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COMPLIANCE RISKS AND CONSIDERATIONS FOR FAMILY OFFICES

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ONE-ON-ONE INTERVIEW

COMPLIANCE RISKS AND CONSIDERATIONS FOR FAMILY OFFICES

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Nick Parfitt is responsible for determining Acuris Risk Intelligence's approach to the market and building subject-matter expertise. He has 18 years' experience in project and programme management, business process change and in implementing technology and business solutions at financial services, telecoms and public sector organisations. His experience in the financial crime sector spans seven years, helping tier one financial institutions assess and improve AML, KYC and sanctions operations. Mr Parfitt has worked for several tier one banks in the UK and holds an MBA (Distinction) from Cardiff University, and a BA (Hons) in Biochemistry from Imperial College.

R&C: What, in your opinion, are the most significant compliance issues currently facing family offices?

Parfitt: We see parallels with traditional small to medium and even large organisations, where it is a challenge to keep abreast of regulatory and compliance obligations – and one that is often exacerbated by the jurisdictional reach and nature of the operation. When single or multi-family offices are subject to anti-money laundering (AML) regulations, compliance is a key challenge due to the depth of knowledge and experience needed around the subject and the implications for the office in question. Beyond specific compliance requirements, family offices also should consider reputational risk exposure. They need to look at what this means for business relationships – either direct relationships with partners and organisations or throughout the vendor supply chain – and how they are identifying and managing this risk.

R&C: What do you consider to be the most notable legal and regulatory developments presently impacting the way family offices approach risk, compliance and reporting processes?

Parfitt: In the UK, a family office can operate in various ways: from being run by trusted family members or individuals to being managed by a professional service provider. UK law requires that investment advice can only be given by a stockbroker or financial adviser, who must be registered with the Financial Conduct Authority (FCA), or in the case of certain larger institutions, the Prudential Regulatory Authority (PRA). Another key aspect of risk for family offices is around limitation of liability and how different legal structures can be used to limit liability if required. The three primary entities used to achieve this in the UK are limited liability companies (Ltd), limited partnerships (LPs) and limited liability partnerships (LLPs), all of which protect the owner, in general, from financial penalties according to the level of equity invested in the family office entity.

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R&C: How important is it for family offices to cultivate a robust compliance and risk management culture across the organisation? What strategies can be deployed to take this process well beyond a box-ticking exercise?

Parfitt: If we look at good practices for AML and countering of terrorist financing (CTF) over the last decade, the adoption of a shared culture throughout the organisation has been central to success. More importantly, it is good business sense to have well-articulated, documented and implemented risk processes and procedures, particularly if the family office has a low appetite for reputational risk exposure, as nearly all of them do. Regularly refreshed training that is tailored to the family office's unique business operations, scope of jurisdiction and articulated risk appetite is a successful way of embedding good practices. From a governance perspective, a suitable risk and compliance governance operating model, including appropriate committees for risk escalation and decision making, provides a key control point for implementing and managing risk policies and procedures.

R&C: Are you seeing more family offices apply data analytics to help them meet their risk management and compliance obligations? What benefits can technological innovations offer?

Parfitt: Data analytics is an exciting and fast-developing area with the potential for significant business impact. It is becoming possible to track and report on key risk indicators (KRIs) automatically and in real time, supporting faster and more informed business decisions. This topic is still front-of-mind for global financial services providers, because the degree to which data within the organisation is actionable depends on its quality and scope. Technology should be at the heart of accelerating processes, providing greater insight into critical business relationships and alerting personnel to trends or breaches that may materially impact operations or crucial decisions. As an example, we see risk-averse organisations making extensive use of enhanced due diligence (EDD) reports to inform and manage business relationships, whether at the start of a new venture or at periodic intervals during the relationship to monitor any material changes in risk. Speed of delivery is critical here and new technology, data and automation is an enabler. But we also recognise the importance of human interpretation in faster decision making.

R&C: To what extent can technology enhance collaboration between the different functions within a family office?

Parfitt: Technology is fundamental for providing efficiencies and improving the quality of decision making but must be balanced with the scope and needs of the family office. The security of the information and the sensitivity of what is being collaborated on should also be risk assessed and ideally have an associated information security policy. This ensures that standards and regulatory compliance, for example with the EU General Data Protection Regulation (GDPR), are 'baked in'. It is encouraging that there are many relatively inexpensive IT solutions on the market that offer great collaboration, security and usability across multiple platforms, providing rich functionality at a relatively low cost. However, it is very important to have corresponding IT security policies and procedures to support IT usage and adoption.

R&C: What essential advice would you offer to family offices on adjusting their internal frameworks and processes to achieve higher levels of risk management and governance?

Parfitt: Perform an enterprise-wide risk assessment that looks at your office's operations, product and service offerings, jurisdictional exposure and the policies, systems and governance across the organisation. Then, overlay regulatory requirements – and importantly, make this an annual event so that you can identify changes in risk. If your office does require adherence to AML/CTF rules, then you need to make sure your risk rating of business relationships is accurate and that you can adjust risk controls accordingly. Governance and control are at the heart of risk management. This approach will enable a risk framework to be overlaid with actual processes and controls to indicate where there are gaps or areas for improvement. It may also indicate where your office is being overcautious.

R&C: Looking ahead, how do you expect the risks and compliance challenges for family offices to unfold and evolve over the coming years? What factors will separate those family offices that can successfully meet their obligations from those that fall short?

Parfitt: The global macro trends of the last 10 to 15 years point to a continued increase in regulatory and compliance rules and requirements that will only ensure a more complex operating environment, and this is unlikely to slow down anytime soon. The opportunity, though, is to be more proactive and use compliance as a competitive advantage. It can demonstrate to the wider business community that you know your risks and can manage them accordingly, and even allow you to take on higher risk as long as it can be identified and mitigated at a cost that does not break the business. Take a three- to five-year view of where the office is now and where it needs to be, factoring in expansion plans. Not taking this approach will only store up issues, putting the office on the 'back foot', which is draining for all involved and will ultimately limit business growth and profitability. R&C