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Ad Hoc and Risk Compliance

David Stoddard: Good morning, good afternoon or good evening depending on where you are in the world and welcome to today's webcast, "Ad Hoc Risk and Compliance Control" brought to you by Bank Systems and Technology, IBM and broadcast by United Business Media LLC.

I'm David Stoddard today's moderator. We want to make sure this event is as interactive as possible so I'd like to make a few announcements before we begin. Speaking of participation, you can join our interactive Q&A session at the end of the event by submitting your questions at any time during the webcast. Just type your question into the Ask a Question text area below the media player window and then click the Submit button. The slides will advance automatically throughout the event. If you would like you may download a copy of the slides by clicking on the Download Slides button located below the presentation window.

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Okay, on to our presentation and I'd like to introduce our speakers. We have Rod Nelsestuen, the Research Director for the Tower Group, Financial Strategies and IT Investments Cross Industry Group. He conducts research on business and IT strategies, emerging trends, growth strategies and issues germane to all verticals across the industry. Topics include customer experience, innovation, operational excellence, sourcing strategies, risk management including governance, risk management and compliance, GRC, and emerging trends.

And we have Joe Boissy the Director of Business Agility and Websphere Industry Marketing at IBM Software Group. He is responsible for the overall go-to-market strategy to all verticals and cross industry solutions for the entire Websphere product line -- excuse me, suite. He comes to IBM through the ILOG acquisition where he was the vice president of marketing. Joe brings over 20 years experience with a strong background in the financial services industry. He has developed many solutions that are currently implemented and deployed.

Joe, Rod, off to you.

Joe Boissy: Thank you David, this is Joe, good morning, good evening and good afternoon everyone. Thank you for joining us for our series in the webcast if you haven't listened to the last one please go back to our website and you can certainly listen to the ones that you missed. Today's topic is compliance and risk management and control. And those of us who have been in the financial services industry know that it's a heavily regulated industry, as you all know.

But we also know that it's unlikely to change, in fact more and more we see regulations coming down the road and being passed as laws. And so delighted to have with us today Rod Nelsestuen from Tower Group who is going to help us, shed some lights on that. So the way we're going to work today, Rod first will give us some insights on his perspective for likely the better part of 30 minutes and then I'll wrap up with a couple of case studies showcasing how our customers are using other technology in implementing compliance solutions and then we'll finish the hour with a series of Q&A.

Without further ado the floor is yours Rod.

Rod Nelsestuen: Well, thank you and thank you all for joining us today. I really appreciate the opportunity to take part and discuss what's happening in financial services across the globe in risk management and compliance. So if we jump to our agenda the next few minutes that I'm going to be talking to you, we're just starting to see what we're calling the rebirth of GRC. As we know, GRC is an old term, been around many years but it's essentially has been pretty ineffective for most of that time, in other words, governance, risk management and compliance has generally been more about the C, Compliance, than it is about the risk management.

And what we're seeing now is a real move to integrate and normalize compliance within a risk management framework to make compliance work as a part of the natural part of the business rather than having compliance become more of a one-off activity, which we've seen over the years in many institutions with separate siloes -- the departments that are working on compliance, almost totally disassociated with the rest of the business.

So, to set the stage for this we're going to spend a few minutes looking at what's the nature of change in 2011, so what are the drivers out there in the world that are driving financial institutions? What are the responses we're seeing as being the most common and what technology initiatives are being pursued in dealing with the world as it is today and as it will unfold over the next two or three years.

It's no surprise that people think that compliance -- think of compliance as the playbook in 2011. It's really a global phenomenon. There are rules that are just coming into fruition, many of these rules are have actually been out there for a long time, a long period of time, they've been talked about but they've not really been implemented at the level that they will be over the next couple of years.

The issue then is how do we create value out of this? Are we just going to comply, are we just going to manage risk, are we going to do them together, separately or what new value proposition value can we get out of the processes that we've put in place and the technologies we use to effect those processes, to improve business overall.

And that goes back then, to how we spend wisely on risk management and compliance and what will be spent, and then take a look at some of the horizontal tools that can be used in a business that will have multiple value propositions. So that's going to be our next few minutes -- the agenda for the next few minutes.

So what are the drivers, what are the big things that are happening? Well, it's no surprise, we already mentioned it, that regulation is the playbook. It doesn't matter where you are. It could be Dodd-Frank, Basel II and Basel III, Solvency II in Europe, the CARD As compared to, MiFiD in Europe, [Safa], whatever it is -- wherever you are there is a new set of regulations that are being developed and have been for some time but in the next year or two we're going to see the real implementation of those standards.

The world is a tougher place to do business, how do we find value, how do we create value, and how do we deliver value to customers? That is an area that's become much more complex and the business world itself has become much more complex.

And finally, one of the things that we're starting to see is a growing disparity between what we call industry leaders and what we see as industry laggards. And we think that that's going to have a tremendous impact on the long-term viability of firms that are falling behind.

So what do we see financial institutions doing about these things? Well, actually people are looking at their whole business model, how do we deliver, how do we make money, what kind of operations do we have, what's our business process for delivering a certain service, how can we do it more efficiently and effectively?

Another thing people are looking at is what lines of business should we be in. Which ones should we grow, which ones should we exit and which ones should we stay pat in? So a real -- a lot of work being done in the corner offices, in the boardrooms to come up with these strategic views of the world.

And then to understand and integrate risk management into operations. We think this has become a key function and a key necessary element to being successful over the long term. And more firms are realizing that they may have had good risk management in a variety of places in their institution, but unless they could connect the dots and draw value from one area into another in managing risk better, they were sub-optimizing their risk management capabilities.

And then everybody's talking about business transformation and we'll get into that in a little bit. SO what does this mean for technology and technology initiatives in the industry? Well, you can see that GRC is actually a number one technology initiative and many companies aren't necessarily calling it that but they are actively pursuing and are taking an architectural view in how they're going to manage risk better, comply with emerging and changing and constantly changing rules and regulations. And then in many cases are leveraging analytics along that line.

We always come back to one of the major challenges we find is data management and that's a problem for number one, as we've talked about. But now we start getting into issues that really look at the customer and customer value. We won't go through all of these but if you look at number three, improving the value of customer relationships, a better view of that and understanding on a real time basis how you're going to serve customers, how you're going to create loyalty, how you're going to gain their favor and grow the business again.

We're looking at cost containment through process automation and trying to figure out how we're going to improve our operational methods and processes. It used to be that your internal business processes didn't impact customer satisfaction. But the closer we move to a real time business environment the more financial institutions are realizing that it doesn't matter if it's in the back room or capital markets in the back office or the middle office, anything that's being done in a business process for example has a customer impact either directly or indirectly. And that's really important to keep in mind.

I think we'll look at number six, we'll look at the channel growth, enrichment and integration. One of the challenges there is finding ways to integrate channels. And channels do not go away, they just get added to. And we've seen that with the move to mobility. And mobility has taken on several fronts, it's not all about the cell phone it's about a multiple, a multitude of devices and capabilities and access channels that people are using on a mobile basis.

The other thing then is, let's look at number 10, planning, bundling and pricing product service spectrum. If you're thinking about products, how easily they're imitated, if you come up with a new product and how quickly the competition can imitate that and can you differentiate at the service levels. And if you can differentiate at service what does it take to do that? Well one of the things we're going to find out is that it impacts business processes pretty dramatically.

So this is a pretty high view of things and I think what we'll do now is drill in a little bit deeper and take a look at regulation. And this is a global phenomenon. We're going to spend just a couple of minutes on a handful of regulations instead, because we think we'll be able to bring them back to why the business process that you put in place is so critical and so important to being able to manage this complexity that's out there today.

So let's take a look at our first regulation, something we all know and have heard about. We know that Basel II focused on credit pretty heavily and operational risk was only partially defined and hardly really addressed. Even though in many parts of Europe a lot of firms have spent a lot of time looking at operational risk.

We know that Basel III has really upped the anti for liquidity and liquidity management, understanding not only what is liquid but what is the impact, what are the things that impact the liquidity and levels of liquidity. What kind of contingency plans do we need to have in place? What do we need to know about our investments and win? This is a set of information that needs to flow into the institution, not for compliance purposes but to manage the business better.

At the same time, this is not the end either. We don't think that the implementation of Basel III will solve all the problems having to do with toxic assets. They'll always be with us, we'll create new ones, we'll find new ones. The nature of innovation is that while many innovations deliver high value to customers, the market place and the financial services industry there are some things that go awry once in a while.

We also know that regulators are going to have very little patience for repeated failure and so will customers, they will have very little as well. Some of the things we don't' know for example about Basel III is really what's going to be liquid as conditions change, the ability to stress test and model those kinds of things and then display that modeling to the regulator, are going to be very, very important.

The other thing is, if we look at Basel III, it's adopted widely in Europe, Canada, it may not be adopted as is in North America. And thus banks that are operating on multiple regulatory regimes are going to find themselves having to comply with different sets of rules in different places.

So we can take a look at the capital requirements. The only real point I want to make here is that we've had this, for the last three years, we've hosted a risk event in Europe and we've had over 40 senior risk officers from both Continental Europe and the UK take part. And as they looked at some of the changes that were being discussed at that time, in May of last year they came to a conclusion that banking will be less profitable. And then we spent a fair amount of time talking about how can we overcome that, what does this mean for the operations, what does this mean for being able to deliver value and to be able to be paid for that value going forward?

We can jump from the financial services side to more of an insurance side and we know that for example that in December the pronouncement was made that by December 31, 2012 the implementation date is fixed for Solvency II. But the problem is that amendments also enable the Europe Commission to specify transitional measures in certain areas so that different targets will have to be met and different hurdles will have to be cleared at different times. What we believe is going to come of this is while this is welcome by some what it really does is increase the complexity and requires a lot more flexibility in both data analysis reporting and planning and the capability to move data around and manage it in a better sense.

By the same token we know that in December a Consultation Paper affirmed the goals of MiFiD in Europe, however, we -- one of the key issues there is there is going to be an extension in looking at investor protection -- raising the bar, for investor protection which is necessarily going to demand more data, more information. And then the regular -- the convergence of regulatory framework and supervisory practices simply means that the level of conversation that most institutions will have to have with their regulator is going to be -- it's going to increase in frequency and should go up in quality and quantity. So what this does, it really this is continuous change we see happening here and it's going to demand greater flexibility and better access to information in many ways, shapes and forms.

Then we can talk a little bit about the US and the US Dodd-Frank Act which is currently in process and interestingly many of the deadlines that regulators had for issuing initial regulations are quickly upon us, some have passed and the regulators have been unable to meet them. So what we really see happening here is an increase in the paper chase that's going to be necessary if you are going to be compliant with the full Dodd-Frank Act, which is a massive change to the financial services industry in the US.

Retrieving service records for foreclosures, we've seen the challenges banks have had in cases where foreclosures have been called into question and the issue of did you do the proper servicing, have you given proper notice, can you prove all of these things, can you demonstrate beyond a doubt, by -- because you've got the right automated trail, that you can deliver that kind of information without doing -- without going off and putting four or five people into a manual process to pull all things together? This is really about business process.

The issue of having multiple levels of transparency. Being able to see down into the guts of the operation and understand what processes are in place and if they are correct then I think the regulatory burden goes down. We know that reporting frequencies and complexity will be increased. And then understanding investments at a different level, whether they're being done in highly unique and exogenous derivatives coming in to the institution to manage risk, or whether they're simply done as part of the business in looking at profit opportunities, there is going to be a significant change there.

And what we're really seeing happen is that there is going to be this tremendous open-ended information request. And how is that going to be managed. Well, first of all we see that the -- before we get to exactly how we see the challenges of managing this, we know that the regulatory impact is really going to vary by industry vertical. So capital markets whether you're in the UK, Europe, the US or anywhere else in the globe, the capital markets industry is facing some of the biggest changes that are out there. Of course, retail banks are going to have a pretty significant increase on the consumer side in Europe and in the US. And then the card industry in the US has been undergoing a great deal of regulatory oversight that's going to dramatically change how they manage their operations as well.

If we want to take a look at what really is going to be faced here, is that as we look at the industry segments on the left-hand side of the slide, we also include not only those that we've known for years, but also the previously unregulated financial institutions including hedge funds, private equity firms and possibly others, the payment providers that have typically been left outside of the regulatory environment can now easily be called in. And we're using the Dodd-Frank Act here as a straw model, but will show you I think that this will be a global phenomenon.

So in the Dodd-Frank Act the Office of Financial Research is mandated to develop a regulatory data center. And what they're going to do then is they are going to request data from all of the financial institutions, certainly not just the banks -- that could be 15,000 to 20,000 different companies throughout the US for example. And this is what they're going to get, multiple data sets, varied formats, different time sequences, different levels of quality and different standards, different definitions. It's going to be a real challenge to be able to get a clear definition that this new regulatory data center will want to develop.

So what that's going to force them to do is define the data for you. And now when they're defining the data that's going to create something that regulators will leave you no choice over. And that regulatory data set actually may or may not have any business value to. Now, we see this as really going to be a scenario that is repeated globally, not just in the US, we see it very clearly in the US over the next two to three years but certainly it's happening elsewhere as firms are trying to get their arms around the data access issues.

So we've talked about regulations then and at this point what I would like to do is drill down into one specific area within risk management and compliance, to go back and talk about how we extend value across the business or a particular function which is both managing risk and complying. So if we take a look at the example here, some of the top drivers that -- as we talked about globally, we'll look at them within financial crimes management. It's no secret that there is continuous and new and emerging threats. And that's not going to stop. We see the macro threats such as the WikiLeaks of the world, we see the micro threats as surreptitious criminals that are stealing data, enriching that data and reselling it. We see the extension of botnets and other technological threats.

And what institutions have been doing over the last year and are doing going forward is they're trying to figure out how to manage risk better, across the institution and to comply with the rules and regulations. As we know fraud management and fraud issues are not far from the whole issue of the Patriot Act and some of the other anti-money laundering rules that are globally pervasive as well.

So the technology tends we've seen, we've started to see some convergence between risk and compliance but a new area is cropping up as well and that is opportunity management. So in other words it's not all about risk, it's not all about compliance, but it also brings into play the issue of being able to create new business opportunity out of the kinds of activities you do in managing a function such as fraud or financial crimes.

So let's take a look at an example here of how we integrate risk and fraud management at an enterprise level. If you look on the left-hand side if you're looking at enterprise fraud management you can detect and evaluate, respond and you update. So you really have a way to improve the output and reduce -- if you find a threat and you find ways to head it off you can reduce that threat even though we know there will be new threats that emerge.

On the far right-hand side, we're trying to integrate that particular fraud management activity with risk management. So what we have is ability to see what is transpiring, see what happened and then to understand what we saw. Then collaboration is really the tool that is tied to business process management because it brings in experts from across the institution, data from across the institution and improves and enhances the business intelligence that you can get out of that risk that you have just encountered, whether it's an event or a series of events or a whole area of risk management.

You can take more effective action and then take a look at looking at uncovering risk correlations between what may be happening for example in a fraud management case for internal purposes and a fraud management case for external purposes. So it's the real-time management of risk that helps you understand what's going on, builds a collaboration model that delivers higher value for risk management and then captures the data, captures the processes and can re -- can deliver those processes and insight into those processes to make sure you're complying with the rules, regardless of where you are.

If we want to drill down a little further here, we'll go into a specific example of how this works in managing business process for an internal fraud event. So here we have an automated case is created out of an incident that is captured by the fraud detection technology and it appears to be an internal fraud event. Well, you don't have this thing fully understood yet, so the investigator takes control of the internal fraud management case and then by having the business processes built in and automated a number of things can happen simultaneously. If you look under number three, we're notifying the legal department that something is potentially happening and they need to be ready to take action.

We notify IT that we may limit the security access and systems access of an individual or group of individuals because of the challenge -- because of the potential case. And you may either call for that to happen now or you may say, at some point, if you don't hear from me within 30 minutes please end the security -- or take this person off access for all the systems that they have.

Obviously management groups need to be informed and different levels of management need different levels of information. Not everybody can absorb all of the information all at one time and they don't need to know. If this is a real critical issue, especially if you're thinking in terms of an internal fraud event where, if it's a false event and a false positive for example, what you then face is the specter of an employee -- accusing an employee when nothing was wrong. So you really need to understand this in the first place and alert -- give the proper alerts and understand what's going on before you make the call. And then you can notify human resources and they can stand by as the investigation goes on.

Now, maybe you notify the customer at this point, maybe you don't, that's a decision that you can make but the issue then is that you can use the same set of information, the same business process flow to define the information that you need to provide the customer.

So what we've done here is really take a single fraud event, we've automated the notification of the right people, getting the right information, simultaneously. And then we can make better decisions when we are sure of the case or not.

SO how does this play into more holistic risk management. Well, as you see on the left-hand side we have the case again where -- the automated case is generated and the investigator is managing this and the same kinds of business processes can be automated again to notify the chief risk officer, not necessarily of this event and all the details but potentially for statistical and analysis purposes. You can notify the chief operating officer who may then investigate process gaps and look at data that needs to be handled in a different way.

Perhaps you've been working with an outsource and that outsource has either interfaces with your internal employee or maybe you've detected the fraud at the outsourcer, whatever the case you can notify that outsourcing company or that service provider as well. And then audit can receive a certain set of information as well. So what we've just taken here is by automating business processes we were able to manage the event, then we were able to contribute to holistic risk management.

And if you take all of what we've talked about now with an internal view, what we're looking at here is really the customer view. The customer doesn't really know any of this is going on as it goes on. And so what they have is just their view of the world which is all of the different contact points they may have with you as a financial institution. They may be working through a third party, they may be accessing something through a mobile device, they may be at a point of sale or a branch, they may be through an outsource call center. So that all of these different areas, from a customer perspective need to be orchestrated so that when a customer is moving between all of these different areas they don't find a huge disconnect.

Now this not necessarily easy to orchestrate but it's really about protecting the customer and your business by being able to deliver the types of information we talked about on the last two slides so that the customer is the one that's protected on -- as we look at this view of the case that we have just talked about.

So how do you create new value? That's one of the things people say, if I've got a fraud case, how do we create new value? We have an actual case study that we've done about a customer living in the Midwest of the US and they had a $6,000 they were running up on their charge card on a Saturday in Miami. The fraud technology alerted -- because it was way out of character and it alerted the potential for fraud and they halted a transaction at Home Depot. The processor got on the phone with the checkout counter and talked to the customer and went through some security checks and asked the right questions and got the right answers and determined that oh, this is an okay deal, what they were doing is they're buying a townhouse in Florida and in this case the customer was furnishing that townhouse.

So the processor approved the transaction, documents the file and closes the case. But what did they miss on the business of things? Well, if you look over on the left side there are a host of questions that come to mind from this false positive and that is, will the customer payoff their Midwest mortgage? Could the customer be in need of a home equity line of credit or did they use a home equity line of credit if they have it. Is it time for a new car, is their card product still viable for them?

Does the customer use online services or will we lose them if they actually move or if they spend part of the year in the South? So what turned out to be in the case of a potential fraud incident is really a signal for a lifecycle change for that customer. Now this event alone of course wouldn't be enough necessarily to signal a lifecycle change. But you have enough information on a client in the institution. If you can combine it and deliver it to the right people, you might be able to head off loss of a valuable customer.

So in summary, just talking about the financial crimes side of things, we see extending the business value is really a cascading process starting with board policy, implementing the report and case level data and aggregating data, applying the analytics to discover new business value through process management and then to execute on those processes while you are complying because your processes are built into a compliance methodology.

And then finally, to facilitate external audit, enabling forensics and protecting customers and company information through the process design and automation.

Well, we have some spending estimates on risk and compliance. And we're first going to look at what we think is going to happen next year on compliance spending. First of all, we think globally there will be $32 billion spent next year on compliance and it will be broken into these categories. As you can see, modeling, analytics and rules engines are going to have a tremendous investment and that investment is going to have to be made to follow -- to enable all of the compliance rules that are out there and have yet to be developed.

See, another significant investment in data management and reporting. Again, compliance being what it is, the ability to report is going to be critical as well.

If we take that $32 billion and look at it another way, in the traditional mode we see the credit risk is still going to get most of the spending but there will be significant analysis and modeling and stress testing being done on market risk. And then, operational risk is really the one that's been underinvested globally over the past several years and we see a huge investment in that for compliance.

Now you can see there's some -- the way these -- this $32 billion will be spent is broken out here with the bulk of it still being spent internally but with significant opportunities, specifically for software to enhance the compliance capabilities in building business processes and capturing data for compliance purposes.

So this adds up to the $32 billion we see being spent in 2012. Well, on the other hand, risk management has its own spending view as well. Now, we think another $30 billion is going to be spent here. Again, you'll see the bulk of this being spent on modeling, analytics and rules. You'll see much less being spent on reporting because when we get to the software side of things, many of the risk management software tools which are being enhanced by combining them into a framework under a process management tools, the reporting is enabled within those tools rather than being one-off types of reporting for the financial institution.

Again, we see the bulk of the spending being done in credit risk, but a significant investment in operational and other risk as well because these are the least understood, both from a compliance perspective and from a real, actual risk perspective. And here again, we see that the spending on -- both internally and on external software is going to add to the $30 billion figure that we see being spent in 2012.

So to summarize this aspect of it, globally spending on risk management will be $30 billion with another $32 billion on compliance. After 2012 the need for risk management will drastically be altered because of changes in the financial services market place, and delivery mechanisms, the business models that FSIs, or financial institutions are building and that sea of new regulations that will be in place.

We see the role of the chief risk officer as becoming more important. However, it's still an underutilization of a key resource. We also think that companies that aren't serious about conquering risk management and compliance will find that after 12 to 18 months and a return to what we might call normal, or even a new normal, people will begin to forget about the importance of risk management and compliance in a way that they now have piqued their attention to.

And then finally, new regulations are going to drive an upgrade to the risk management practicing capabilities and will drive a separate line of spending for compliance. Now, we think much of this can be integrated but we don't see that happening currently.

So we'll tie some things together here as we kind of conclude and look at the value points that we see developing in IT. For example, data. There's more of it, it's more of it, it's unstructured, it's overlapping, it's real time, it's a challenge and it's going to continue to be a challenge to develop over the -- to get your arms around data over the next several years.

Analytics. It's been all over the financial institutions, but -- and in 2009 and 2010, but really uncovering new business value as we talked about in our example of a consumer where we had a false positive on a potential fraud event, that's where we see analytics really adding new business value going forward.

Business intelligence. We've seen a real increase in the use of business intelligence, applying analytics to it and a lot of very interesting things happening such as more of the CRM capability and more of that corporate performance management capability has been pulled into business management tools. But the challenge there is that unless they are put into business processes, which we see happening in 2012, unless that -- this business intelligence actually impacts and can be implemented in a business process, it will have less meaning and in fact it will be ignored in many cases.

On demand access. Pretty much a need for regulators and business users, whether it's risk management or compliance. Safety and soundness. Again, the new -- a new look at stress testing and liquidity management. And being able to incorporate that, for example all the way down to almost the trading desk level where you have a trader doing major movements and taking major risk positions where you're going to have to be able, on the spot, provide that trader with information about capital allocation for example, how their portfolio will change and how the capital will be -- what the capital will be demanded for the trade they're about to do and project this to see if the trader wants to go through with it or not.

Security, of course is a never-ending process and we think that both managing regulation and managing threats will -- are not necessarily the same thing and you really need to think about security as a business option, more than a regulatory option.

And then we're going to see that most institutions will find themselves dealing in multiple parts of the world and you're going to have multiple sets of rules and your ability to understand, have rules in a controlled environment and build your processes so that you can meet those rules, clearing the highest bar regardless of where that bar is.

So what we really think is going to happen here is the combined pressure of regulatory aggressiveness and customer demands and the continuous technology advancements are really going to force some hard decisions and new approach to business and the business model. Mastery of data is really going to emerge as a defining skill for differentiation in all segments of the industry.

A holistic approach to risk and compliance really has new business value, we showed one brief example of that, we know that there are several more. We have other case studies and we'd be happy to talk about those if you're interested.

Business process management will be a determining factor of success because many things are still executed by people. And the relationship with customers are still built, in many cases, around people. And if business processes are not integrated smoothly, not integrated within the stream of business and business processes are not friendly to both the user, could be an internal staff person, and externally to the customer, that's going to be a determining factor of whether you're successful or not.

And finally, while the market place continues to evolve, the issue of having the capability to amend business rules, change them on the fly, is going to be continuously important, simply because compliance is still going to be a five- to eight-year journey as we've seen with the implementation being spread out for Solvency II as we've seen with Basel III, the standards being spread out all the way out to 2019 and other issues in the US such as the Dodd-Frank Act, and some of those rules being spread out over several years to come.

So the issue is being able to create new opportunity to repurpose risk and compliance spending to create that new business opportunity, is really where you can get a new value proposition. But you can't do it unless you're able to tie it in to the business operations and make it seamless to the customer and to the internal user.

I'd like to turn the floor back to Joe.

Joe Boissy: Thank you Rod, thank you for these great insights. And it's certainly I think where -- it definitely shows that risk and compliance don't have to necessarily be seen as a constraint and as a difficult thing to work with or something we have to go by. But certainly it's an interesting approach that looking at the solution you can turn it around and make it as an opportunity as opposed to only be something to be compliant with or we have to abide by a particular rule.

So what I would like to do over the next 10 minutes or so is just giving you a couple of case studies that showcase how to use the technology. And for that, I'd like to start by maybe level setting a little bit and for that I'm going to go to this chart that shows you risk and compliance, what do we do in BPM and BRMS. And I know maybe these are acronyms are that you're not familiar with, but BPM as Rod mentioned, stands for business process management.

And business process management is the set of tools that you have to model, create and analyze and execute on the various steps that go from inception to settlement of any process, including like a risk management process, a compliance process, any kind of thing that's happening operationally in your enterprise.

Now, within that process there are -- there's a particular area which is very, very relevant to risk and compliance and it's what we call rules. And you heard the term many times, rules for like a rule engine. And I'm going to explain here what we mean by BRMS which is business rule management system. And if you think about it for a second, the rules that we're talking about we're talking about eligibility rules, fraud detection rules, all things related to AML rules, credit risk rules, operational risk rules, any kind of compliance rules.

All these rules are scattered around in fact, you'll either find them inside of applications, inside documents, inside Excel spreadsheets or things like that. And even within processes themselves. And sometimes you can find them even in the heads of people, people think about them, we have this policy, it's a new policy for this thing and it's not written. Maybe it's written somewhere but it's only in the heads of the people it's not implemented by any means, by any automated means for that.

And the idea of a BRMS is to automate that. And first thing, and foremost, what you do is you extract all these rules and you put them in a central repository. And the idea here, of course, is not to have inconsistency when it comes to rules. You have a new rule come into play, this rule will be placed in somewhere and this will be shared across the processes, across the applications that are using that tool.

On top of it, these rules are not written in obscure or programmatic language. And what that means, it means that now business users are able or capable of changing, monitoring, creating, offering, maintaining these rules. So we're not talking about IT being involved every single time we have a new policy or a new change in a rule or a new compliance mandate. Each and every time we're doing that, the compliance office or the compliance manager, the compliance program manager, the risk manager, can themselves make the changes because they're written in plain English, or plain language, that you're talking in.

Now, of course, on that, you have what we call the rule engine, the rule server, that will be executing and automating these rules -- automating these rules, within the processes, and that's what makes it really interesting as a whole perspective. And on top of the whole thing, that's what we call the BRMS or the business rule management system.

Now I'm going to go in and showcase a couple of cases. The first one is that a big -- one of the largest banks here in the -- in North America. And their situation was primarily they were coming under scrutiny, coming to fraud. And they realized that they need to much better -- they need to get their act much better when it comes to know your customer AML.

And this is not, I think, typical to that particular bank. Any bank that has that size, which means its been acquiring banks after banks and smaller and bigger institutions, year-over-year, you end up with a multiple systems. And you end up with difficulties, in fact, to implement a bank-wide, consistent program for compliance. And that's what happened here. And so they embarked on this project, which the -- really centered around, first, KYC and AML. And, of course, that would help them first to understand better how things are working together, but more importantly how to make things consistent across their branches, across their routes.

So the project, in fact, you can see here, the key business outcomes, how they were able to reduce dramatically their operational costs, but I think if you look at the implementation of the projects, that was even more interesting because they started with a particular project that was only on KYC and AMLs. But then, again, going back to what Rod was mentioning earlier, about how to create value, they started going, okay, we know now, we have the fraud situation, we're managing that, we're automating this thing to detect automatically the rules. What happens when we have rules that are coming into play that are interesting?

So they created the dynamic questionnaire, which are the ways of understanding, detecting these things, and examples that they gave earlier, Rod, is exactly that kind of thing they were able to do. It's taking a situation, taking an alert, taking an event, and from that, converting it into a situation where they can understand better the account, understand better how to do that.

And they did that gradually.

The important thing to mention here, when we talk about these projects, we're not talking about projects that take years and years to implement. You can immediately get benefits within the quarter, within two quarters. We have something implemented. We have something you start using, you put in production and start using.

Now I'm going to switch to another application, another type of application. This one, we're talking about another example where a customer is in Europe, it's a very large bank in Europe, and this time it's more regarding risk management and preventive care for their customers. And the idea here was not much about -- they were facing a situation where they were -- they did an analysis and they realized that they have a lot of, a lot of -- their customers, when they're doing defaults or they're going bankrupt, if you like, they were not -- they didn't have any way of looking into it.

So what they did is that they made analysis of the situation. They realized that the advisors, the people who are on a day-to-day basis advising their customers on what to do and what kind of products they need to buy and what kind of applications they have to go buy to apply for new products, were not necessarily aware of the latest and greatest in the offering of the bank.

So they went into creating this project, which was simply about doing two things. The first thing you can see here, on the right side, is overnight they were processing everything that is happening on their customer base. And from that, they were able to understand better what are the best situations, combining that with business analytics to detect when is -- the customers -- or when is the customer potentially going to go bankrupt?

And before doing that, they were able to prevent that by offering their customers the right tools.

So not only, again, going back to creating value here, not only they were able to prevent things -- to detect when bad things are happening or about to happen, they were able to advise their customers what are the right things to do in order to do that. And in the end, the results were night and day between the difference from before, when, again, not only counting about the time wasted by the advisors, they were spending hours and hours, almost a couple of hours every single advisor, and they had 13,000 of them, just looking at things and trying to browse and understand what to do. And after that, they were really guided by the system to tell exactly what to tell to the customers, what to present to them.

So these are two examples, and we can go on a lot of others. But the bottom line is that with this expertise, what we're trying to tell you here is that you have a number of benefits that you can get immediately from a system like this. I remember the first time we were talking -- the worst thing that can happen for a situation is not necessarily not to be compliant with the regulations, it's not to know if you are compliant with the regulations. Because, and this is where it comes into play, we heard that from Rod, about DFA, the Dodd-Frank Act, you have to document, you have to demonstrate, without a doubt, that everything that happens is needed.

But what BRMS and BMP prevents you here, is the -- it provides you, is the possibility of delivering not only a finer grain understanding of what happens when, but you can trace it, you can analyze it and you can create it in a way that there's no doubt here. You see what happens. You have a report that tells you what rules are in application, what rules are being accessed and where they're accessed.

So that's one way of looking at it.

Another thing, which is very important, again, is that the possibility of having the business people, the line of business people, and not IT, involved in every single time you want to make a change to a rule, make a dramatic difference here. Because as you know, and you'll see it, these regulations keep changing. These regulations keep coming.

So if you want to burden the IT department every single time you have a change in rule, a modification to a rule, you're going to -- it's going to take a much longer time. And frankly you won't be as efficient as you have the possibility of, within your line of business, within your compliance team, able to make the changes, understand those things.

And again, one more thing, when we talk about compliance, when we talk about things, a number of our customers are returning this in upside down. And by that I mean, instead of saying, well, there's a Regulation D coming, there's a Regulation E coming down the road and we have to cope with it, and saying okay, that's a constraint, let's make sure that we're compliant with that, well, they are getting ready for that way ahead of time, when they know the regulation is in play, when they know the regulation is going to come and become law pretty soon.

They start, because the BRMS and BPM system allows them to emulate the system, they go with the what-if analysis. So they go and they implement, in their system, the new regulation, even though it's not yet official. It's not yet mandated. It's not yet passed as a law. And they run that and they emulate that with their existing set of customers that have transactions. And as a result, they look at it and say, what's the outcome? And out of that, they are able to make the necessary changes, either in their organization or in their divisions or in their products, either to better cope and use that, again, returning and maybe as an opportunity, and creating value out of it.

So that's it.

Now, with all said, I'd like to say, okay, well how do you go about that? I have two options to propose to you here.

Firstly is, we have something we call the process improvement discovery workshop. Because we believe, and after we've done many of these applications in the implementations, in over 1,000 implementations left and right on BRMS and BPM, we know that there's no one-size-fits-all.

And as a result, we know that the best way to go about it is to sit down with you and when we sit with you, it's both with IT and line-of-business, and go over, we have a very, very methodical methodology that details how to do, what to do, what to decide and where to start. And, again, we're not talking about projects that take years to be implemented. We're talking about projects, specifically, that are in 45 days. You have something running and in production that you can use and start using it very quickly in your system.

And the second way of looking at it is really going about documenting and running the processes in the cloud. And for that, you don't have to have anything. You just go and sign up for our Blueworks Live, which you have the link here on the page.

And this allows you to say collaboration, understand better with your collaborators -- with your partners, with customers, with your colleagues around the world, what to do, what's the process, how is it like and how to make it work for your compliance needs.

Next, I'd like to invite you to come to our big user conference. This is a yearly conference in Vegas. Usually we have around -- last year, we had over 6,000 customers. We're projecting close to 7,000 customers this year. This is a great opportunity, not only to mingle with your colleagues and see what's going on with a lot of customers from the banking industry who come to this conference, but also we have a very, very well thought out, both technology program and a Forbes business leadership program. So you can benefit on both sides. And if you happen to be more than one individual to sign up for this conference, you can have a special discount at a company pass, at the link, ibm.com/impact.

My last slide here is really some links to some solution overviews, some success stories, some learning demos and things like that, that you can use. Please feel free to go to these, there were great stories there, great documents that you can download.

With that, I thank you and back to you, David.

David Stoddard: Great. Thank you, Joe. And thank you, Rod. Great presentations. Very timely, considering what organizations are concerned with these days.

So we're going to move into our Q&A portion. Before we do that, I wanted to put before you, our attendees, our feedback form and links to our feedback form and it would be very helpful to us, with future broadcasts, to get you feedback about how we can improve and anything you'd like to see in webcasts in the future.

Okay.

Well, let's move on to the Q&A portion. And just to remind everyone, if you'd like to submit a question, all you've got to do is type your question in the Ask a Question text area below the media player window and then click the Submit button and we'll address your question.

So let's go to the first question today. Rod, it looks like one for you. Does more accurate and sophisticated risk management software and techniques mean profit centers will pay more attention when recommendations reduce profits or bonuses?

Rod Nelsestuen: Well, I think you mentioned the world in bonus that -- gets my attention anyway, I'm one of those people that, yes, the -- because information is always -- has not always been accurate. And if you're in the throes of the business, you're an experienced trader, for example, and you're making a decision based on years of experience, past the proof points that you have in mind, and also the whole issue of gut feel that traders still use, sometimes you need better quality information and that better quality information, if you know can trust the information, I think it has a tremendous impact on the ability to impact how I think about what I'm going to do, what that's going to mean to me going forward. And specifically, again, as we're starting to see firms seeing interest again, especially in very large trade deals, be able to pre-analyze trade on the spot and do some capital allocation to that trade, to see, for example, from a trader's perspective, is the reward great enough for the risk that they're taking and the capital that they're exposing to it?

David Stoddard: Okay. Great. The next question is for you, Joe.

Local versus global. Does centralized rule repository -- or a centralized rule repository mean that we need to go with a one size fits all approach? For instance, can we define region- or product-centric risk management rules?

Joe Boissy: Yes, absolutely not. In fact, the central repository for rules means that we have consistency across multiple systems, multiple applications, if we opt to use the same rules. However, we can, and that's what all customers do, decide on the hierarchy of the rules. For example, they can say, okay, this is the overarching rule for our internal compliance. This is what we need to do and this is non-negotiable. Everyone has to abide and go by these rules.

But then you have specificities. Either by region or by typical divisions or specifically for typical types of regulations that are -- don't apply the same way in country A and country B. And that is always something that you can implement and that's what implemented the system. In fact, allows you to doing that.

And not only the system that allows you to do that, but it can have also a permissioning system that says I am responsible for compliance for them, for my region, and therefore, that's the area that I can touch and only these areas that I can touch. However, someone else, who's responsible for another region can own their own region. And someone else who is responsible for the overarching mandate can touch whichever they like.

So the whole permissioning system also lends itself very well for a very much organized system that can be, at the same time, centralized, but at the same time, very much coping and caring for specific needs for each region.

David Stoddard: Okay. Good. Thank you. A question, it looks like, for you, Rod.

Have you estimated the rate of growth in spend in this space? So you referenced the total estimated spend. I wanted to know if the increased regulations are driving significant increase in spend?

Rod Nelsestuen: Yes, we see it driving spending between maybe a two- or three-year period, a year-over-year, somewhere around 10%.

So it's in it and you can compound that as you go. So the spending that we have, the reason we talk about 2012, for example, is that we did some estimates for 2011, which incorporate some of the dollars you saw in the estimates for 2012. What really happened, and we put that together late last year, is that we've seen the implementation time tables slip, not necessarily at the institutional level, but at the regulatory level.

So this whole issue of the money's going to get spent, but we look like it's going to get compressed and it's going to get pushed into 2012, so if you look back a couple of years, there have been some investments being made like 2011, 2012, would have been around 10% each year, but much of this now is being pushed into 2012.

We haven't actually gone back and said how many -- exactly how much dollar-for-dollar and what does it mean for 2012? Because that's still unfolding. And as we know, many of the rules negate time in 2012, still won't have to be complied with until sometime after 2012. So it's a really -- we're really starting to see a compression of the spending going into 2012 and beyond.

David Stoddard: Great. Joe, here's one for you. Are impact analysis capabilities for IT users only? Or do you have these available for business users as well?

Joe Boissy: Absolutely. It's primarily done, in fact, for business users more than IT. I mean, IT are here to make sure that the system is well -- and the infrastructure of the system is well orchestrated, that everything is done in a proper way, that we have all the back-ups and things.

But primarily, IT is important -- involved in the implementation, putting the platform together, the infrastructure, and the rest, 99% of the time, is really going to be handed off to the business users.

So from the impact analysis, most of the time, the users that are using the emulations, the systems, the test analysis, the what-if analysis, and all the kind of simulations that we do, are in fact the business people. They run the system, they take their portfolio either from historical values or theoretical values, and as they run it on their rules and say, okay, well, let's fine tune these rules because they're not giving the outcomes that we'd like.

And they can continue to fine tune that until a point where they see, okay, this is a good set of rules that we like. These are the good parameters that we have. Now we can put it in production.

David Stoddard: Okay. Great. A question for you, Rod. Is there a study or rule of thumb as to whether to use the highest common factor of rules across all geographies versus customizing by geographies?

Rod Nelsestuen: Well, I think that's a choice. I mean, if you -- if you're clearing the highest bar across all of geographies, then you're going to be okay in those, where the standards may not be that high. If I understand the question right. So I mean, you can implement things that way.

But I think one of the true advantages of business rules tools and capabilities is you can configure that to -- so that you have a different rule for one part of Europe and another part of Europe, based on the rules that are explicit to those areas and you can be compliant everywhere with the controls that you need in place.

So I think that's really where the advantage is, although as I said, I mean, if you really want to set -- let's set the highest bar and operate that way everywhere, you can do that. And maybe some institutions would do that because of capital constraints or reasons that they just want to keep it there, they have a very narrow, simplified business model. But I think the reality, it's -- it's really something you should look at regionally.

David Stoddard: Okay. Great. Thank you, Rod. Thank you, Joe, for all your answers and thank you to our attendees, who had some great questions. If there are questions that you asked that we didn't get to, someone will respond to you shortly with the answers. And so let me move to close our broadcast for today.

Thank you for attending today's webcast, Ad Hoc Risk and Compliance Control, brought to you by Bank Systems and Tech, and IBM.

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On behalf of our guests, Joe Boissy and Rod Nelsestuen, thanks for your time and have a great day.