UK Financial Services Practice

Conduct Risk

A Pragmatic Approach to Implementation

2014
“Shaping the future of finance… combining critical thinking with world class delivery”

PARKER FITZGERALD is an award winning professional services firm specialising in the delivery of risk and regulatory transformation within the financial services sector.

We partner with the world’s leading financial institutions to manage the strategic impacts of new financial regulation across the enterprise and deliver market leading capabilities for the risk function.
Executive Summary

Market Observations

With conduct risk now broadly accepted as a principal risk for all firms, the definition of conduct risk remains both unclear and problematic in terms of ownership and implementation responsibility.

Conduct risk frameworks have evolved with the industry setting its own standards in the absence of specific guidance from regulators. Despite this, the challenge remains how conduct practices and metrics are embedded within firms business models and risk frameworks.

The maturity of operational risk and position with the wider risk management framework necessitates a detailed understanding and articulation of relevant conduct risk drivers and a taxonomy that provides an integrated view of outcomes. This is proving to be extremely challenging for firms due to a divergence in views amongst CROs and CCOs with respect to the optimal model for conduct risk governance.

Despite this, over the course of 2013 significant progress has been made by industry in relation to the design and roll-out of group principal risk policies, the initiation of new governance arrangements and the appointment of leadership with associated accountabilities.

More recently firms have been focussed on how best to incorporate conduct risk appetite into strategic decision-making and developing management information to facilitate the monitoring of conduct risk profile against the appetite.

However, it is clear that more work is required if firms are to arrive at a place that allows them to have a full and comprehensive understanding of underlying conduct risk drivers that are both relevant and informative at both the business unit and board levels.

Getting Practical with MI

Given progress already made coupled with the emerging concerns of the FCA as outlined in their 2014/15 risk outlook the key questions remain:

- how do firms implement a conduct risk strategy and underlying framework that addresses an evolving regulatory expectation?
- what are appropriate forward looking metrics and how are these captured within firms?
- how are these metrics successfully aggregated, reported and remediated in line with the firms strategy and overall risk appetite?

Addressing these key questions will depend on many factors including the size and complexity of the firm, strength of governance and positioning of conduct risk. However, common to all institutions is the need to establish a meaningful set of metrics and measurement processes that are underpinned by a responsive MI reporting solution.

This is not only critical to the evidencing and embedding of new and adapted controls, but also to ensuring the alignment of conduct risk strategy, governance, risk appetite and underlying business processes.

To date, many firms have struggled to identify metrics that are both meaningful and helpful in determining required management action. This is primarily down to a limited understanding of how conduct risk co-exists with operational risk and the adjacency of other controls frameworks.

Management information is the key enabler to the successful implementation of your conduct risk framework.
The Conduct Risk Journey: Key Influencing Factors

There are various considerations that need to be taken into account when designing your conduct risk framework.

Conduct risk programmes and associated governance arrangements should be aware of the wider regulatory agenda, key market developments in technology and the broader economic environment in designing their implementation strategies.

| Conduct Risk | Section Two |

Convergence of supervisory expectations in relation to consumer protection and conduct risk.

Pace of technological change is front running the conduct risk agenda as the digital age matures.

Planned structural reform (e.g. Barnier, Vickers, Volker) may have a negative conduct risk outcomes.

Further focus on governance and culture led by the Financial Stability Board (FSB).

Client segmentation challenging due to new distribution channels and contradictions in regulation e.g. MiFID II.

The velocity and cost of regulatory change is resulting in resourcing constraints and budgetary pressures.

Conduct risk programmes should consider these influencing factors when planning their implementation approach.

Success is built on reliable data and insightful management information.
Industry Progress: Our Observations

Whilst good progress has been made on strategy and governance, there are varying levels of maturity across the industry in all other areas. The primary areas of concern are business processes as well as metrics, monitoring and evidencing.

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<th>Processes</th>
<th>Culture</th>
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<td>While many governance frameworks have been successfully formed, banks are yet to articulate specific roles and responsibilities of management – especially with the advent of attestations required under the senior persons regime.</td>
<td>As with overall strategy, risk appetite is well defined at a high level, in many instances prompted by formal FCA requests for conduct risk diagnostics, but banks still have to fully cascade that appetite throughout their organisational frameworks.</td>
<td>There is a significant amount of business process transformation expected from 2014 onwards following the successful articulation of strategy, governance and risk appetite. Chief among the required changes will be evidencing and embedding to reflect the progress already made.</td>
<td>We are yet to see newly articulated strategies transform cultures within institutions – largely owing to a lack of conduct risk incentives including, but not limited to, incident reporting, whistle-blowing programmes, incentive changes and conduct related KPI’s.</td>
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**Metrics, Monitoring and Evidencing**

While 2013 saw banks focus on their strategic thinking around conduct risk, in 2014 the industry is turning its attention to putting that thinking into practice. To a significant extent, this will be achieved through the embedding and evidencing of robust business processes. As yet, no bank has a fully operational MI system in place. The implementation of best-in-breed metrics and monitoring is key in achieving this but this, but is far from straightforward.

A lack of pragmatism in the design and roll-out of the firm’s conduct risk framework poses the greatest threat to its success.
Our conduct risk offering focuses on the implementation of your strategic conduct risk framework, the evidencing of your key controls to accountable stakeholders and the remediation of key areas of concern.

### Conduct risk service offering

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<td><strong>Process Design and Embedding</strong></td>
<td>The translation of conduct risk strategy into a catalogue of core business requirements and processes that require adaptation in order to meet internal risk appetite tolerances. Validation and quantification of process effectiveness covering pre and post sales, execution and documentation.</td>
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<td><strong>MI Reporting and Evidencing</strong></td>
<td>The design of an integrated conduct and operational risk taxonomy to enable a consistent understanding, aggregation and reporting of key controls by risk type, business unit, and activity. Identification of root cause for concern and development of remediation approach and read-across to other areas of conduct risk vulnerability.</td>
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<td><strong>Remediation</strong></td>
<td>The resolution of key conduct risk incidents from either a crystallised risk event or as directed by the supervisory authority regarding an area of concern e.g. Conflicts of Interest. Review and management of remediation efforts to address crystallised risks and / or areas of concern through to closure.</td>
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<td><strong>Deep Dive Readiness</strong></td>
<td>The preparation of senior management and associated stakeholders for FCA deep dives (C1 and C2 firms) and proactive engagement meetings. Production of executive briefing packs, training materials and mock interviews aligned to the scope of the deep dive or review.</td>
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### Programme Delivery and Specialist Resourcing

- Accelerating the delivery of your conduct risk programme through the adoption of our proven delivery methodology and implementation approach that accurately informs the required change effort and resourcing requirements throughout each stage of the framework roll-out
- Provision of interim conduct risk, internal audit and compliance specialists to assist in key areas of remediation under a managed service offering

We combine deep subject matter expertise and delivery know-how with a dynamic and cost effective engagement model to address your key areas of concern.
Conduct Risk: Solving the MI Problem

Parker Fitzgerald and Empowered Systems have recently launched a market leading solution that enables the analysis and reporting of conduct risk metrics. Our platforms enables you to identify and aggregate conduct risk groups, categories and sub-categories at any level and provides critical and real-time identification of conduct risk exposure to help prioritise remediation effort.

Our solution enables you to analyse the likelihood and impact of inherent risk, perform score ranking and identify the degree of residual risk after mitigating actions have been taken by management.

The model is applied to your ‘business activities’ e.g. Sales, Trading, Research, Structuring, Financing and Private Side and is collected from the various business teams e.g. Retail, Corporate Finance, Equities, Fixed Income.

Our conduct risk MI solutions directly enhances the approach firms are able to take towards the identification and aggregation and reporting of conduct risk exposures.
Our Track Record: Conduct Risk and Programme Delivery

**Wholesale Supervision Secondment**
Seconded expert practitioners to the Wholesale and Investment Banking team to advise and help develop industry best practice in relation to the integration of Conduct Risk Frameworks with Risk Appetite and Enterprise Risk Management strategies. This included attendance on a number of client meetings with senior management on a number of thematic issues.

Delivery: 2013

**Financial Crime Assurance**
Appointed to support the creation and integration of the Financial Crime Centre of Excellence. This included the consolidation of multiple assurance teams from Business Services, Corporate and Retail into a single unit to support all aspects of financial crime due diligence, including AML sanctions, ABC and implementing best practice assurance methodology to support the firm’s new approach towards conduct risk.

Delivery: 2014

**Conduct Risk Framework**
Engaged to support the Investment Bank in a number of Wholesale conduct risk advisory and delivery assignments. Supported senior compliance stakeholders through all stages of a FCA Deep Dive review, comprehensive revisions to conflicts of interest matrices. Instigated the development of Conduct Risk Management Information reporting utilising software tools in partnership with Empowered Systems.

Delivery: 2014

**Remediation (IRHP)**
Appointed to provide oversight and challenge to the existing advisory team on relevant regulatory aspects of derivatives mis-selling remediation. Advised on end-to-end aspects of the remediation, from governance arrangements for the remediation management team and the effectiveness of risk and control functions, to advising on conduct issues of the initial mis-selling by front line staff.

Delivery: 2013-2014

**Strategic Risk Platform (FDSF)**
Responsible for the design and delivery of the PRA’s strategic risk platform to support the independent verification of banks’ own stress tests and associated capital requirements. Mandate included the establishment of multi-authority programme governance, delivery of requirements, design of underlying data architecture and integration of vendor solutions into the strategic BoE architecture.

Delivery: 2012-2013

**Post Merger Integration**
Appointed to oversee the integration of the risk management function following the acquisition of HBOS. This included the design and implementation of a new strategic architecture, Basel II ratings system, regulatory application management and implementation of a new operating model to support the enlarged risk function across the Retail and Wealth divisions.

Delivery: 2012-2014

**Divestment Assurance**
Appointed to advise on several stages of the divestment process including regulatory considerations and impacts on the risk and finance reporting operating model; in addition to delivered the strategic risk architecture and rating models allowing ‘Verde’ (TSB) to achieve IRB waiver status in June 2013 resulting in significant capital savings across unsecured and secured products.

Delivery: 2013

**Post Merger Integration**
Following the acquisition of ABN Amro, Parker Fitzgerald was appointed to oversee the integration of global finance functions. This included the design and implementation of a revised operating model to support finance operations in over 52 countries, rationalisation of OD structures and embedding of new business processes and controls.

Delivery: 2009-2011
Your Delivery Team: Conduct Risk Advisory Specialists

Lotfi Baccouche
Partner

• Lotfi is a senior risk management practitioner who brings over 20 years of industry experience to Parker Fitzgerald where he is responsible for the firm’s Advisory and Enterprise Risk Management practice
• A former Chief Risk Officer of a major international Insurance Group, Lotfi has advised the boards of several European financial institutions on key strategies in relation to risk, capital and performance management, governance and regulatory policy
• Lotfi has worked with both the FSA, PRA and Industry on the implementation of Solvency II and has been instrumental in the development of ERM and ORSA strategies for several general insurers and leading Lloyds of London syndicates
• Lotfi holds a BSc in Industrial and Operations Engineering from the University of Michigan and a graduate degree in Operational Research (Master of Engineering) from Cornell University

Ayaz Siddiqui
Partner

• Ayaz is a senior audit and compliance practitioner with over 20 years’ experience advising and building audit teams within leading financial institutions and consultancies including RBS, BNY Mellon, Prudential Insurance, Deloitte and KPMG
• He has an in-depth understanding of conduct risk acquired on a secondment to the Financial Conduct Authority (market conduct, market abuse, financial crime and rogue trading controls) supplemented with experience acquired from first hand experience at a number of international financial services organisations
• Specialist in both buy-side and sell-side operations across Investment Banking, Asset Management, Asset Servicing, Treasury, Capital Markets and IT audit, as well as a detailed product knowledge covering Equities, Fixed Income, Derivatives, Hedge Funds, Trackers and Quants
• Ayaz is a Chartered Accountant (ACA) having trained with KPMG in Leeds

Daren Cheverton
Senior Advisor

• Daren is an operational and enterprise risk consultant with over 20 years’ experience delivering major risk, compliance and internal control initiatives at leading financial institutions
• Darren is an expert in enterprise risk measurement methodologies, control processes and reporting requirements underpinning complex and diverse organisations with considerable and tangible experience in the identification and mitigation of both existing and emerging risks
• Specialist in all aspects of the implementation lifecycle, with particular expertise in end-to-end process improvement and re-engineering
• Darren has demonstrated at board level the commercial benefits achieved through Operational Risk management policy and strategy
• Darren holds diplomas in Investment Operations and Investment Compliance and is a SFA Registered Representative (Securities)

Pauline Lawton
Senior Advisor

• Pauline is a recognised industry expert in both Operational and Conduct Risk management with over 30 years’ experience providing domestic and cross-border regulatory, risk and corporate governance guidance to Investment Banks in the UK, US, Australia and Japan
• Former General counsel and Global Head of Legal and Regulatory Affairs for one of the world’s largest investment banks, Pauline has held the CF10 and CF11 positions and liaises directly with regulatory bodies on matters including major regulatory reviews and event driven investigations
• In addition to acting in a senior advisory capacity, Pauline has a proven track record of delivering both strategic and tactical solutions across a broad spectrum of prudential and conduct related regulatory issues
• Pauline is a solicitor of the Court of England and Wales, and holds a Bachelor of Economics and Accounting and Finance
“PARKER FITZGERALD offers unique insight and compelling solutions for very difficult issues facing the industry today. We work with them because they understand risk and how this translates into our business.”

Group Chief Risk Officer
Global Banking & Insurance Group
We serve clients in over 16 countries from our global office network located in the world’s largest financial centres of London, New York, Singapore and Amsterdam.

Our consultants have an average of 15 years’ experience gained at the industry’s largest financial institutions and Regulatory Authorities.

Our consultants combine sector and subject matter knowledge with delivery know-how to create solutions for our clients that are both compelling and relevant.

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About Parker Fitzgerald: our relationship with the UK regulatory authorities

Parker Fitzgerald is a trusted consulting partner to the UK Regulatory Authorities, comprising the Financial Conduct Authority (FCA), the Prudential Regulatory Authority (PRA) and the Bank of England.

Technical Secondments

In January 2014, Parker Fitzgerald commenced its formal secondment programme with the FCA. Consultants who are selected for the programme have the opportunity to spend three to 12 months within a variety of departments and functions. Throughout their secondment selected consultants have the opportunity to rotate between departments and functions, learning about and contributing towards key supervisory processes and firm reviews.

Skilled Persons Panel (Section 166)

In April 2013, Parker Fitzgerald were formally appointed by the UK Regulatory Authorities to their Skilled Persons Panel. A Skilled Person Review is one of the regulatory tools that can be employed under the Financial Services and Markets Act (FSMA) as amended by the Financial Services Act 2012. Parker Fitzgerald are approved to conduct reviews for; Deposit Taking Institutions (i.e. Banks), Insurance firms, Recognised Clearing Houses, Investment firms and Intermediaries.

Key areas of focus

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<th>Asset Valuations</th>
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<td>Resolution and Recovery</td>
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About Parker Fitzgerald: practice structure

Our core consulting practice comprises of four highly focused centres of excellence

We deliver maximum value by combining deep technical knowledge and delivery excellence with a dynamic engagement model to ensure our clients receive the right level of support at each stage of the implementation lifecycle.
Delivering maximum value for clients requires a dynamic engagement and pricing model that is sensitive to both the complexity and risk profile of the engagement balanced against the benefits of continuity.
About Parker Fitzgerald: Global Locations and Contact Details

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