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Submitted via email to RegTech@fca.org.uk

London, February 3rd 2016

Call for Input: Supporting the development and adoption of RegTech

Dear Sirs,

Markit is pleased to submit the following comments to the FCA in response to its *Call for Input: Supporting the development and adoption of RegTech* (the "**Call for Input**").

Markit¹ is a leading global diversified provider of financial information services.² Founded in 2003, we employ over 4,000 people in 11 countries and our shares are listed on Nasdaq (ticker: MRKT). Markit has been actively and constructively engaged in the debate about regulatory reform in financial markets, including topics such as the implementation of the G20 commitments for OTC derivatives and the design of a regulatory regime for benchmarks. Over the past years, we have submitted more than 140 comment letters to regulatory authorities around the world and have participated in numerous roundtables.

Introduction

Markit is a leading, established provider of innovative RegTech solutions with many of our services designed to support our customers' compliance with regulatory requirements across asset classes, throughout the trade workflow and for a range of financial market participants and service providers. Our RegTech services facilitate firms' compliance with regulatory requirements and reduce the related costs and risks, hereby lowering barriers to entry and fostering competition in the market place.

On the pre-trade side our solutions help firms, for example, to perform due-diligence on their counterparties,³ trading algorithms⁴ and vendors⁵ and to manage their research payments in an effective and transparent

¹ See www.markit.com for more details.

² We provide products and services that enhance transparency, reduce risk and improve operational efficiency of financial market activities. Our customers include banks, hedge funds, asset managers, central banks, regulators, auditors, fund administrators and insurance companies. By setting common standards and facilitating market participants' compliance with various regulatory requirements, many of our services help level the playing field between small and large firms and foster a competitive marketplace.

³ Provided by Markit's [KYC.com](http://www.markit.com/kyc) platform.

⁴ The Markit Counterparty Manager platform (MCPM) helps firms perform due diligence on trading algorithms used by their executing brokers. This is a requirement, for example, in Hong Kong and under MiFID 2.

⁵ Firms perform due diligence on their third party vendors as part of their business continuity and disaster planning programs. See <http://www.markit.com/product/ky3p> for more details.

manner.⁶ Post-trade firms use our services to comply with their best execution,⁷ reporting and margin calculation requirements.⁸ Other RegTech services of ours assist firms in complying with tax regulations⁹ or valuation requirements.¹⁰ The below are examples of regulations and Markit's related RegTech services that seem most relevant in the context of this Call for Input:

- Regulatory demands in relation to bank capital calculations such as the Fundamental Review of the Trading Book¹¹ have shifted complexity from implementing state-of-the art analytical models to also include efficient data and workflow management. Further, the incorporation of capital, credit and funding costs into pricing and position management creates complex technology burdens at a time when firms aim to reduce costs, consolidate platforms and eliminate manual processes. Markit Analytics solutions have evolved with regulatory and client demands to handle both internal and standardized model based approaches by leveraging a modular and versatile framework combining a powerful calculation engine with a sophisticated data management framework.
- Regulatory requirements in relation to data management such as BCBS 239¹² form a fundamental prerequisite for strong risk data management. Compliance with these standards necessitates a thorough revision of existing data management practices.¹³ Markit EDM¹⁴ allows our customers to validate data from different sources, check completeness, and manage exceptions to facilitate compliance with a variety of regulatory requirements.
- Know Your Client ("**KYC**") and Anti Money Laundering ("**AML**") requirements¹⁵ (as well as the FCA's regulatory action in this area) have boosted compliance costs and potential liabilities for banks, sometimes to the extent that they might no longer be willing to transact in certain countries or with certain types of counterparties.¹⁶ Markit's recently launched KYC.com¹⁷ platform provides market participants¹⁸ with standardised and repeatable processes designed to facilitate client onboarding.¹⁹ By removing the need for firms to perform duplicative, non-standardised processes our service significantly lowers compliance costs incurred by individual firms and their clients and allows them to establish new counterparty relationships in a timely fashion.²⁰ Importantly, the service fosters competition by reducing barriers to entry for new entrants that would otherwise need to develop their KYC/AML processes from scratch.

⁶ Markit's Commission Manager platform helps firms manage commission sharing agreements in an efficient manner. See <https://www.markit.com/Product/Commission-Manager>

⁷ As required, for example, under MiFID 2. See <https://www.markit.com/Product/Transaction-Cost-Analysis>

⁸ This is required, for example, under the EMIR and Dodd-Frank risk mitigation techniques for uncleared derivatives. See <https://www.markit.com/product/analytics>

⁹ Our platforms help firms comply with "Common Reporting Standards" (see <http://www.markit.com/Product/File?CMSID=675f66d146e94986ad043d78f47e3558>) as well as with the Foreign Account Tax Compliance Act (FATCA) requirements. See <https://www.markit.com/Product/Fatca-Service-Bureau>

¹⁰ The Investment Company Act in the US requires firms to determine the "fair value" of their assets in situations where market quotations are not available. See <https://www.markit.com/Product/Pricing-Data-Fair-Value>

¹¹ Also the standardized approach for measuring counterparty credit risk exposures (SA-CCR) or ISDA's standard initial margin model (SIMM) de-emphasize the relevance of internal capital models and promote standardized approaches instead. Such approach is less difficult from the modelling perspective since it is sensitivities based, but more challenging in terms of operational impact on banks.

¹² See <http://www.bis.org/publ/bcbs239.pdf>

¹³ For example, under BCBS 239, supervisors expect banks' data to be materially complete, with any exceptions being fully identified and explained.

¹⁴ Markit Enterprise Data Management ("EDM") supports risk data aggregation for BCBS 239, Emir, Solvency II, MiFID and Basel III.

¹⁵ For an overview of KYC/AML regulations in various countries see: <http://www.pwc.co.uk/assets/pdf/anti-money-laundering-quick-reference-guide-2015.pdf>

¹⁶ See, for example, <http://www.fiercefinanceit.com/story/deutsche-bank-stops-onboarding-new-clients-high-risk-areas-pending-kyc-revi/2015-12-01>

¹⁷ See www.KYC.com for more details

¹⁸ As of today, ten of the largest global banks have signed up for the service (or are in the process of contractual negotiations) and more than 1,400 buy-side and corporate clients are on the platform.

¹⁹ Markit's KYC.com platform helps its subscribers to upload, disseminate and maintain over 200 types of documents across 45 categories, thus assisting firms in complying with their KYC/AML requirements effectively and efficiently.

²⁰ Regulators have recognized that the use of such KYC Utilities can help maintain a vibrant correspondent banking activity, herewith supporting the flow of international capital and trade and ultimately economic growth.

- Increased regulation of OTC derivatives²¹ has imposed significant operational and compliance challenges on firms that are active in these markets. Markit's derivatives processing platforms²² are widely used and recognised as tools to increase operational efficiency, reduce cost, secure legal certainty and facilitate market participants' compliance with various regulatory requirements. Specifically, our derivatives processing platforms facilitate the electronic confirmation of many OTC derivatives transactions worldwide, submit them for clearing to 16 CCPs globally, and, for many counterparties,²³ report their details to trade repositories in various jurisdictions.²⁴
- Recent regulations demand not just the accurate but also a more nuanced view on the valuation of positions in financial instruments, and require firms to quantify the degree of valuation uncertainty²⁵ as well as the liquidity of their positions. We have developed our various pricing services²⁶ to provide our customers with measures of valuation uncertainty as well as liquidity risk,²⁷ herewith facilitating their compliance with regulatory requirements on prudent valuation and liquidity risk management.²⁸

Comments

We welcome the publication of the Call for Input and we appreciate the opportunity to provide the FCA with our comments. Our experience as a RegTech provider has shown that regulated firms seek to fully comply with changing regulatory demands and want to do so in the most cost effective fashion.

We welcome the FCA's stated goal to foster the development of technological solutions that can address the increased regulatory burden that firms are subject to. We strongly agree with the FCA that, to enable effective competition and promote innovation in financial markets, it should support "technologies that help firms better manage regulatory requirements and reduce compliance costs."²⁹ We believe that the existence of efficient and effective RegTech solutions reduces the risk of firms concluding that some of their activities are no longer viable,³⁰ which could result in less liquid and more fragile financial markets.

Specifically, based on our experience as a provider of numerous RegTech services to the financial industry around the globe, we recommend that the FCA:

1. Take active steps to promote the development of RegTech within its organisation by:
 - Establishing an official point of contact within the FCA and a channel for communication with individual (unregulated) RegTech firms and services (and their advisors),³¹ and
 - Publicly supporting and encouraging the use of third party RegTech solutions and consider conducting a Thematic Review on firms' use of RegTech providers;

²¹ Mostly on the back of the 2009 G20 Pittsburgh commitments, see <http://www.g20.utoronto.ca/analysis/commitments-09-pittsburgh.html>

²² See <http://www.markit.com/product/markitserv> for more details.

²³ Globally, we currently report OTC derivatives transactions to Trade Repositories for over 100 firms and more than 1,000 entities, including most of the large, globally active dealers.

²⁴ Including in Europe, the United States, Canada, Japan, Hong Kong, Singapore and Australia.

²⁵ See the EBA's final RTS on prudential valuation under CRR: <https://www.eba.europa.eu/documents/10180/642449/EBA-RTS-2014-06+RTS+on+Prudent+Valuation.pdf>

²⁶ See <https://www.markit.com/Product/Pricing-Data> for more details.

²⁷ See <https://www.markit.com/Product/File?CMSID=00bd57831a874fd1b1333717b563f77d>.

²⁸ For example, use of the most recent market prices is critical for calculating margin requirements which will form the basis for determining movements of collateral between counterparties.

²⁹ See Pg. 3, para 1.4 of the Call for Input.

³⁰ As reflected, for example, in the recent CPMI IOSCO report on correspondent banking activities. See <http://www.bis.org/cpmi/publ/d136.pdf>.

³¹ Access to a designated contact at the FCA should also be available to RegTech firms' advisors. This is because any need for unregulated firms to take expensive caveated advice from advisors who are unable to discuss new issues with the FCA would represent a material disadvantage for them.

2. Take active steps to promote the development of RegTech solutions by promoting it with the firms it supervises by:
 - Clarifying its supervisory expectations to enable regulated firms to rely on solutions provided by RegTech firms, for example by endorsing standards that RegTech providers have developed in dialogue with the industry and/or by establishing a certification process for certain types of third party providers;
 - Ensuring that its supervisory expectations in relation to material outsourcing arrangements are both clear and proportionate; and
 - Recognising that the most significant benefits of the use of RegTech solutions accrue in the area of “shared services” such as KYC Utilities or reporting solutions, i.e., where regulatory compliance requires largely a duplication of efforts and/or where there is a lack of standards;
3. Work to ensure that the regulatory framework in the UK supports (or at least does not hinder) the development of RegTech services by:
 - Carefully assessing its existing and upcoming regulations to ensure that they do not (unintentionally) prevent the use of third party RegTech solutions;
 - Requiring Financial Market Infrastructures, including CCPs and Trading Venues, to provide RegTech firms with open, non-discriminatory access where they request access on behalf of regulated firms;
 - Providing safe harbours or initiate changes to data privacy laws to facilitate the use of and sharing of information with and by RegTech services; and
 - Fostering the adoption of RegTech solutions, for example by requiring regulated firms to provide relevant information to designated RegTech providers in a timely manner or by establishing commitments with regulated firms in relation to their (unregulated) customers.

Please find below our responses to the FCA’s specific questions that explain the reasoning behind our above suggestions in more detail.

Question 1. What RegTech could be introduced in order to make it easier for firms to interact with regulators, at a lower cost and administrative burden?

RegTech solutions enable firms to comply with regulatory requirements in an efficient and effective manner. We believe that “shared solutions”, i.e., services where a RegTech provider operates a central hub that centrally performs compliance tasks for its customers that would otherwise need to be performed by each of these firms individually, are particularly relevant in reducing burden and cost for the industry whilst facilitating interactions with regulators.

For example, KYC/AML obligations in various jurisdictions require firms to manage and update documentation for each of their clients. Without any centralized solution significant portions of the underlying processes would be performed individually by each firm dealing with the same client resulting in significant duplication.³² Third party RegTech providers³³ can generate very significant benefits to the industry by centralising the document gathering, validation and management process, thereby facilitating compliance with the requirements and

³² However, it is worth noting that other parts of the process will still need to be performed by individual firms, e.g., compliance review or risk analysis.

³³ Such as Markit’s [KYC.com](https://www.kyc.com), Swift’s KYC registry, or Thomson Reuters’ Accelus.

reducing the time required to establish a trading relationship.³⁴ Such approach significantly reduces costs for each individual firm that is affected by the regulation as well as for the industry overall.³⁵

Importantly, activities of “shared services” are also instrumental to reach agreement upon appropriate standards in the market that benefit both firms and their supervisors. Regulation that requires interpretation from firms often results in differing standards of implementation depending on the approach taken by individual firms. Our experience has shown that the emergence of third party shared services can facilitate firms’ agreement on the interpretation of requirements and implementation standards. Importantly, the greater the commonality in these aspects across regulated firms, the easier it is for regulators to supervise, engage and effectuate change in the industry. As explained in further detail below, we encourage the FCA to foster such initiatives by actively working with relevant RegTech providers and, where necessary, clarify its supervisory expectations. It should also consider endorsing certain industry-set standards and certifying certain types of providers as explained in more detail below.³⁶

Question 2. What role would it be most useful for the FCA to play in order to foster development and adoption of RegTech in financial services, and what method would best suit this engagement?

We believe that the FCA could most effectively foster the development of RegTech services in the UK by (a) establishing an official channel for communication between the FCA and RegTech providers (and, where applicable, their advisors) and (b) clarifying its supervisory expectations through the endorsement of industry-set standards and/or the certification of certain RegTech providers, where appropriate.

• Establishing an official channel for communication between the FCA and RegTech providers (and their advisors)

While most UK-based firms that use RegTech services are FCA regulated (and remain ultimately responsible for their compliance), the majority of RegTech providers themselves are not regulated by the FCA. This means that typically there is no “official” relationship between such third party providers and the FCA. We believe that this situation slows down the development and proliferation of such services and their broader adoption and we hence encourage the FCA to address it.

The success of Project Innovate³⁷ demonstrates the value of creating a single point of contact for firms who are not currently regulated to engage with the FCA. We recommend use of a similar approach also for providers of relevant RegTech services. We believe that the existence of such a point of contact could provide several benefits to RegTech providers and the FCA, for example it would allow relevant RegTech providers to:

- Notify the FCA of issues that are directly or indirectly related to the interpretation and implementation of shared services solutions and request (informal or formal) guidance from the FCA on relevant regulatory requirements;
- Raise concerns about certain regulatory requirements that may act as a barrier to the provision of third party solutions³⁸ and recommend how the FCA could best address such issues;
- Highlight areas where the FCA should clarify its supervisory expectations; and

³⁴ Once a firm has uploaded all the documents in the central KYC database, new trading relationships can be established by permissioning firms to view those documents using the central database. Firms would then only be required to refresh those documents on a regular (typically annual) basis.

³⁵ MarkitSERV’s OTC derivatives reporting services provide delegated reporting under Dodd Frank, EMIR and other reporting regimes. Firms that are required to report in different jurisdictions will not need to connect to different Trade Repositories but just establish a single connection to the MarkitSERV platforms, resulting in significant cost savings.

³⁶ See the 2nd part of our response to question 2.

³⁷ See <https://innovate.fca.org.uk/>

³⁸ See our response to Question 3.

- Notify the FCA of any outage of (or other issues impacting) their services to FCA supervised firms that might affect their compliance.³⁹

We believe that the existence of an official point of contact and channel of communication with the FCA would greatly help RegTech providers to design their services in line with regulatory expectations. It would also allow the FCA to highlight that it regards the use of certain third party shared services as acceptable for compliance with certain regulations or for certain function in support of compliance. Such guidance could ensure that regulated firms do not feel obliged by the FCA to develop their own expertise and build systems from scratch rather but can rely on qualified third party service providers.

- **Clarify the FCA’s supervisory expectations through the endorsement of industry-set standards and/or the certification of RegTech providers that operate to certain standards**

We welcome the suggestion made in the Call for Input⁴⁰ for the FCA to support the development of shared standards. We suggest that the FCA endorse such standards, where appropriate, and also consider establishing a certification process for RegTech providers that operate to certain standards without extending the regulatory perimeter.⁴¹

We believe that providers of RegTech services and their customers would benefit from the FCA taking a clear and consistent approach in relation to the use of these services by regulated firms. Specifically, we encourage the FCA to review and, where they are found to be appropriate and consistent with the FCA’s supervisory expectations, endorse standards that have been developed by RegTech providers in dialogue with the industry. It would further assist the development of RegTech solutions if the FCA developed some form of accreditation for RegTech firms that provide solutions for FCA regulated firms. This could be provided either by the FCA or by another accreditation body. We believe that such approach would give regulated firms more confidence in using RegTech services. We acknowledge that this would be a significant development for the FCA and therefore recommend for the FCA to discuss this idea further with regulated firms and relevant RegTech providers.

To further foster the adoption of RegTech services and provide regulated firms with confidence they can use these services, we also recommend the FCA consider conducting a Thematic Review on the use of RegTech services and shared solutions by regulated firms in the UK.⁴²

Question 3. Are there any specific regulatory rules or policies that cause barriers to innovation or adoption of RegTech for financial services (products or processes)? Please provide examples of when these rules or policies have stifled development/adoption and describe the impact (e.g. delay, abandonment of project, economic impact). We are also interested in hearing about regulatory rules or policies that may extend beyond the UK regulatory jurisdiction including, for example, European or international policies and agreements.

³⁹ We understand that the obligation to provide such notifications would still remain with regulated firms. However, the FCA should note that any outage of the service would first be recognised by the third party. We believe that, particularly given the large number of firms that some RegTech providers support through some of their services, it would be more efficient and effective for the third party provider to submit such notification directly to the FCA.

⁴⁰ See Pg. 5, Supporting the current FinTech and RegTech environment.

⁴¹ We generally believe that direct regulatory oversight of RegTech providers would not be appropriate since the ultimate responsibility to comply with the relevant regulatory requirements generally remains with the regulated firms in any case. However, where the FCA believes that a RegTech service required authorization we strongly recommend it consider the use of a staged Part IV authorization process. Such approach would allow providers of new services to build up their operations to meet regulatory standards within the first 24 months of authorisation rather than having to be immediately wholly compliant.

⁴² As we have highlighted in our recent response to the FCA’s Consultation Paper on the Asset Management sector. See <https://www.markit.com/Company/RegulatoryResponsesFile?CMSID=69af1701bafd45fdb66da53dd7fcd858>

We welcome the fact that regulators (and regulations) are generally supportive of the use of third party service providers to facilitate compliance and allow for efficiency gains.⁴³ However, the FCA should note that, nevertheless, RegTech providers are often confronted with aspects of regulation that might, mostly unintentionally, slow down the adoption of RegTech services provided by third parties or, in the extreme, preclude firms from using them. We strongly encourage the FCA to identify and carefully consider those issues going forward.

- **Carefully assess existing and upcoming regulations to ensure that they do not (unintentionally) prevent the use of third party RegTech solutions**

Our experience has shown that the design of some regulatory requirements can cause, mostly unintentionally, regulated firms to conclude that they cannot use third party services to facilitate their compliance. The FCA should note that these situations can occur even if the use of a third party service was explicitly permitted and it offered many advantages to them.

For example, many counterparties in the OTC derivatives markets currently use third parties for affirmation/confirmation services and to help them identify and correct any erroneous trades before they are cleared. A newly introduced regulatory requirement for derivative transactions executed on electronic trading platforms to be submitted and accepted for clearing “as soon as technologically practicable” following execution,⁴⁴ also known as Straight-Through processing or “STP”, aims to reduce risk in the marketplace.⁴⁵ However, our experience has shown that, if the technical standards for STP were not set appropriately, for example because proposed timeframes were too short, in essence requiring firms to weigh expedience more heavily than accuracy and risk reduction, firms might conclude that the potential additional latency that the use of a third party could introduce, even if only minor, might challenge their ability to comply with the STP requirements. To avoid a situation where overly demanding STP requirements would question the ability of firms to use third parties, the technical standards should provide sufficient flexibility and allow firms to determine when it is practicable for them, given the characteristics of the trade to ensure the accuracy of a trade with the use of third party services, e.g., via affirmation, or to forego the services of a third party and any opportunity to correct errors before a trade is submitted to and accepted for clearing.⁴⁶

Based on our experience in relation to STP and other matters, we urge the FCA to carefully review its existing and upcoming regulation to consider the potential implications for the use of third party RegTech providers. It should make adjustments to them, where appropriate, to ensure that firms are in a position to use third party solutions where they regard them as the most effective and efficient solution to their compliance needs.

- **Address issues related to data privacy and data sharing⁴⁷**

As part of the provision of their services, RegTech providers are often expected to receive, transmit and store non-public personal information (“**NPPI**”). Our experience has shown that data-privacy related concerns of firms⁴⁸ can cause significant challenges to third party service providers in this context in many jurisdictions and, in the extreme, might discourage firms from using third party providers.

⁴³ For example, the ISDA Amend service used for regulatory representations in the context of EMIR and Dodd-Frank has been endorsed by regulators as a standard way of making such representations. See <http://www.markit.com/product/isda-amend> for details.

⁴⁴ Dodd-Frank requires the Straight Through Processing (STP) of trades executed on an electronic platform. Similar requirements exist under MiFID II where STP proposals intend to minimize the time between execution and clearing of both electronically and voice traded derivatives.

⁴⁵ See ESMA, Draft regulatory technical standards on the obligation to clear derivatives traded on regulated markets and timing of acceptance for clearing, RTS 26, at paras. (i) and (ii), available at https://www.esma.europa.eu/sites/default/files/library/2015/11/2015-esma-1464_annex_i_-_draft_rts_and_its_on_mifid_ii_and_mifir.pdf

⁴⁶ Similarly, overly demanding timing requirements in relation to the “embargo rule” also questioned whether third party services could be used for the reporting of transactions to Trade Repositories.

⁴⁷ Any changes should be decided upon as part of a consultative process with the industry.

⁴⁸ For example, The Data Protection Act in the UK “controls how your personal information is used by organisations, businesses or the government.” See <https://www.gov.uk/data-protection/the-data-protection-act>

For example, under upcoming MiFID 2 transaction reporting rules, firms will be required to report certain NPPI datafields to National Competent Authorities. Firms generally have an interest in delegating reporting services to qualified third parties. However, such third parties would need to store and transmit NPPI to the relevant National Competent Authority. We have found that this can discourage regulated firms from using third party services for this purpose while it would also expose such service providers to significant legal liability.

To address such data privacy related challenges we suggest the FCA provide a safe harbour or a protocol for the provision of NPPI to qualified RegTech providers and initiate related changes to relevant laws where appropriate. We believe that such measures could reduce firms' legal uncertainty about liability related to the submission of personal data to third party RegTech providers for processing.⁴⁹ These measures should also allow qualified RegTech providers to process the data⁵⁰ on behalf of the firms submitting data without requiring the firms or the RegTech providers to seek a separate set of approvals or permissions from the data subjects.

- **Ensure that the FCA's supervisory expectations in relation to material outsourcing arrangements are clear and proportionate**

The FCA should note that the classification of a RegTech service as "material outsourcing"⁵¹ results in significant additional compliance burden and costs for the provider of the service. In the extreme such classification will make the service no longer viable (or it might never be launched in the first place). To reduce the number of these situations and avoid stifling innovation we urge the FCA to:

- Keep the number of services that are classified as "material outsourcing" to a necessary minimum whilst this decision is being made on a firm by firm basis;
- Define clear, objective criteria to determine whether the use of a third party service represents "material outsourcing". This might be by reference to additional / updated guidance to that contained in the MiFID connect guidance on this subject;
- Clarify the requirements that a RegTech provider needs to satisfy in case of material outsourcing and ensure that those are proportionate and not overly demanding without a corresponding benefit;⁵² and
- Facilitate compliance for material outsourcing service providers to "comply once" rather than having to demonstrate compliance to numerous clients for the same service, which could potentially be supported by use of a registry.⁵³

⁴⁹ Otherwise, service providers would need to structure their service as such that there is no need for them to hold the NPPI, for example through systems of coding at the firm and decoding at the regulator. However, this would probably lead to a significant increase in the cost of the service and might not be acceptable.

⁵⁰ Including, without limitation, by disclosing the data to third parties at the direction of the firms submitting the data.

⁵¹ See MiFID connect guidance, page 2: "MiFID applies detailed requirements regarding the measures firms must take to manage the risks associated with outsourcing "critical or important" functions or investment services or activities (the "Outsourcing Obligation"). The FSA applies the Outsourcing Obligation to all firms carrying out MiFID and/or CRD business ("common platform firms") and also applies it as guidance for outsourcing that does not involve "critical or important" functions or investment services or activities. The requirements apply to a common platform firm's material outsourcing in relation to: (i) UK regulated activities whether MiFID business or not (e.g. deposit taking activities as well as MiFID investment services and activities), (ii) listed activities under the BCD (e.g. lending activities), and (iii) ancillary services under MiFID (e.g. provision of investment research)." See http://www.mifidconnect.com/mifidconnect/downloads/MiFID_Connect_Outsourcing_Guide.pdf

⁵² For example, where appropriate, the provider should be allowed to perform independent internal audits. Also, where appropriate, audits would only be required on a biannual basis.

⁵³ This could be achieved through an FCA or independently hosted and audited registry of firms that have self-certified compliance with relevant material outsourcing requirements.

Question 4. Are there any regulatory rules or policies that should be introduced to facilitate innovation and adoption in RegTech for financial services (products or processes)? Please provide examples of when the absence of these rules or policies has stifled development/adoption and describe the impact (e.g. delay, abandonment of project, economic impact).

We believe that some of the key issues that are holding back the adoption of RegTech solutions in the UK are (a) a lack of clarity about the FCA's supervisory expectations and (b) dependence on firms' customers for the actual adoption of a service. We encourage the FCA to take action as per below to address these issues.

- **Provide clarity about the FCA's supervisory expectations**

Our experience has shown that innovation in RegTech solutions for financial services depends not just on creating a competitive environment for such services but even more so on the FCA providing sufficient clarity about its supervisory expectations. We therefore encourage the FCA to review and, where appropriate, support standards that RegTech providers have established in dialogue with the industry, as it would facilitate the broader adoption of services provided by these firms.

For example, several competing KYC Utilities have worked towards creating standards of the documentation that needs to be gathered for certain jurisdictions and counterparty types.⁵⁴ We believe that the market-driven creation of such standards is a sign of a functioning, competitive market where providers of such services innovate to support firms' compliance in the most effective and efficient manner. The FCA should note that developing these standards has led to all firms adopting the highest standards (rather than them coalescing around the lowest common denominator).

Where such industry-led standards have been successfully set, the FCA should provide regulated firms with the same, consistent feedback about the suitability of such standard to achieve compliance. Specifically, where appropriate, the FCA should create clarity about its supervisory expectations by endorsing standards that have been developed and agreed by individual RegTech providers with industry participants. We believe that such step could significantly accelerate the broader adoption of RegTech solutions.

- **Fostering the adoption of RegTech solutions by firms' customers**

Our experience has shown that the overall benefit of a RegTech service to the marketplace tends to be directly proportional to the number of firms that subscribe to it.⁵⁵ As a standard business practice we work closely with the broader industry when developing our RegTech solutions. In addition, we also regularly partner with other firms⁵⁶ with the objective of assisting regulated firms with their compliance in the most effective and efficient manner.

In general, most of the major regulated firms have embraced the use of RegTech solutions given the benefits it provides to them from a compliance, cost and risk perspective. However, even where a RegTech solution is endorsed by the major financial firms, it is the lack of willingness by their clients to participate and take action that often represents a significant hurdle to their broader adoption. For example, the broader adoption of KYC Utilities is slowed down by the fact that banks' clients⁵⁷ are not sufficiently incentivised to support such

⁵⁴ For example, Markit's [KYC.com](https://www.markit.com/kyc) service has worked towards creating standards between banks and their trading partners as has Thomson Reuters' Accelus. The SWIFT KYC Registry on the other hand has created standards for correspondent banking relationships.

⁵⁵ The industry refers to these solutions as "Shared Services" that centralise operational functions, originally performed in separate divisions or locations of a company, with economies of scale and standardisation of processes ultimately translating into cost savings. The strategy can also involve sharing services between two or more firms. "Shared services" can span across different functional areas of the value chain including Finance, Operations, IT, Risk or Human Resources and tasks including reconciliations, settlements or clearing.

⁵⁶ For example, Markit has partnered with Genpact to provide a centralised platform that facilitates firms' compliance with their KYC/AML obligations.

⁵⁷ Including asset managers, corporates, hedge funds, etc.

centralised solutions while time and effort is required from them to onboard themselves to these platforms. Many of these firms will hence fail to onboard and provide the requested documents in a timely manner despite significant efforts from banks and KYC Utilities to resolve this lack of action. This slows down the broader adoption of such services and creates a risk that KYC compliance is applied inconsistently by firms to the detriment of market integrity.

We encourage the FCA to take action to address the issue of slow adoption by firms' customers. Specifically, where the relevant firms are FCA regulated they should be made subject to explicit regulatory requirements to provide relevant documentation to the chosen RegTech providers. Where the FCA is not in a position to require such firms to provide these documents, for example because they are not regulated, it might consider agreeing certain commitments with the banks to allow them to impose credible pressure on their clients.⁵⁸ Commitments in relation to AML/KYC onboarding could contain specific, agreed targets for banks in relation to the percentage of their relevant clients that have provided required documentation to the chosen KYC Utility (or Utilities).⁵⁹ We believe that such commitment-based approach could speed up the adoption of RegTech services by empowering regulated firms to impose greater discipline on their (often unregulated) clients and thus raising the overall level of compliance.

- **Require Trading Venues and CCPs to provide open, non-discriminatory access to RegTech providers**

We urge the FCA to ensure that RegTech firms are provided with fair, reasonable and non-discriminatory access to other financial market infrastructures, including Trading Venues and CCPs, when they request it on behalf of their clients as this will often be a pre-condition for them providing their services.

For example, third party processing hubs like MarkitSERV play an important role as intermediators in the OTC derivatives market. The features of non-standard derivatives make post-trade processing and trade capture into a financial institution's risk systems costly and challenging, particularly if each financial institution had to build its own capability to process these transactions. Third party hubs can provide market participants and trading venues with a single point of access to clearing venues and other post-trade service providers, herewith enhancing the range of cleared, standardized products accessible to market participants and trading venues, as well as promoting competition in the market for clearing services.

We note that MiFIR introduces a requirement for trading and clearing venues to provide open, non-discriminatory access.⁶⁰ However, our experience as a third party provider has shown that such access is not always granted by all CCPs and Trading Venues to third parties seeking access on behalf of their clients. We therefore recommend the FCA apply heightened scrutiny of discriminatory actions when a clearing or trading venue appears might discriminate against third party hubs, in particular where such market infrastructure offers a competing service or appears to discriminate against these hubs in order to protect a dominant incumbent position in an asset class.⁶¹ Robust protections of competition and express protections for third party hubs and their customers will reduce barriers to entry and level the playing field for trading and clearing venues alike, thereby fostering competition in the marketplace. Similarly, the FCA should ensure that operational requirements for accessing a clearing or trading venue are applied uniformly and non-discriminatorily whether a customer uses a third party hub or not.

⁵⁸ Such commitments are not without precedent. For example the OTC derivatives regulators forum ("ODRF"), a body of national OTC derivatives regulators has previously co-operated to create standards that would enable the OTC derivatives markets to operate efficiently. For example, the ODRF created trade repository subgroups that would "develop expectations regarding the data that authorities would like to see registered in the respective repositories". See <http://www.otcdf.org/work/index.htm>

⁵⁹ In the event that banks' clients have not furnished such documentation by an agreed date banks would be empowered to stop transacting with them.

⁶⁰ See Articles 35 and 36 of MiFIR.

⁶¹ In the latter scenario, a dominant clearing or trading venue may be motivated to eliminate the role of third party hubs in the asset class it dominates because the hub's value is in its ability to facilitate clearing and trading in different venues. In asset classes where third party hubs plays little or no role, the ability of new trading or clearing venues to compete with a dominant incumbent is reduced because the third party hub pipeline through which liquidity could be transferred would be effectively closed.

Question 5. Which existing regulatory compliance or regulatory reporting requirements do you feel would most benefit from RegTech?

We believe there are two types of use cases that would benefit most from the development and adoption of RegTech solutions. They are situations where (a) there is a large overlap of required actions between individual firms and/or there are significant benefits to be gained from the use of a central infrastructure and/or (b) there is a lack of standards.

- **Reducing duplication of efforts**

We believe that regulatory requirements that result in significant duplication of activities or require connectivity between a large number of market participants are prime candidates for the provision of shared RegTech services. A pertinent example is the reporting requirements for derivatives. Processing platforms such as MarkitSERV act as central hub and have expanded their value proposition to provide, in addition to trade confirmation services, connectivity to CCPs in the case of derivatives that need to be cleared and reporting to Trade Repositories.⁶² Such provision of centralised infrastructure removes the need for firms to individually connect to the various CCPs and Trade Repositories, instead firms connect directly to the central hub and direct the middleware platform to send trades to the desired CCP and trade repository respectively. The FCA should note that the industry has accrued significant cost savings as a result of this while also reducing the operational risk that would arise from individually establishing and maintaining connectivity to these various venues.

As we have explained in more detail above, to enable those shared solutions or central hubs to succeed, it is crucially important that the (often unregulated) providers of these services are provided with open, non-discriminatory access by the relevant (regulated) market infrastructures.⁶³

- **Endorsement of industry standards**

Regulatory requirements will often demand interpretation by individual firms, and supervisory expectations might not be clear or even conflicting. In these situations the establishment of market-wide standards provides significant benefits. Initiatives that are driven by RegTech providers are often essential to create such standards.

Specifically, RegTech firms that are in the process of developing their product offering will often work closely with the major industry participants to agree upon standards that are acceptable for firms that need to comply with the regulation. Such standards will be designed to satisfy the compliance expectations of each of these participants. For example, RegTech providers addressing KYC/AML requirements have made strides to standardise the erstwhile ad-hoc and inefficient processes performed by banks to collect counterparty information. Standards in relation to the specific documents to be collected and the frequency of updates, for example, have been successfully created by KYC RegTech providers for several market segments and jurisdictions.⁶⁴

We encourage the FCA to foster such industry-led initiatives by endorsing standards that have agreed upon in dialogue between industry participants and RegTech solution providers, wherever the FCA regards such standards as appropriate and sufficient.

⁶² The MarkitSERV derivatives processing platforms perform delegated reporting, which is explicitly allowed under EMIR and Dodd-Frank derivatives reporting regimes.

⁶³ See Markit's response to the Fair and Effective Markets Review launched by the Bank of England: <https://www.markit.com/Company/RegulatoryResponsesFile?CMSID=c746a76f13a24e61a883d19e0f24d396>

⁶⁴ Markit's [KYC.com](https://www.markit.com/Company/RegulatoryResponsesFile?CMSID=c746a76f13a24e61a883d19e0f24d396) has created standards for banks-asset manager trading relationships in the US and UK. These standards were created based on our dialogue with several major banks.

We hope that our above comments are helpful to the FCA. We would be more than happy to elaborate or further discuss any of the points addressed above in more detail. In the event you may have any questions, please do not hesitate to contact us.

Yours sincerely,

A handwritten signature in black ink, appearing to read 'M. Schüler', with a stylized flourish at the end.

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