Regulatory reporting

Are you only seeing the tip of the iceberg?

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The financial crisis that shook the world early in the new millennium obliged governments to rethink their approach to controlling and regulating the financial system. However, how can you control something without a clear understanding of what is going on? The answer is simple: you can’t. This is why a push for greater transparency has begun.

Availability and accuracy of data
The primary challenge centres on data, which may be spread all over the organisation. It might be stored on legacy mainframes, hidden on the internal hard drives of employees, lost in a newly created private cloud or even kept outside of the company. The good news is that an increasing number of organisations are investing in data warehouse projects to streamline and rationalise data management, storage and archiving processes. Organisations must ensure that reportable data is accurate and up-to-date. For instance, a valuation of a derivative contract based on outdated market figures will cause the company’s real exposure to be inaccurate and result in a misstatement of information to regulators. Failure to report accurate data may lead not only to financial sanctions, but also to legal and reputational risks if auditors and authorised inspectors reveal the inaccuracies later. The quality of reportable data therefore needs to be organisations’ number one priority. A good practice for quality assurance would be to establish internal control policies and introduce the principles of accountability and data ownership to the business lines involved in reporting.

Outsourcing versus in-house reporting
Making accurate data available for reporting is extremely important, but it is only the first step in our reporting journey. The next step is to decide which reporting mode to use, i.e. whether to perform the reporting in-house or to outsource it to a third party. Unless the company provides reporting services to other firms, the costs associated with reporting are not recoverable, as reporting activity does not generate any income for the organisation.

If providing reporting services to others is not on the agenda, companies need to analyse whether these additional reporting costs can be absorbed using existing human and technological resources. From a human resources perspective, this includes the availability of current employees and their ability to take on the additional responsibility of extracting, preparing, approving and submitting the data. Companies should clearly understand that submitting a report is rarely the last step of the reporting process, as repairs and reconciliation may be necessary. From a technological viewpoint, a careful assessment of software/hardware capabilities is required to understand whether the complete reporting value chain is covered. In technical terms, this involves the ETL (Extraction, Transformation, Loading) software configured and adapted to the specific needs of the report in question.
Good candidates for in-house reporting would be companies with well-established IT processes and procedures, as this would foster a smoother integration of new reporting services. Companies performing one type of reporting can investigate the possibility of reusing existing in-house reporting services for another type of reporting. For instance, global banks with entities in the US and Europe might seek to mutualise Dodd-Frank Act and EMIR reporting related to their derivative contracts in view of their relative similarity. Likewise, nearly 40% of the data provided for EMIR and AIFMD reports is the same, including standardised identifiers (LEI, Broker ID, Product ID, etc.), valuation data, clearing details and product taxonomy.

On the other hand, companies should consider outsourcing opportunities. Time constraints often dictate the choice of an outsourcing option, as companies usually do not have enough time or resources to prepare the full reporting value chain. We also see some companies attracted by an ‘easy’ outsourcing solution, thinking that no further involvement from their side is required. This is a false assumption. Regardless of whether reporting is performed in-house or outsourced, the company still needs to extract and prepare the raw data. However, an analysis of available outsourcing offerings is worthwhile from a cost perspective.

Selecting an outsourcing provider
Offerings can be broken down into companies specialised in providing one type (or a very limited number) of reports and those providing a much broader spectrum of reporting services (‘all-in’ reporting providers), including reporting within multiple jurisdictions and for multiple industries.

Specialised reporting providers
Specialised firms might offer more flexibility in terms of data formatting and may provide a more responsive and proactive client relationship. On the other hand, they may not cover every step of the reporting value chain, leaving the company to deal with additional activities internally. Among these are certain steps to data transformation, reconciliation, and error handling. In addition, should your company be subject to multiple types of reporting, you would have no choice but to look for another reporting provider or to perform the reporting in-house, which means additional costs, new interfaces, supplementary communication channels, vendor relationships, etc. It is fair to say though that most specialised reporting providers are becoming ‘all-in’ players over time, offering additional types of reporting.
‘All-in’ reporting providers
These companies offer a broad spectrum of reporting services, usually covering a full reporting value chain and in some cases including additional services such as derivative valuation, thresholds or capital requirement calculations, and other data preparation and transformation services. Certain providers may offer analytical and data mining services. In addition, ‘all-in’ providers usually cover reporting for multiple jurisdictions and different regulatory bodies within each jurisdiction (for instance, the regulatory reporting solution for banks provided by Moody’s covers more than 50 countries and offers around 3,000 reports). These providers often have offerings for different industries, which might be of interest for holding companies covering multiple business sectors. While companies might benefit from contracting an established and recognised reporting provider (potentially in the eyes of a regulator), they might suffer from certain restrictions and a lack of flexibility in terms of raw data formats. Poor responsiveness from the provider as a result of a large number of other clients is also possible.

Conclusion
Today’s financial institutions are overwhelmed with regulatory obligations and have to face multiple challenges, including timely and accurate reporting to regulators. Ensuring that reporting data is available and accurate is the first and most critical step of regulatory reporting. The choice of whether to perform the reporting in-house or to outsource it depends on the business profile and internal capacity of the company to absorb these regulatory costs. When selecting outsourcing providers companies should explore the opportunities of mutualisation, especially if they are subject to multiple types of reporting. In this case, companies may see it as more cost-effective to work with ‘all-in-one’ reporting providers offering a wide spectrum of services. Regulatory reporting is an activity that should be taken seriously, especially in our increasingly regulated world.