues including reduced operational efficiency, customer service concerns, or legal and reputational risk. These issues could have a domino effect throughout the organisation if not handled appropriately. Also,

successful implementation of change does not mean that unexpected factors will not come into play and affect the organisation in the future. All of this could significantly affect the bottom line, with irreversible impacts on the success of an organisation. In contrast, a well-implemented regulatory change management programme is a key risk mitigation mechanism that will leave fewer things to chance. Regulatory change management should be everyone's business and not just the concern of a select few within an organisation.

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