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# Wealth Management Review 2021

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SECTOR TRANSFORMATION

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CASHFAC

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CONSULTANCY - EVENTS - RECRUITMENT - TRAINING

# Introduction

## FOREWORD

The UK Wealth Management landscape has changed over the last 25 years. Brexit, the pandemic, and a wide range of other factors will create challenges and opportunities for the sector meaning that the sector's transformation will continue in a way that few could have predicted.

During the first few months of 2021, Goodacre UK collected data from over 120 investment executives who provided input based on the experiences at their own firms, combined with future intentions for their respective businesses.

This Review provides an insight into UK Wealth Management based on data from those actually working in the sector.

Financial Services are an important part of the economy and despite many challenges to those companies providing products and services, the obstacles of the past year or so have been successfully navigated.

I would like to personally thank those individuals and firms who have provided input for this review.

**“The obstacles of the past year or so have been successfully navigated.”**



### ANGELA KNIGHT

Angela Knight is the senior Independent Director at Tullet Prebon and Non-Executive Director at Taylor Wimpey, Provident Financial, Arbuthnot Latham and Encore Capital. In addition, Angela is an Associate at Goodacre UK and the Vice President of the Securities Industry Management Association.

Previously, Angela was Chair of the Office of Tax Simplification, Senior Independent Director on the board of Brewin Dolphin Plc, a member of the board of Transport for London and an advisor to PARC and Oxera. Until the end of 2014, she was chief executive of Energy UK and prior to that the Chief Executive of the British Bankers' Association.

Angela joined the BBA from the Association of Private Client Investment Managers and Stockbrokers.

Angela was MP for Erewash from 1992 - 1997, and during that time a Treasury Minister, working for the Rt Hon Kenneth Clarke MP, Chancellor of the Exchequer.

## OVERVIEW

The information gathered during this review identifies several challenges within the Wealth Management Sector but also many opportunities. We have titled the Review Sector Transformation as it is now evident that the Wealth Management Sector is making changes to the conventional way of providing services and operational delivery of the same. In many firms, these changes are happening now, in others they are being introduced. Very few are standing still.

Despite the pressures which arose early in 2020, many firms have adapted to a new way of working and in many instances, identified improved levels of services and more cost-effective operational processes. The development and delivery of digital services

ranks very highly across the board as the area of most interest to the majority of firms. This is followed closely by identifying opportunities to differentiate and increasing the return on capital.

Generally, the Wealth Management Sector recognises that investors want instructions followed promptly with information delivered swiftly, requisites which can only be satisfied via FinTech.

Nevertheless, there remains an understanding that clients will want to make personal contact with firms and the visual communication channels which have been around for a while but because of the pandemic have become universally accepted, will address this need.

FinTech developments coupled with effective APIs are delivering cost effective solutions to the sector, removing the dependence, cost, and frustration of enhancing legacy systems. In addition, outsourcing and third-party services are becoming much more acceptable, particularly within the small to mid-range firms.

Acquisitions remain in focus for larger organisations in order to maintain and increase market share. A number of respondents commented on the possibility of other major entities, perhaps household names not currently involved in investment services, entering the sector having identified opportunities in the UK Wealth Management space.

The majority of firms actively involved in the Wealth Management space are very aware of the changing dynamics but also cognisant of trends which have moved into play that have reduced investment scope for private investors, either deliberately or by accident. These trends include Initial Public Offerings and earlier in 2021, Interactive Investor, Hargreaves Lansdown, and AJ Bell, three leading share dealing platforms joined forces by writing to the Treasury to demand more rights for retail investors during initial public offerings. They say that UK listings have become the preserve of financial institutions for too long and deny retail investors fair access to share offers.

Such moves by firms active in the market point to a trend where changes are being called on by participant firms, rather than by legislators, regulators or for example, stock exchanges.

During the course of this review, a number of respondents were concerned as to a lack of a central focus on issues ranging from but not limited to, the Financial Services Compensation Scheme through to regulation. It is fair to say that a number of executives feel uneasy commenting on issues of concern, particularly where such remarks could be construed as criticisms of the regulators.



### STEPHEN PINNER

Stephen is the Managing Director at Goodacre UK, the specialist consultancy for the finance and securities industries. He has established several businesses on behalf of Goodacre UK's clients, including one of the largest share dealing companies in Europe, two private client Stockbrokers and an Institutional trading firm.

Prior to establishing Goodacre UK, Stephen held board positions at Extel, Hoare Govett, Societe Generale Security Settlements and Cater Allen. He is a regular presenter on business development and operational issues and features regularly in the media on the full range of securities Industry issues.

Stephen is a Chartered Fellow of the Chartered Institute for Securities and Investment (CISI), Director of the Securities Industry Management Association (SIMA) and a Trustee for the Stock Exchange Veterans Charitable Association.

**“Many firms have adapted to a new way of working.”**

**“Investors want instructions followed promptly with information delivered swiftly.”**

## Management summary

The executives participating in this review were asked to consider seven areas of their business and provide comments on the level of challenges.

The first two areas concerned the biggest challenges for their business during the next 18 months and then, the key operational challenges. In each of these two areas, respondents were presented with 6 features now relevant to the Wealth Management Sector.

By taking all responses into account, the biggest company challenges can be summarised as follows:

1st	Increasing Customer "Self Service"
2nd	Differentiation Of The Business
3rd	Increasing The Return On Capital
4th	Consolidation Of Operations Following Acquisition
5th	Changing The Business Post Brexit
6th	Reducing The Capital Tied Up In Operations

Turning to the key operational challenges, these were ranked as follows:

1st	Managing The Mix Of Staff Working From Home With Flexible Returns To Office
2nd	Changes In / Increasing Complexity Of Compliance
3rd	Managing Surges In Online Demand
4th	Increasing Throughput In Operations
5th	Managing The Operational Side Of Acquisitions
6th	Managing Migration Of Technology To The Cloud

The third area concerned BREXIT and respondents were given a choice of 3 alternatives, i.e.

- **No / little impact**
- **Need to expand in the home market**
- **Shift of some operations to EU will take time to settle down**

The vast majority reported little or no impact. The regulatory changes regarding capital was the fourth area. Here, few participants thought that changes were unnecessary but more of an understandable reaction to market developments.

The fifth area considered Intraday Risk Control. This was something considered to be particularly important and likely to become more so as regulators continue to enhance safeguards for investors and

firms. The trend towards comprehensive Fintech solutions was confirmed by the vast majority of respondents.

The Senior Managers Certification Regime (SMCR) featured as the sixth area. Respondents commented that while this was prompting additional training in some firms, it was seen by many as a confirmation of responsibilities rather than a new demand on senior executives.

The seventh area questioned Compliance costs. Many firms reported increases in compliance costs of over 3% in the last three years.

## Challenges in the next 18 months

### INCREASING CUSTOMER SELF SERVICE

From all the feedback received, increasing the range of services offered directly to clients using digital tech, was the area most in focus. Half of all respondents suggested this as the biggest challenge. Open banking is seen by some to be a 'standards' business which will be extended to private client investment services and generally, the main challenge was seen to be for firms to become more user friendly, effectively employing digitally direct service to secure better and more relevant client engagement.

Tech-driven transformation moving to cloud-based operations was also considered to be a significant

challenge. Some respondents felt that companies need to leverage data to form decisions on clients, rather than making calls on investments based on more 'traditional' methods. Unsurprisingly, Robo-advice or 'goal-based investing' was seen as a way forward by those firms offering such services but considered to be of much less interest to others.

This view is quite possibly influenced because some major organisations withdrew their products shortly after launch coupled with the very small profit margins which demand high volumes of trades to become commercially viable.

The FCA Spotlight on accountability performance and fees was also acknowledged to be a challenge as was:

- A lack of sustainability products, especially for younger investors
- Phasing out paper
- Implementing digital signatures
- Retaining talent in the firm
- Organic growth
- "Getting older clients online"

**"The digitally enabled client of the Asset & Wealth Manager will no longer be subject to segmentation. In 3 years, the operating assumption will be that every client will require elements of self-service"**

Greg King, Senior Director, Wealth Management Strategy and Product Development, FactSet

**"It would be easy to look back on the pandemic as a period of curtailment and restricted mobility. However, we shouldn't underestimate the creativity that it has encouraged in terms of both what businesses do and how they do it. The UK Wealth Management sector is no exception, and many businesses have substantially evolved the way they do things. Those businesses that are behind the curve need to up their game if they are to maintain their relevance and satisfy the evolving needs and expectations of their customers."**

Simon Lewis, CEO at Partridge Muir & Warren



### DIFFERENTIATION OF THE BUSINESS

Next to the development of digital services, differentiating the business ranked most highly with almost half of respondents saying this was the biggest challenge.

Traditional family succession (Intergenerational Wealth Transfer) is seen as a less reliable source of business remaining at the firm, given the new investment alternatives coming to the market; it was said that each transfer now sees a roughly 35% leakage of assets. New brands are being developed at some firms, mainly digitally led, for different client types to prevent client loss and encourage new business.

Brand identity was generally seen to be important.

Interestingly, while digitally led services topped most polls, the majority of firms did not consider that completely automated products and services was an overall solution. Many felt that investors wanted to know they could speak to someone and could actually get through on the phone - or indeed via a virtual meeting.

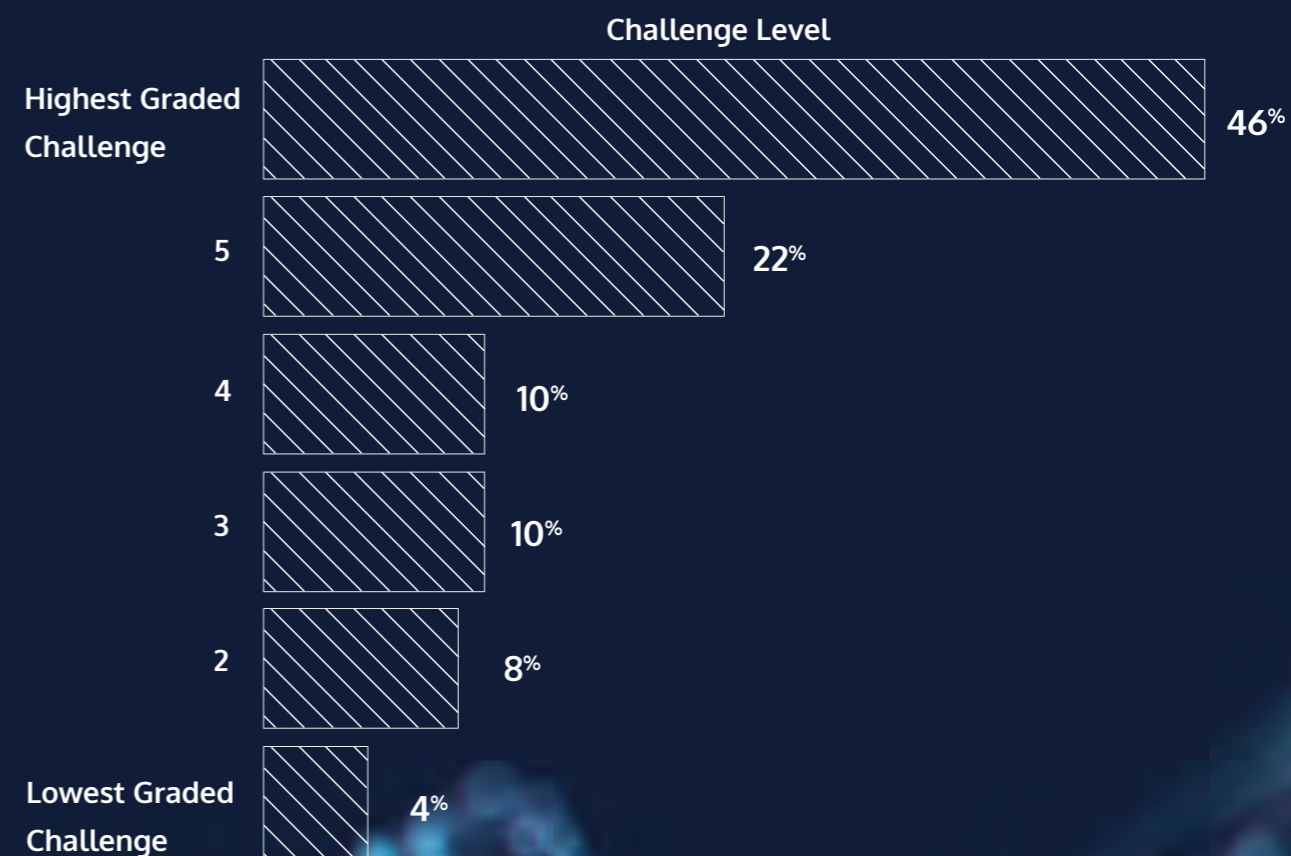
Differentiating businesses via operations has become a major factor with facilities regularly becoming available to deliver truly cost-effective alternatives in many

areas. APIs which support applications not available (or less efficient) from core systems are coming to the forefront of all development considerations. Encouraged by the Senior Managers Certification Regime, most boards recognise the need to understand tech at the highest level to avoid inefficiencies, non-compliance and/or unnecessary costs.

Outsourcing is also now a real alternative for firms, although with relatively few providers which can deliver the full spectrum of pre, post and ongoing support.

**“There are insufficient sustainability products for younger clients. Companies also need to leverage data to form decisions for clients. Succession (Intergenerational Wealth Transfer) sees a significant leakage of assets and firms relying on business from the older generation will suffer”**

Ian Judd, former Head of Client Integration for Institutional Investors UK, ME & SA at BNP Paribas

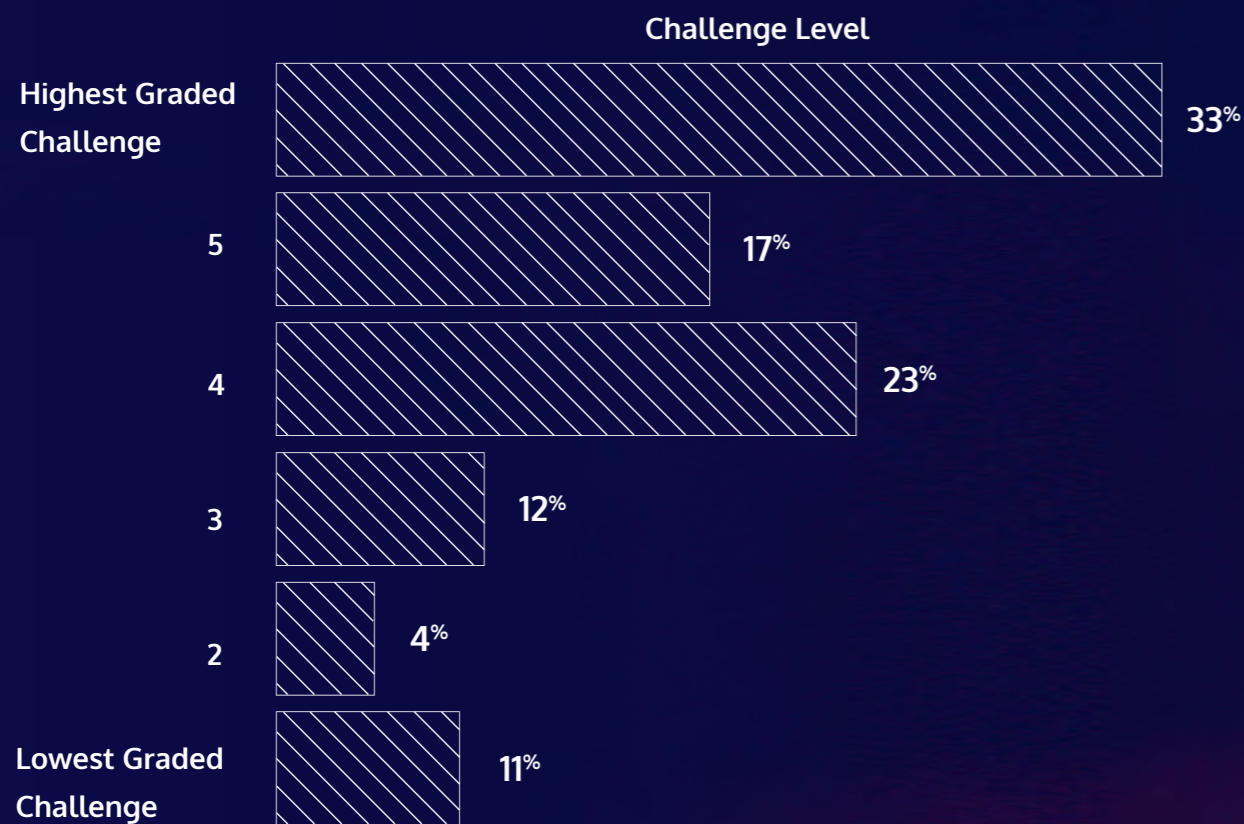


### INCREASING THE RETURN ON CAPITAL EMPLOYED

One third of respondents thought that increasing the return on capital would be the biggest challenge.

Operational costs will become in focus if profitability reduces as a consequence of lower margins or increased competition. In some firms, excessive management layers have already been removed as transformations to more appropriate operating models are implemented.

In addition, the attraction of a variable operating cost base through the use of outsourcing or clearing firms, is becoming more attractive especially for the smaller to mid-sized end of the market.

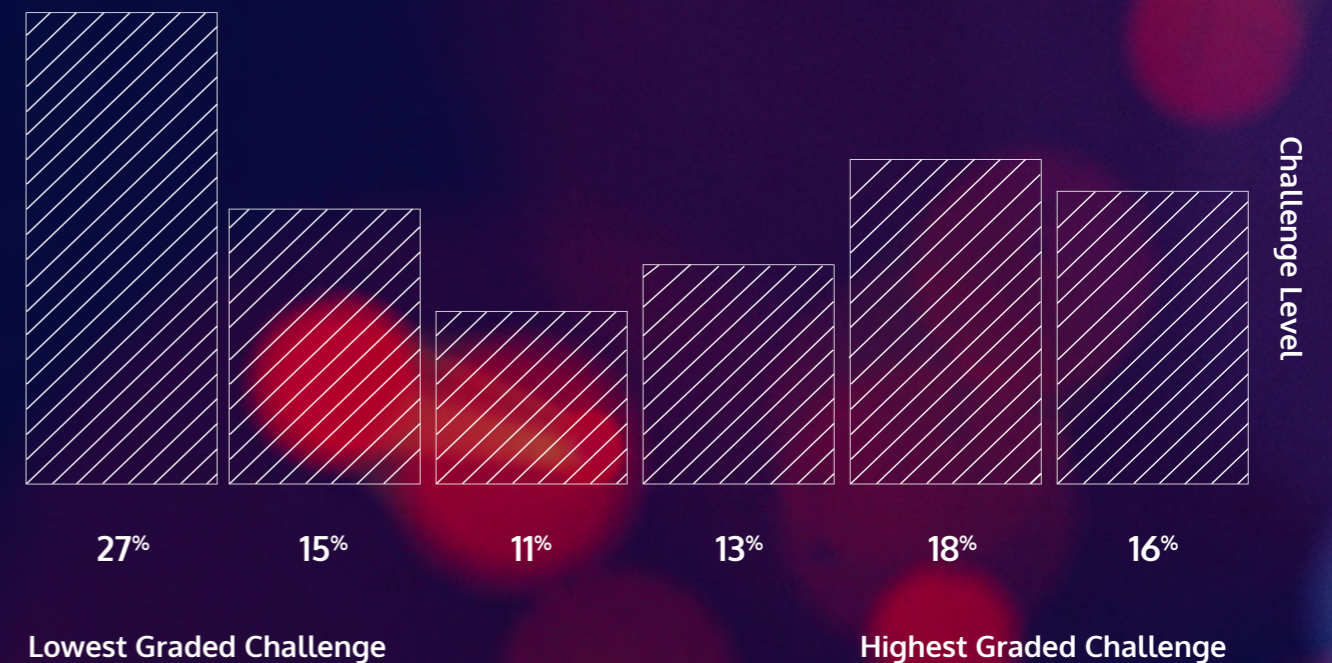


### CONSOLIDATION OF OPERATIONS POST ACQUISITION

Obviously, not all respondents had been involved in acquisitions, hence almost one third of firms dismissing this area as a challenge.

The focus therefore is on the 'acquiring' firms which in the main, while becoming familiar with the process of migrating records and data, recognised the size and complexity of the work involved.

There are a number of aspects to consider, and both the quality and accessibility of information housed on legacy systems from the firm being acquired, are said to present difficulties. In addition, importing transactional history presented serious and expensive operational challenges at some firms.



### CHANGING THE BUSINESS POST BREXIT

Little over 10% of respondents reported that changes to their business post Brexit were the biggest challenge. JM Finn said that servicing funds of EU passport holders requires considerable additional and disproportionate management effort.

Brewin Dolphin said that some operations had moved to their offices in Eire but there were no other significant shifts.

In respect of the feedback

from those interviewed, the majority of participants ranked Brexit the least of the challenges, with just 11% suggesting that the UK departure from the EU posed the biggest problem. The main reason for this feedback is the UK centric focus of client bases, with little or no overseas business.

One of the founders of The Share Republic suggested that

Brexit may assist in a more

rapid expansion of business and possible acquisition opportunities.

Canaccord felt that industry bodies should push harder for a better deal for UK financial services businesses.

Generally, however, respondents felt little or no impact with no need to expand in the UK market to compensate for any lost EU business.



Challenge Level



Lowest Graded Challenge

Highest Graded Challenge

**“Servicing funds of EU passport holders requires disproportionate effort.”**





## Paul Stratford | Expert opinion

EY's Paul Stratford, Wealth and Asset Management Associate Partner, provided his views on the impact of BREXIT on financial services businesses.

Brexit has had an impact on all UK businesses across all sectors. Whether directly or indirectly, significantly, or marginally, it has touched the products, services, and supply chain of millions of companies. Across the Wealth and Asset Management Sector, the biggest factor at play is the extent to which activity is UK or wider focused.

Since the Referendum in 2016, over 30 of the largest asset managers have said publicly that they are considering moving or have confirmed that they are moving some of their operations and/or staff out of the UK as a direct effect of Brexit.

On the Wealth Management side, the majority of the top 20 UK firms, who already had some level of presence in the EU market, have had to enhance their capabilities on the continent, many smaller firms are focused exclusively on the UK market, so Brexit has not significantly impacted

their operations. Perhaps the biggest complication has been retirees moving to sunnier climates, leaving firms with a difficult choice around whether to invest in EU infrastructure to continue serving these clients or to wind down such relationships.

For firms that had an established EU client base before 2016, the pre-Brexit model of distribution to the bloc using significant and scalable UK components, has had to be duplicated in the UK and EU. With over four years of political uncertainty as to what the future EU/UK relationship

would permit in relation to cross-border activity, firms have had to consider everything from the location of their MiFID authorised entities, to the location of relationship managers and booking models. The final deal provided no enhancement of third country cross border provision of services, and equivalence determinations are still outstanding.

In the UK, a reinvigorated policy agenda around the future competitiveness of financial services with a focus on sustainability, fintech and levelling up will support all

managers looking to expand in their home market. For those that have set up new entities in the EU, confidence that the UK will focus on key areas of strength to ensure the continued growth and exportability of financial services will be paramount.

Many firms are focusing on growing their client footprint to make the most of their new infrastructure, and for those that are struggling with sub-optimal costs relating to their EU client base, there will also be M&A opportunities. As the new EU/UK relationship becomes more established,

firms operating in both jurisdictions will need to ensure their operating model strategies are optimal in terms of efficiencies.

While there is no "right answer", not least given the uncertain regulatory environment, making decisions that bring an increased degree of certainty to the operating model will be one of the most important drivers for Wealth and Asset Managers in this post-Brexit environment.

**"Firms operating in both jurisdictions will need to ensure their operating model strategies are optimal in terms of efficiencies."**

**"The final deal provided no enhancement of third country cross border provision of services, and equivalence determinations are still outstanding."**

### REDUCING THE CAPITAL TIED UP IN OPERATIONS (INCLUDING TOP-UPS)

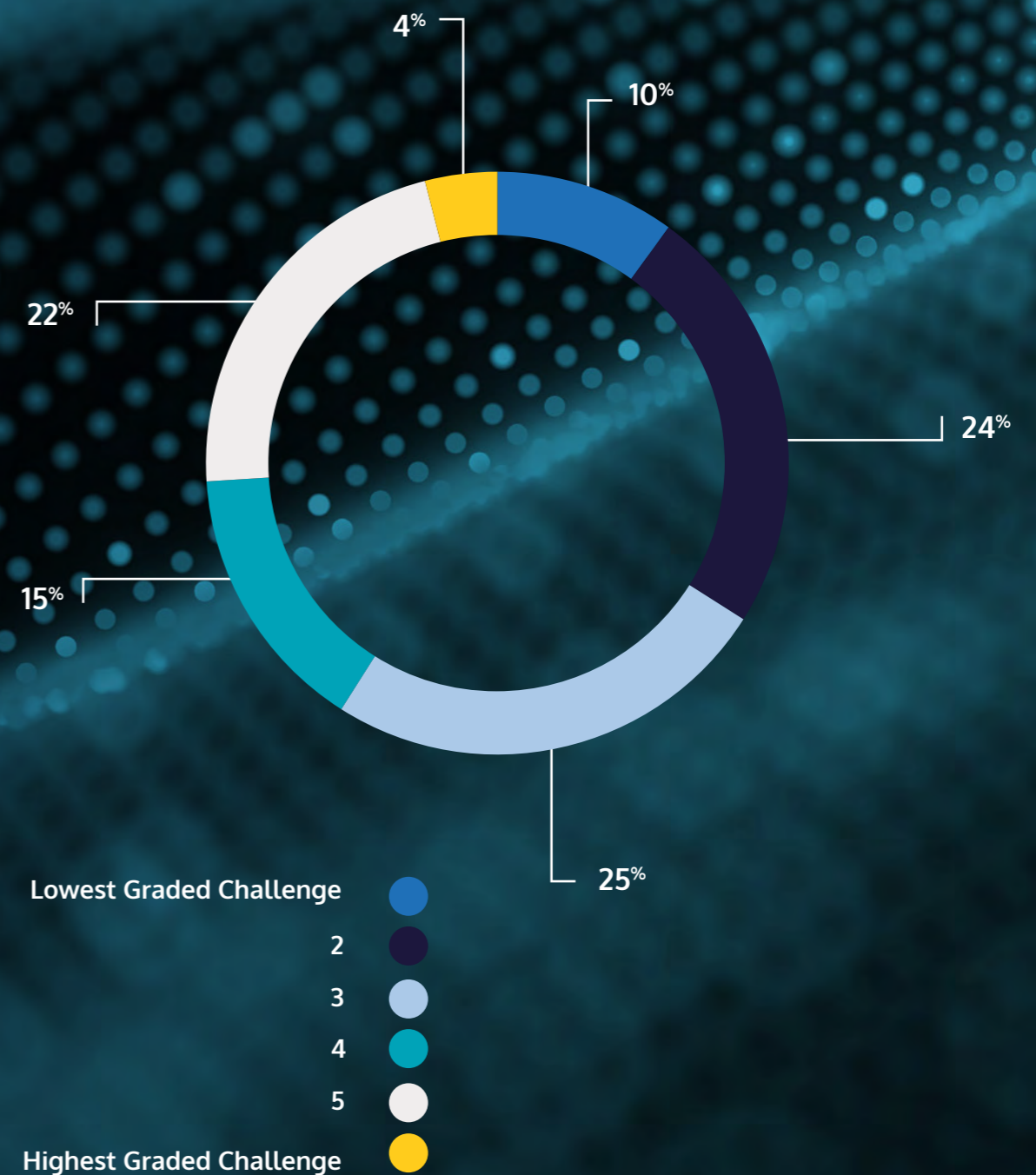
Across all respondents, there was a trend towards reducing the capital necessary for operations, as far as was practical. However, a number of firms acknowledged that by retaining legacy systems, this was difficult on the basis of the manual effort required to support older processes. Some firms were investing in new tech to reduce the amount of 'operational capital' but the cost of migration was substantial, and the improved cost efficiency was said by more than one respondent to be "a few years away"

Some Wealth Management companies have benefited from constant growth in high-net-worth client wealth. This can cover over operational inefficiencies. If this growth decreases, such firms need to ensure their structure is suitable going forward for profitability and an expansion of service range.

It is also now important to consider the 'new normal' working environment where staff may continue to work from home for at least some part of the working week. The survey of respondents as

shown on page 9 (Managing the Mix of staff Working from Home with Flexible Returns to the Office) established a number of factors, including a trend towards 'hot desking', i.e., where desks are shared among employees, to deliver cost efficiencies.

The pandemic has altered clients' expectations for interacting with the Wealth Manager. Some respondents recognise this and are moving to an omni-channel advice delivery model by increasing their digitisation processes.





## Nigel Reynolds | Expert opinion

Nigel Reynolds is a senior executive who has been involved in the securities industry for some 25 years. Following 8 years at Charles Schwab, Nigel joined Hargreaves Lansdown before becoming Development Director at OMX Securities and then TD Waterhouse Corporate Services.

He was then appointed CEO of FIS Platform Securities. He has a comprehensive and extensive understanding of the Wealth Management Sector, having provided outsourcing services to many firms for a number of years. Nigel is now Chief Information Officer with Mattioli Woods,

a leading provider of Wealth Management and Employee Benefits services. Here, Nigel provides his views on the biggest challenges to the sector.

As we emerge from the pandemic, Wealth Managers globally continue to look for opportunities to improve the outcomes for their clients. They want to unlock wealth accumulated during the savings boom, while building out propositions that will attract and retain some of the trillions of pounds that are due to be passed from generation to generation over the next couple of decades.

Coping with exaggerated changes in inflation, markets and other data as the world suffers and recovers at different rates is only part of the challenge. Wealth Managers also need to review their business models and work out what will make them win in an increasingly competitive market. No longer is Wealth Management needed by the wealthy. The democratisation of wealth, driven in part by need and in part by technology, is introducing a new demographic as a source of clients.

This new generation of potential investors is being created through industry changes

such as auto-enrolment and robo-advice. These younger investors will accumulate more wealth over their lifetime than the previous generation, and Wealth Managers need to reach into this new generation now if they are to attract real wealth in the future.

So, what challenges do Wealth Managers face when attracting these clients? Paperwork needs to go. For years Wealth Managers have looked to reduce paper as a way of increasing efficiency and reducing risk; now, any piece of paper that needs a wet signature is seen as a significant barrier to entry to some investors.

Quality of service must become a given. This requires building the confidence and trust that when a button is pressed, or information is requested, it happens seamlessly.

Tomorrow's investors will accept that portfolios will go up and down over time, but they won't accept variations in service quality.

Trust and confidence are also built by providing information on demand that is relevant, timely, accurate, and available across whatever medium the investor is using at the time.

But the biggest challenge Wealth Managers face

goes deeper. As technology advances, Wealth Managers need to decide how they can best add value to their proposition. Do they build, buy or partner? Letting go of things they are good at, and focusing on things they are extremely good at, is a difficult but essential task and the best way to maximise return on capital investment in the business.

Now is the time to decide what type of Wealth Manager you want to be. And the decisions you take now will determine whether you thrive, or just survive.

**“Paperwork needs to go.”**

**“Quality of service must become a given.”**

# Operational challenges

## MANAGING THE MIX OF STAFF WORKING FROM HOME WITH FLEXIBLE RETURNS TO THE OFFICE

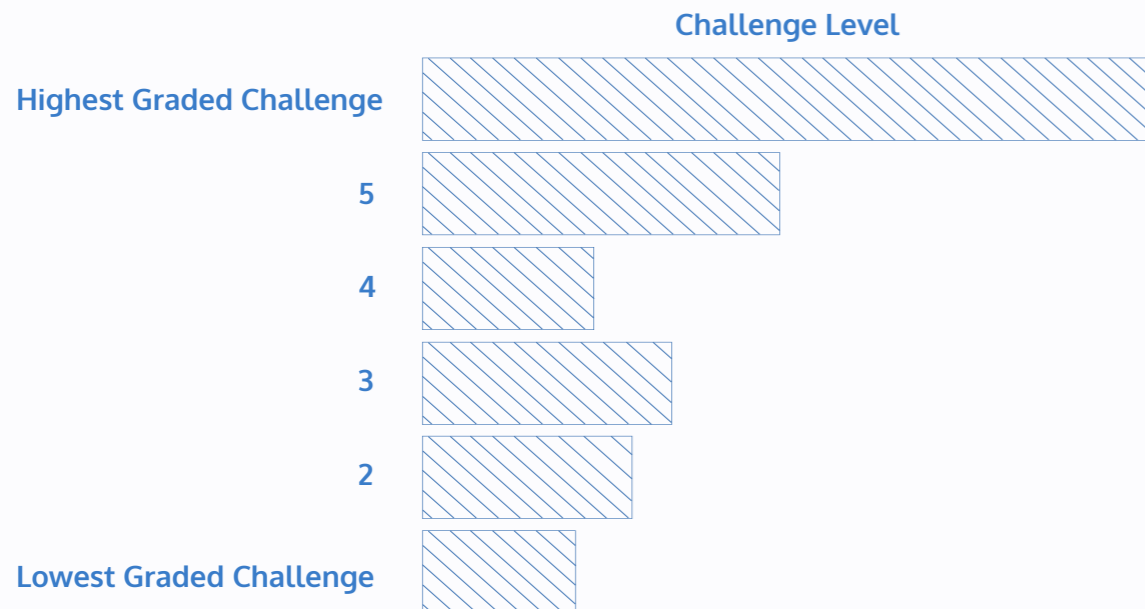
Getting staff back to the office and deciding who should stay at home is seen to be a major challenge by the majority of respondents. Decisions will of course depend on government rulings in respect of commuting and social distancing. Concerns were mentioned that public health policy will continue into the future as was limited opportunities to meet people face to face.

Some respondents said that the pandemic has been tough on younger employees starved of mentorship and camaraderie. In addition, appraising staff and handling career goals had been difficult to manage remotely for a few companies. Overall,

many felt there was a strong possibility towards a permanent shift towards flexible working. Some firms were considering such an approach, coupled with perhaps one day a month when the majority of staff would attend the office. Rathbones has allowed staff to return voluntarily subject to a maximum level.

Canaccord's Sean Taylor said that a hybrid approach was likely to be adopted by many firms. He added that staff should be given the choice for their preferences. Sean also commented that the pandemic had provided an opportunity for female workers with families to become further involved

in the business through the working at home regime. Other firms reported that some staff were keen to continue with working from home, not least to save on travel costs to and from the office. With this in mind, consideration is being given to such requests but at a reduced salary. Working from home has caused some recruitment and management issues with, in some instances, a lack of oversight. Some staff have found working at home difficult due to their available accommodation while some have felt over worked being available 'at any time'. Overall, the sector reports few problems switching from a physical to virtual working structure.



# Complexity of compliance

## INCREASING COMPLEXITY OF COMPLIANCE

Compliance continues to challenge many firms with over one half of all respondents ranking this as the largest or second largest challenge. While there is widespread recognition of the need for effective regulation, the survey noted an underlying unease with the performance of regulators over the past few years.

The fallout from the mini bond scandal and failed firms contributed to FSCS claims resulting in a supplementary levy being charged, of some £78 million, to authorised firms in February 2021. Indeed, the FSCS expects to face a number of challenges in the coming year including continuing vulnerability of customers, a higher number of firm failures

and a growing number of complex claims. The general concern from respondents is simply that if there was tighter supervision of risky businesses, those firms who keep their house in order would not be called upon to contribute such large amounts to investors who had been disadvantaged. The amount of new or amended regulations shows little sign of decreasing and a firm's ability to cope is trending more and more towards digital solutions.

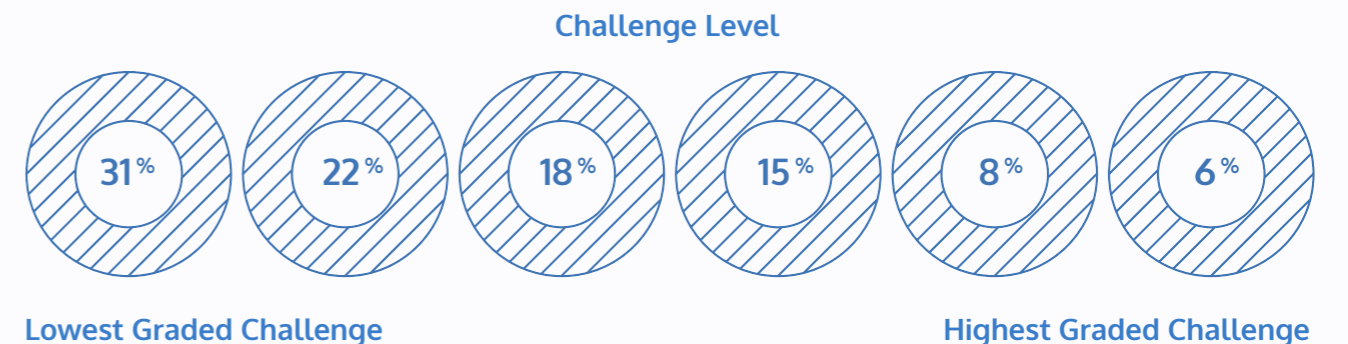
Similarly, the regulators are being encouraged to deliver effective RegTech - regulatory technology. Technological advances involving data science, machine learning and cloud computing provide for more accurate and

reliable ways of coping with regulatory risk. In a way, these developments offer a real opportunity to UK regulators and legislators much in the same way as the awful consequences of the pandemic created the way for invented solutions such as the highly effective furlough roll out from HMRC and the UK governments highly successful vaccine programme.

Respondents commented that RegTech can facilitate real-time market surveillance and predict where problems will arise, helping authorities to be pro rather than reactive. RegTech could also reduce costs with less reliance on skilled personnel performing checks and balances.

**“FCA regulation has been increasing at an alarming rate. More Wealth Managers may walk away from the industry or leave our shores”**

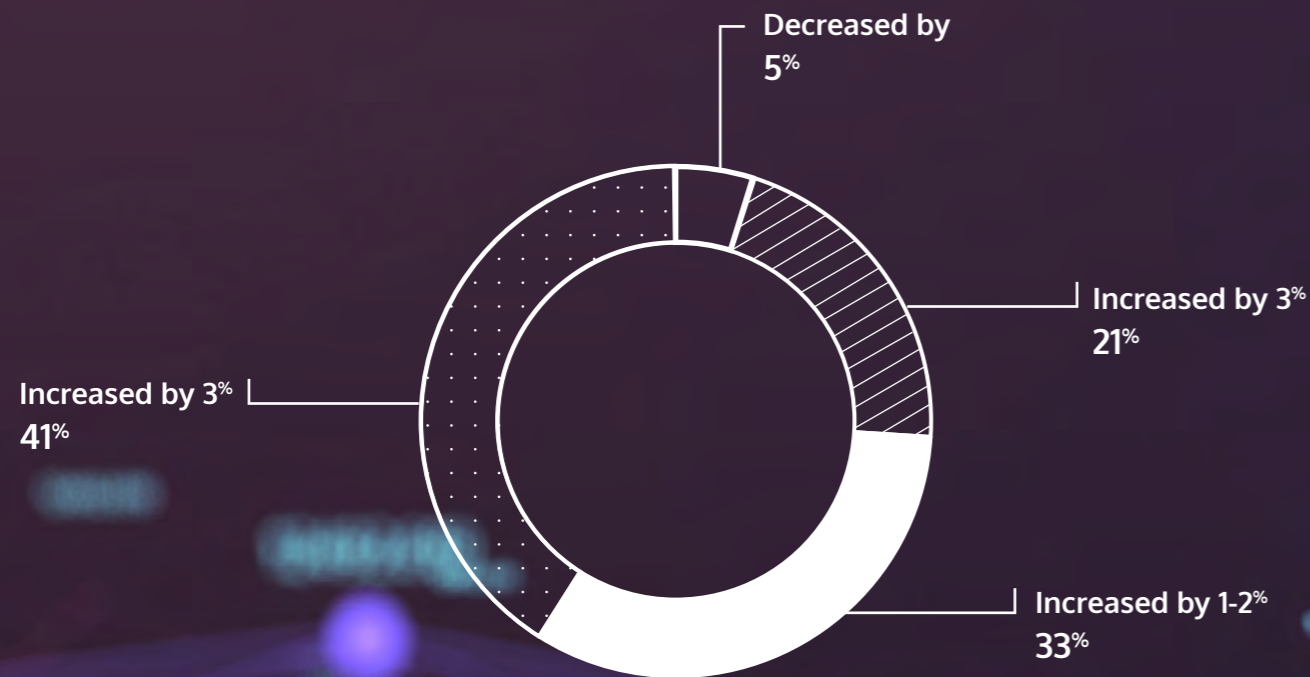
Charles McSwiggan, Director Ceres Securities



### CHANGES TO COMPLIANCE COSTS IN THE LAST THREE YEARS

The majority of firms reported higher compliance costs. In a number of instances, the increased costs were due to additional staff required to ensure that processes remained compliant and that adequate arrangements were being made to meet requirements of new regulations.

There is little doubt that this background is encouraging firms to implement FinTech solutions to automate and replace manual processes and secure cost savings.



**“Cost for just the indemnity insurance & eye-gouging contribution to the Financial Services Compensation Scheme contribute to a double-digit increase. Compliance is the fastest growing expense”**

Simon Lewis, CEO, Partridge Muir & Warren

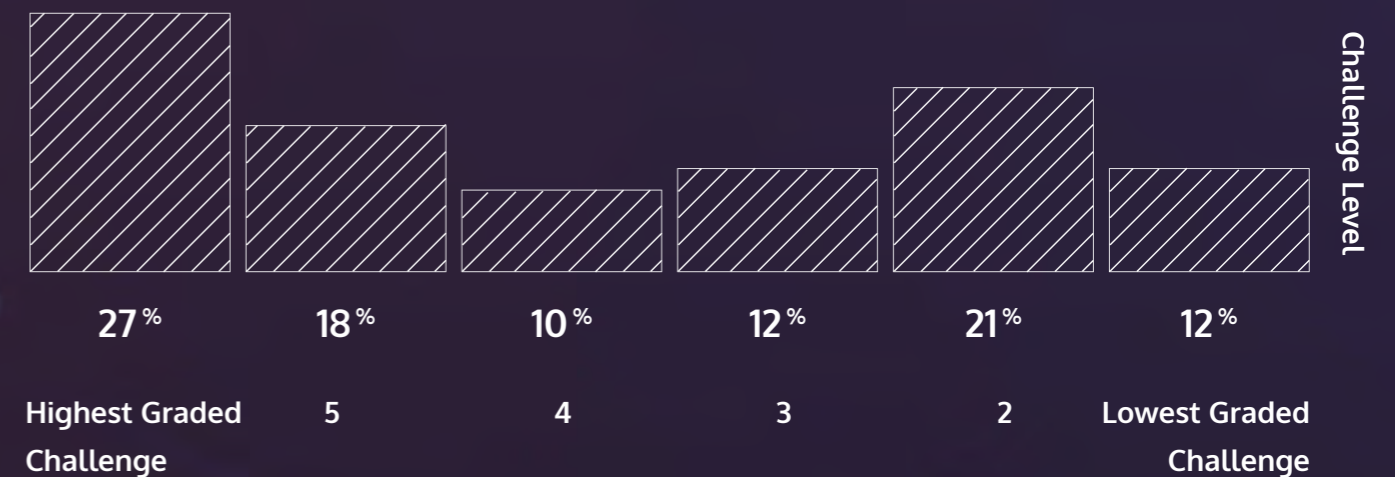
### MANAGING SURGES IN DEMAND

Another major challenge for 27% of firms following the trading peaks in November 2020 when a number of the larger ‘execution only’ share dealing platforms were criticised by clients who were unable to place their dealing instructions.

One firm has since said that they have carried out a detailed analysis and taken steps to strengthen the resilience of their platform during times of unexpected market activity and volatility.

These issues are not new for firms offering low-cost share trading. Before online

dealing was introduced, at times of peak activity clients had difficulty in phoning their brokers to place trades. Engaging the appropriate level of order taking staff was often based on educated guess work. However now, technology is available to avoid all bottlenecks by using scalable applications.



### MANAGING MIGRATION OF TECHNOLOGY TO THE CLOUD

Few companies considered migration to the Cloud to be significant challenge. One respondent for example, had successfully completed a full migration to facilitate

working from home and a flexible approach to a return to work, citing the importance of oversight and control. The overriding concern was with cyber security and while all

Wealth Management firms maintain robust protective measures, the increase in fraud during the pandemic particularly with the main banks, was a subject very much in focus.

**“The key challenges with the flexibility of migrating to the cloud are around oversight and control”**

Ian Clogg COO Fiske plc



### INCREASING THROUGHPUT IN OPERATIONS

One fifth of participants said that increasing operational capacity presented challenges, due mainly to the systems currently employed which required considerable manual intervention and support.

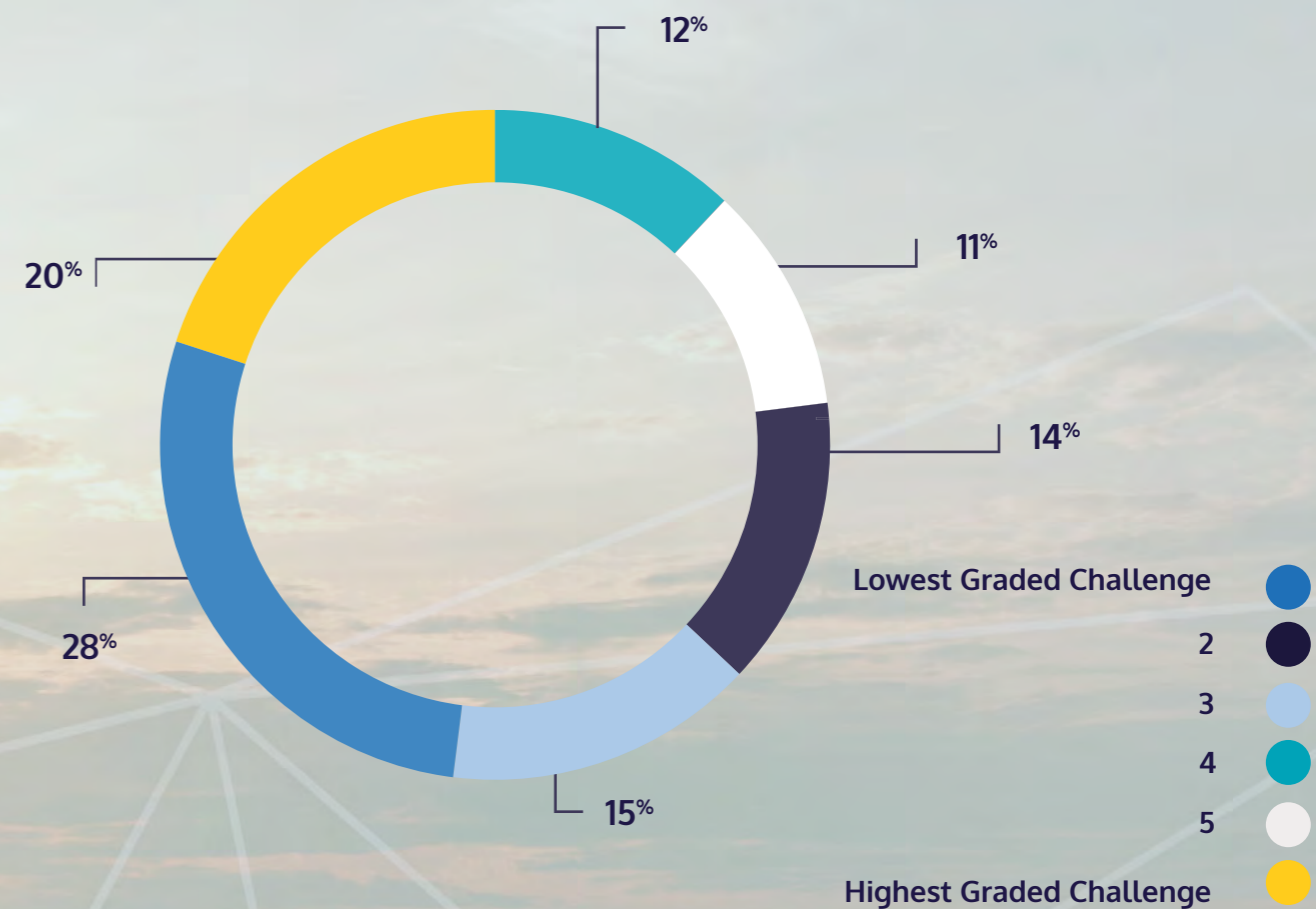
While many firms were moving towards automated processes for tasks such as reconciliations, the use of Excel remains in a number of organisations which of course requires close manual

oversight and management. The use of Excel is similar to the use of other non-core applications, referred to by some as ‘Shadow IT’, the use of applications without explicit company policy approval.

Using standalone applications has grown exponentially in recent years with the adoption of cloud-based software and services. Whilst ‘Shadow IT’ can improve employee productivity and

drive innovation, it can also introduce serious security risks and compliance violations.

To avoid these risks, management in firms adopt policies to ensure that non-core applications can interface seamlessly with the main system architecture and provide reliable and continuous exception and management reporting.



# Operational compliance and controls

## INTRADAY RISK CONTROL

Many firms thought that intraday risk control had become much more in focus both within the firm and not surprisingly, by the regulators.

Many firms already have processes to measure risks on an intraday basis but the extent to which these are automated and integrated varies. Risk management systems which simply provide reports on risk exposure are being overtaken by those which provide alerts before adverse events surface.

Intraday risk control is necessary for traders, who are increasingly turning to applications which include predictive tools using historical data to model portfolios.

As importantly from an operations perspective, companies are adopting solutions which provide control and compliance over

cash management operations. Firms which have ‘followed the rules’ are annoyed with the companies which have failed in recent years due to various factors, including insufficient controls over their business. There is also a strong feeling of injustice as to the current processes following the collapse of an authorised investment business.

In the last few years, the Financial Services Compensation Scheme (FSCS) has been called upon to support clients of failed firms to the tune of many millions. Ironically the FSCS pays compensation because it is fully funded by the financial services industry. Firms authorised by the Financial Conduct Authority (FCA) and Prudential Regulation Authority (PRA) pay an annual levy which funds the cost of running the FSCS service.

Given the significance and complexity of the FCA’s Client Assets Sourcebook regulations (CASS), firms are turning to appropriate Fintech applications. Favoured solutions are those which will not only deliver payments clearance and settlement but will also provide banking interfaces which eliminate the manual task of reconciliations, together with an automated control environment. Such applications are becoming business critical, provide assurances to Senior Managers and importantly, firm evidence of good practice to regulators.

The regulator continues to explore ways in which investors may be protected as far is possible while also ensuring that firms are equipped to assess exposure and measure risks on a more frequent or ideally constant basis.

## SENIOR MANAGERS CERTIFICATION REGIME (SMCR)

Generally, SMCR has forced firms to think about how a system or function might fail because of non-compliance. The regulator reported recently that the regime has introduced changes in the way firms allocate responsibilities, align those responsibilities to

relevant controls and ensure oversight as to how these controls operate. By imposing personal liability, the regime puts compliance in focus for all senior managers.

In some firms, SMCR has created a higher awareness, particularly in “the front office”

of responsibilities for senior managers which previously were not necessarily in focus. Many firms mentioned that SMCR had created concerns for managers as they could be held to account for failings in the firm due to, for example, inadequate systems.

**“SMCR provided the opportunity to revisit areas of ownership associated with the workflow and ensure areas of responsibility were understood and documented”**

Eric Moe, Partner and COO, Whitefoord

**“SMCR prompted stronger focus on qualifying employees and added an additional demand on training, making individuals aware of their own responsibilities”**

Mark Powell Head of Charities, JM Finn



## FCA regulations regarding capital



### Tim Dolan | Expert opinion

The vast majority of firms interviewed considered that the regulatory changes were an understandable reaction to market developments which firms of course, needed to adapt. Tim Dolan was also invited to comment.

Tim is a highly experienced financial services lawyer who began his career working for financial services regulators initially in New Zealand and then with the Financial Services Authority in the UK. He has extensive experience of advising on the scope of the financial services “perimeter” in the UK and the impact of different financial services directives including MiFID 2; the Capital Requirements Regulation; and Payment

Services Directive 2. Tim routinely helps financial services institutions to ensure that they have the correct permissions to operate in the UK and in Europe and routinely interacts with the PRA and the FCA on behalf of clients as well as with European regulators. The new regime contained in the EU’s Investment Firms Directive and Regulation (IFD/IFR) package that comes into force in the UK on 1 January 2022 is an understandable development.

It recognises that the current Capital Requirements Directive and Regulation derived regime is not suitable for the majority of investment firms (because their risk profile is nothing like that of a banking

group). However, the new regime is anything but light touch for Wealth Managers and many will see their capital requirement increase (although there are some helpful transitional provisions).

By way of reminder: Class 1 firms are those which take on principal trading risk and/or have assets over €15 billion. At the other end of the spectrum Class 3 firms are those who meet a number of stringent conditions including (but not limited to!): holding no client money and no client assets; having AUM of less than €1.2 billion; having no principal trading positions; holding a balance sheet of less than €100 million; and having total annual gross revenue from

### “K-Factors are one of the biggest changes.”

financial services business of less than €30 million.

Some Wealth Managers will fall within Class 3 and may have a manageable requirement of the higher of either a permanent minimum capital requirement (PMCR) of €75,000 or a quarter of the firm’s fixed overheads (FOR).

By contrast those in Class 2 will be required to hold capital exceeding the higher of their PMCR; FOR or a new liquid capital requirement: The K-Factors.

For Class 2 firms their PMCR will (if they take principal risk) a minimum requirement of €750,000 or €150,000 if the firm holds client money / assets. Those firms that do not

hold client money/assets may have a PMCR of €75,000.

The K-Factors are one of the biggest changes in the new regime and require firms in Class 2 to apply a series of percentages to specific risks including:

- **Risk to the Client (AUM, client money held, assets safeguarded and administered and daily trading flow)**
- **Risk to the Market (net position risk or clearing margin given)**
- **Risk to the Firm (trading counterparty default; daily trading flow and concentration risk).**

The issue with the new K-Factors is that while they may be relevant to the risks faced by investment firms (including Wealth Managers) they are complex for firms to review and to understand and there is a real risk that some firms will miscalculate how the new rules apply to them.

On balance the new requirements are an understandable, but all Wealth Managers need to be reviewing this new regime and how it will apply to their business now given the rapidly approaching implementation date.

“The new regime is anything but light touch.”

“Some firms will miscalculate how the new rules apply to them.”



## Conclusion

This Review establishes that the rapid and accelerating level of fintech adoption is leading to a significant transformation in the Wealth Management Sector.

Industry stakeholders are now focussing on Fintech solutions to assist in meeting the changing demands from their clients while also looking to deliver cost effective solutions which will alleviate the pressure on margins.

The realisation of the advantages that companies adopting appropriate technology have over their competitors is now firmly enshrined within most firms. Companies and of course Senior Managers, look to install robust applications which will deliver efficiency and demonstrate regulatory compliance which is very much and will continue to be in focus.

With this background, for the vast majority of firms Fintech has become the standard for

the sector. The mission for many firms now is to identify products and levels of service which will differentiate deliverables compared to those of competitors.

Client demands, regulation, quality of service, competitive products and profitability were said to be the 5 main drivers for firms to adapt to Fintech. Regtech and Artificial Intelligence are fast moving up the scale of interest as firms seek to service the changing Private Wealth Investor landscape.

In respect of the measures firms have taken or are taking in connection with their businesses, a variety of actions were mentioned.

These included setting business development targets for their company within a 3-year time frame, reviewing operational models with a specific focus on tasks which are carried out manually and identifying Fintech

solutions which would support client acquisition, increase productivity, improve efficiency and reduce costs.

There are continuing examples of firms looking to secure higher levels of AUM through acquisitions while others are looking to streamline operations. Either approach requires high quality technology, delivered swiftly and supported continuously.

Despite all challenges and overall, respondents had an enthusiastic outlook for the future and were keen for the Wealth Management Sector to enhance its image.

The sector had responded well since the difficulties of the pandemic and is now keen to fully embrace and exploit all possible Wealthtech advantages.

**“Client demand, regulation, quality of service, competitive products and profitability are the 5 main business drivers.”**

## Acknowledgements

The executives who took part in this review came from firms across the UK, as shown in this map. A total of 122 individuals were involved from companies providing services to the Wealth Management Sector.

Additional information has been provided from legal and audit firms coupled with the research carried out by Goodacre UK.



# CASHFAC

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