hearsay

2021 Finserv Compliance Benchmark Report

Hearsay's 2021 Finserv Compliance Survey* uncovered several mandates for financial services compliance organizations to optimize their digital communications for client-facing financial professionals.

First, technical skills are lagging on these teams, and must be bolstered in order to meet the challenges of increased complexity and quantity of digital communications, along with the demand for additional communication tools to drive business results.

In many cases, compliance departments have taken a "wait-and-see" approach to implementing technology that can unleash key business results, including expanded reach and better client service. In order to meet increasing demands with the same human resources, they must apply best practices in automating supervision where appropriate. To build these automation arsenals, they must also fine-tune their lexicon and testing processes to both defend their systems to regulators and focus human interventions on areas of the highest importance.

In this report, we explore some of the reasons for this hesitation and how to overcome them, which forces are continuing to drive change, and what we can expect and prepare for in the future for maintaining compliance over expanding digital channels.

**Hearsay's 2021 Finserv Compliance Survey gathered feedback from a random sample of 50 North American compliance leaders, using an online survey tool between August and September, 2021.*

Where we are today

Hearsay's 2021 Finserv Compliance Survey shows that while compliance resources for financial services have remained steady, the quantity of digital communications—and their corresponding complexity—has exploded in our hybrid work-from-home environment. Simultaneously, demand for additional digital communication tools that drive business results for FinServ professionals is increasing.

HOW HAS THE SIZE OF YOUR COMPLIANCE WORKFORCE CHANGED IN THE LAST 12 MONTHS?

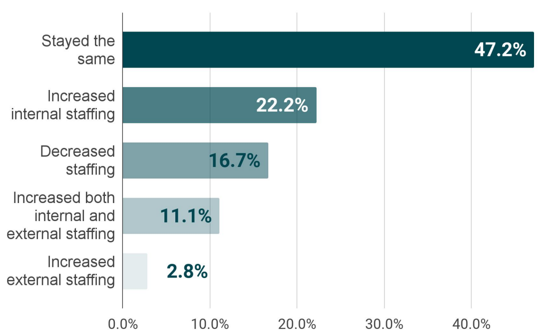


Exhibit #1: Despite expectations that they would decrease, compliance resources have been, and are expected to remain, steady.

Anecdotal evidence suggests that compliance teams are struggling to deliver more with fewer resources. However, the survey data shows that compliance resources have not decreased in the past 12 months and are not expected to decrease over the next 12 months.

The survey revealed that 47% of firms kept staffing the same, 17% decreased staffing, and 36% increased staffing over the past 12 months. Of the increases in staffing over the past year, 62% of that was completely internal, 8% was completely external (or outsourced), and 30% comprised a mix of internal and external staffing.

Going forward, more stability is expected, with only 3% expecting a decrease in staffing over the next 12 months, 67% expecting to stay flat, and the balance expecting increased staffing.

What *is* happening is increased pressure to do more with the same limited resources.

HOW ARE YOU DRIVING EFFICIENCY ACROSS YOUR SUPERVISION TEAM?

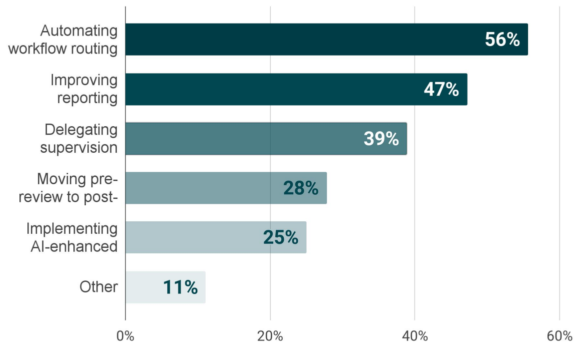


Exhibit #2: Notwithstanding continually stretched resources, compliance teams overall are not embracing technology in general—and AI specifically—to handle increasing demands.

Compliance teams must find ways to leverage technology to become more effective, to better handle increasing demands, and over time, become leaner. An over-reliance on manual functions means compliance teams are overwhelmed by low- and moderate-risk issues. Technology and automation have to be considered as part of the equation, so that teams can focus on the riskiest issues that matter most to the business.

The survey showed that teams are driving efficiency primarily by automating workflows and improving reporting; several pointed to lexicon enhancement and risk-based monitoring improvements. But as technology gets more intelligent, there is a significant opportunity to use artificial intelligence (AI) as a catalyst to enhance program efficiency. While this can lead to a more mature, impactful compliance program and increased trust throughout the organization, it is currently underutilized.

As programs mature and manual processes become more automated, the level of comprehension and evaluation demanded of compliance teams is rising, driven by the need to substantiate how supervision is performed and how these tools' design and function are validated. Partly due to this challenge, only 25% of survey respondents are implementing AI-enhanced review to improve efficiency. When asked about the compliance team's weaknesses, the number one answer was the ability to leverage technology.

Where is the risk coming from? The survey found that compliance teams experience reputational risk the most on far-reaching platforms such as Twitter and Facebook. Regulatory risk, on the other hand, is more centered around 1:1 communication channels, which are perceived as more challenging to supervise.

Of the respondents, 63% permit texting for business purposes. Respondents from these organizations likely have a texting solution that meets regulatory requirements with respect to capturing and monitoring that activity. However, firms that do not allow texting saw this as a significant regulatory risk. Recent enforcement actions have shown that when firms prohibit texting, and fail to provide a channel for their employees to text compliantly or prohibit texting, there is a strong onus on those firms to ensure adherence to policy. The measures these firms rely on to defend their policy are costly and complicated.

With respect to reputational risk, our survey indicated that the majority of firms feel social media represents the greatest source for this type of risk. While more than 50% allow the use of Facebook and Twitter, and ~90% permit LinkedIn, it's clear that capturing, monitoring, and archiving this

WHICH DIGITAL COMMUNICATIONS CHANNELS DOES YOUR ORGANIZATION BELIEVE ARE THE HIGHEST SOURCE OF RISK?

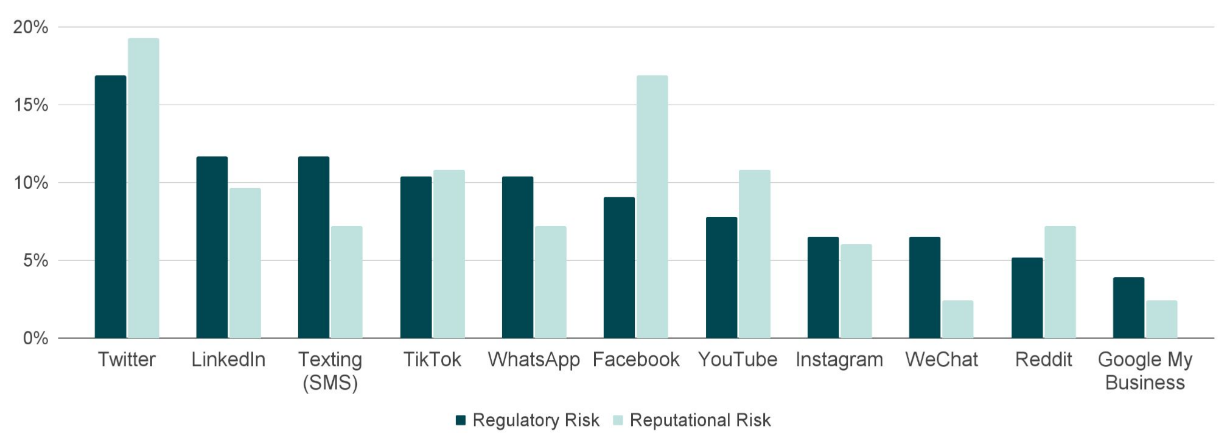


Exhibit #3: The survey showed a strong correlation between social media and reputational risk, and between one-to-one channels like texting, WeChat, and WhatsApp and regulatory risk.

data is less of a concern than the intrinsic risk of being able to adequately supervise the content itself. Given the maturity of these social media channels, there are sufficient methods for capturing, monitoring, and archiving these permissible outbound communications. However, in some cases, this can happen after the fact, allowing potentially problematic activity to stay in the public eye while the activity goes through the post-approval process. This also underscores the importance of an appropriate lexicon; the post-approval process relies entirely on the efficacy of an organization's lexicon.

Without confidence in the lexicon applied, a firm may overestimate the reputational risk it is subject to.

In summary, we find ourselves in a marketplace that has become increasingly virtual, driven by shifting participant engagement and technology advances. However, concerns regarding regulatory acceptance of solutions has some compliance departments maintaining a "wait-and-see" posture.

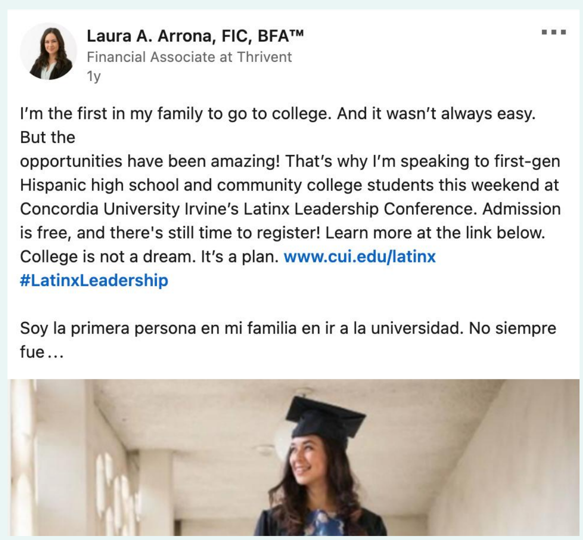
CUSTOMIZATION IS KEY

Allowing customization of social media content has become table stakes. And although it's not required, many compliance organizations are still doing pre-approval of original content.

Two-thirds of firms surveyed allow advisors to generate unique content for social media. This is critical to program success: Across Hearsay client data, we've seen that original content garners up to nine times the engagement of content provided by corporate. Even altering corporate content with a custom introduction or comment increases engagement by up to three times.

Interestingly, 90% of firms surveyed pre-approve some or all of this original content, even though regulators have lessened the obligation to do so.[1] This aligns with the finding that compliance teams are hesitant to implement AI-enhanced review and other technologies that can automate the supervision process.

Generally speaking, pre-approval is needed when original content is related to a firm's products and services, but not when this content is more general in nature. It's possible that any hesitation to implement AI is due to a lack of confidence that AI-enhanced functionality would be able to reliably flag content in a way that will sufficiently differentiate between that which requires review, and that which doesn't. Further, a compliance team will need to defend the reasoning as to why AI flagged some communications—but not others—which can sometimes be challenging due to a lack of visibility into how these AI systems determine alerts.



Original content that is personal in nature is effective for humanizing advisors and strengthening their relationships.

[1] See FINRA FAQs Section C.4 with respect to non-promotional retail communications

Where are we going

Today, most financial services firms allow LinkedIn and texting, and about half allow Facebook and Twitter. Many would like to offer Instagram, YouTube and Google My Business (GMB). Channels that offer "show not tell" functionality, such as video, are increasingly in demand due to their ability to cut through the noise.

Across lines of business, there wasn't significant variation when it came to interest in particular channels, with the exception of Property & Casualty (P&C) insurance, which was more likely than other business lines to allow the use of Nextdoor. This is likely because P&C's regulatory requirements are less stringent than other business segments, and because Nextdoor's specific focus on local communities, business recommendations, and homeowners provides relevant conversations for local P&C agents to engage in.

WHICH DIGITAL COMMUNICATIONS CHANNELS ARE AVAILABLE TO YOUR ADVISORS/AGENTS?

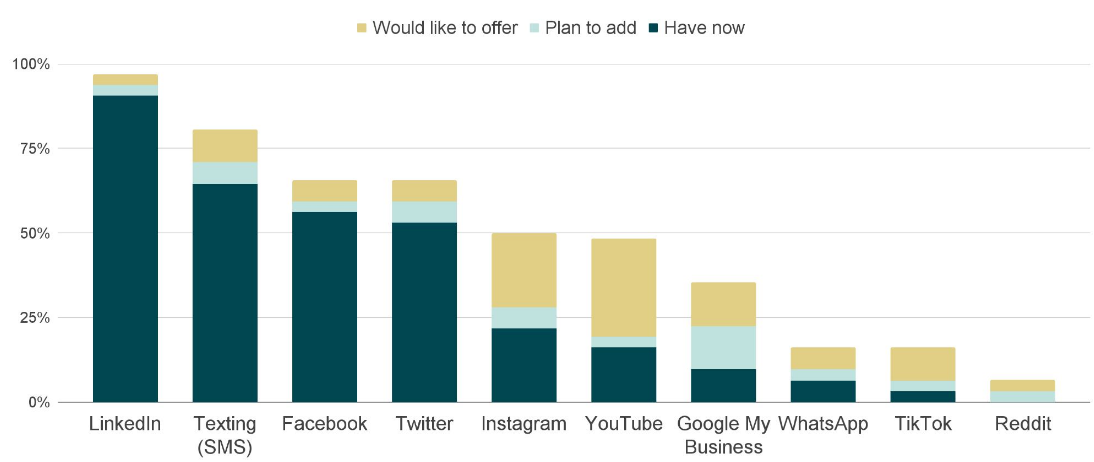
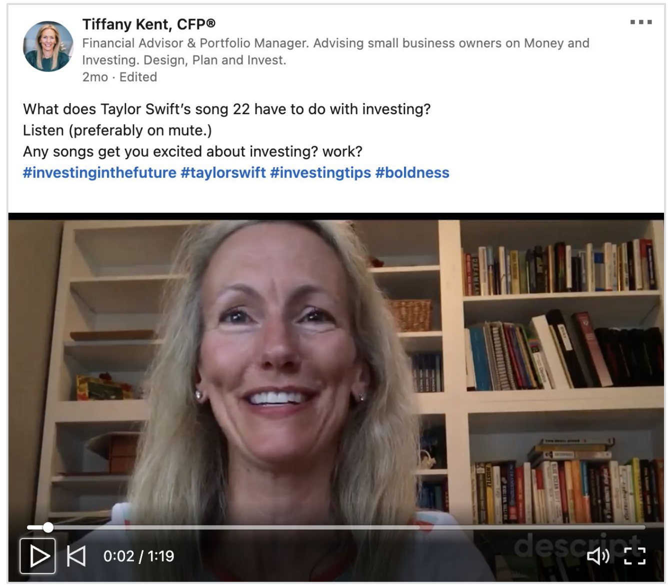


Exhibit #4: Firms are looking to expand channels that "show not tell."

The channels that firms were most interested in adding were Instagram and YouTube—not surprisingly, channels that allow for "show not tell." Particularly given the lack of face-to-face interaction over the past 18 months, video has emerged as an important tactic used by FinServ professionals to showcase who they are and what it's like to work with them. Besides being sticky and shareable, video helps break down walls by highlighting human faces and emotions.



Video is an excellent medium to demonstrate what it's like to work with a particular financial professional.

Besides being sticky and shareable, video helps break down walls by highlighting human faces and emotions.

The challenges in adding such new channels focus first and foremost on concerns over regulatory acceptance of supervisory technology and methods. This goes back to the need for—and challenge with—adopting and overseeing new technologies, including artificial intelligence, for supervision support.

Among those surveyed, the majority expressed concern about the effectiveness of technology available to meet regulatory requirements as well as whether regulators deem the solutions adequate. By design, social media platforms have not been developed with the financial services industry in mind. And while many networks have made great strides to open up their platforms to third party solutions, there still exist some gaps in these technologies with respect to satisfying financial services firms' regulatory obligations. The survey results reflect these gaps, as well as the effectiveness of some of the workarounds that technology vendors have implemented to close those gaps. Survey respondents are rightfully nervous about these workarounds, both in terms of their ability to meet a regulator's expectations, as well as the respondents' ability to explain them to a regulator.

FOR THOSE CHANNELS THAT YOU WOULD LIKE TO OFFER BUT CANNOT, WHAT IS THE PRIMARY CONSTRAINT?

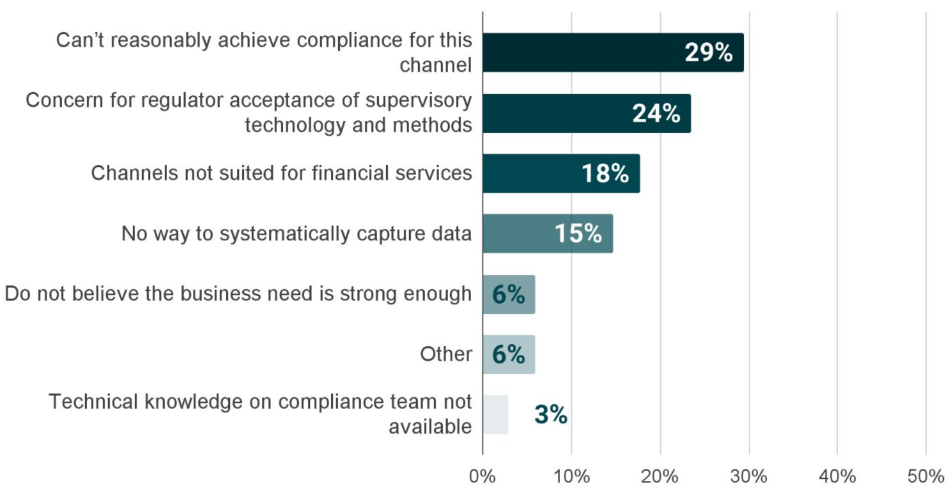


Exhibit #5: Regulatory acceptance and reasonable oversight are limitations to new channels.

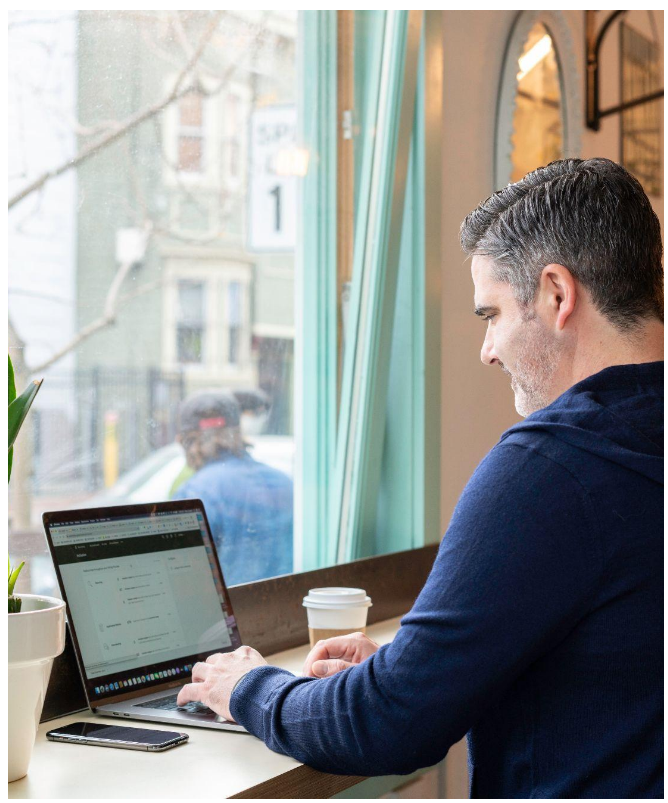
Regardless of channel, the survey found that allowing endorsements and testimonials on social media is controversial and differs significantly by line of business.

Wealth and Asset Management firms offer fewer opportunities for advisors to give and receive endorsements and testimonials, while Life and P&C Insurance are somewhat more permissive in this regard. Interestingly, the majority of Wealth and Asset Management firms do allow advisors to participate in online groups (88% allow this always or sometimes), likely not wanting to miss the opportunity to share expertise in the forums where modern investors are conducting research.

When it comes to endorsements (e.g., LinkedIn skills, Facebook likes) and testimonials (e.g., reviews, recommendations), there is much less consensus on permissible behavior. To seize the opportunity provided by peer-to-peer testimonials, 29% of wealth and asset management respondents said they don't currently, but are planning to, allow accepting testimonials within the next 12 months. Eighteen percent of this group is also planning to allow giving and receiving endorsements in that same period.

A likely driver of this momentum is the new Marketing Rule coming into effect in November 2022. In preparation, firms are re-evaluating their approach to testimonials and endorsements, and aligning their business need and desire against their ability to tap technology to establish controls around the new rule's permission of these activities.

The majority of Life and P&C Insurance respondents allowed participation in online groups, as well as always or sometimes allowing giving and receiving of endorsements and testimonials.



Regulatory pressure has increased to implement and better oversee technology related to supervision (including implementing policies and procedures, testing system changes, and access controls). However, compliance teams cite technical skills as their biggest weakness.

As FINRA wrote in its June 2020 report on AI and again reiterated during its Fall 2020 Conference on AI, compliance professionals need to understand how the technology they are implementing aligns with regulatory expectations. These steps include a documented understanding of the data set-to-action translation and a method to regularly test the system to validate it meets legal and regulatory requirements. When the algorithm informing your AI is hidden in a "black box," this can prove difficult.

Compliance teams need to face their real or perceived lack of technical skills and open the proverbial black box. To take advantage of automation, compliance teams must learn to explain how they supervise and test these tools. A key goal for 2022 planning should be to develop these technical skills within the team and learn best practices in documenting, explaining, supervising and testing automation tools.

AREAS OF OPPORTUNITY FOR COMPLIANCE TEAMS

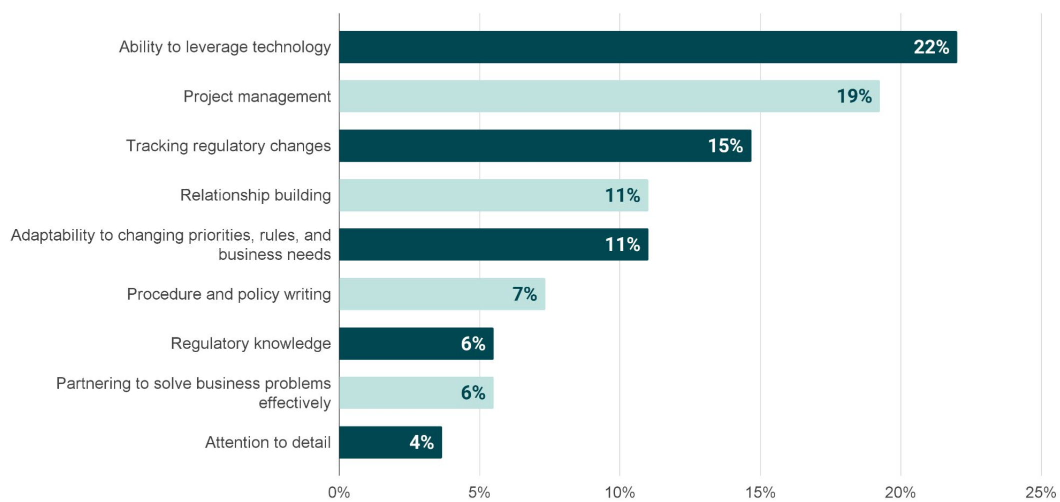


Exhibit #6: The ability to leverage technology was cited as teams' top weakness and area of opportunity.

SHARE THE VALUE OF THE RESULTS YOU BRING, NOT JUST YOUR EFFICIENCY METRICS

Compliance teams prioritize efficiency when it comes to measuring performance. According to the survey, the top three metrics used were time spent on supervision, time saved by automation, and alerts generated. However, leadership is more focused on the business results of the program, including usage by advisors/agents, ROI of programs, followed by time spent on supervision.

This mismatch spotlights an opportunity for compliance teams to elevate their results in the eyes of management by focusing reporting on the value of the program delivered while maintaining compliance. Measures that tie most closely to business results include size of the collective social networks of advisors/agents (i.e., reach), new connections added over a time period, total number of clients and prospects engaging with content, growth in engagement rates over time, and website traffic generated from social media. If you have a texting program, share measures such as advisor response time to client-initiated messages, and volume of conversations between advisors and clients over time.

While efficiency metrics are critical for self-assessment of supervision effectiveness, changing the lens to highlight business performance when reporting externally can be more valuable.

Conclusion

Taken together, the survey results provide a mandate for compliance teams to strengthen technical skills on their team, learn and apply best practices in supervising and testing automation tools, and hold vendors accountable for explaining and documenting AI logic and providing visibility into how AI systems are working.

In addition to expanding these technical skills, compliance teams should also strive to offer more digital communication tools that drive business results, such as adding "show not tell" channels and allowing for client testimonials in a compliant manner.

Finally, share more of the program's business results, such as growth in reach (e.g., the expansion of your collective social media connections) and improved client service (e.g., improved advisor response time to client texts) with your leadership to elevate the value of your contributions.

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