Osborne Clarke's 2022 Future of Financial Services week

The future of advice and AI in financial services

9 March 2022

Speaking with you today

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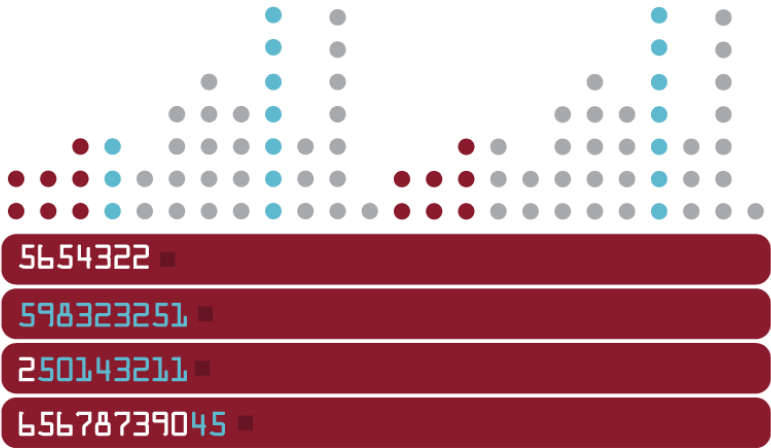T +44 20 7105 7105
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AI and Machine Learning
What is the difference between AI, ML and Deep Learning?

Decision Tree →

Bayes Net →

Deep Neural Network →

← Neural network

Artificial Intelligence

Machine Learning

Deep Learning

Machine Learning

What makes the technology different?

Traditional

Problem

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Prescriptive Program

Defined Solution

ML

Problem

Training Process (data dependent)

Variable Solution

Machine Learning
What makes the technology different?

Training

Supervised

Known results
(labelled data)

Unsupervised

Unknown results
(unlabelled data)

Reinforcement

Competitive closed
environments
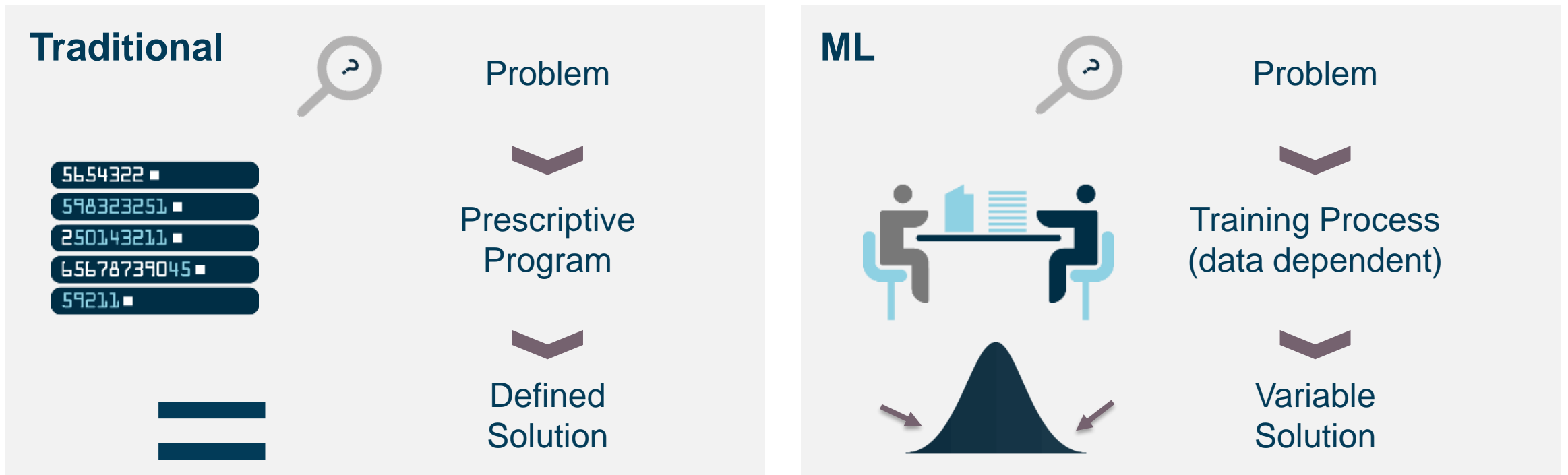
Machine Learning

What makes the technology different?
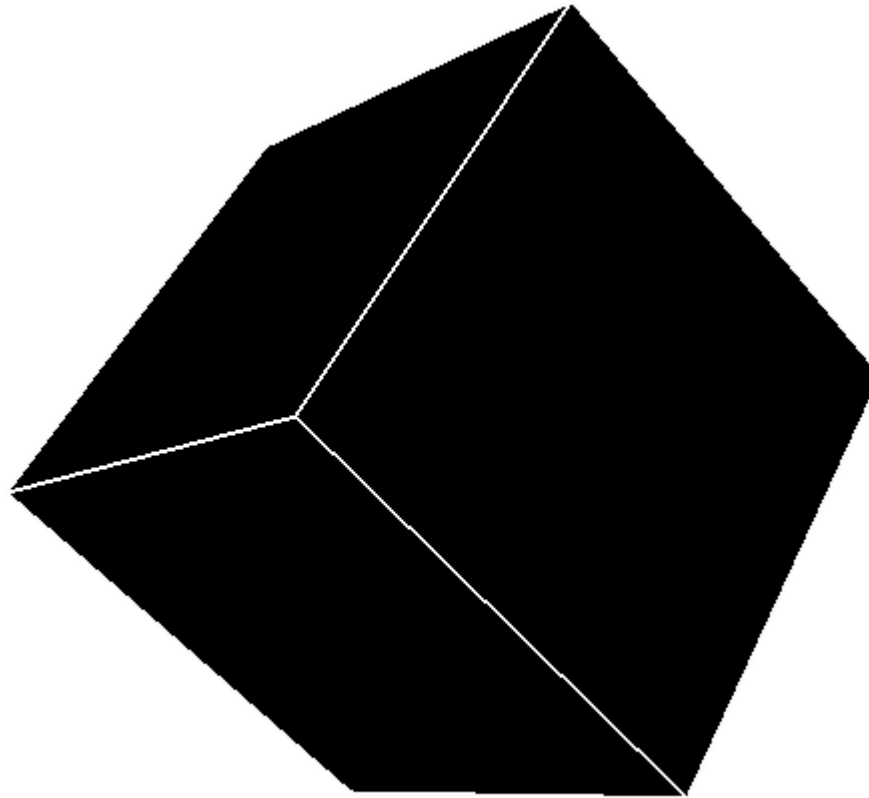
Machine Learning – What's it good at?
Classification

Machine learning helps us predict a category based on the data the system has been trained on.

Cat
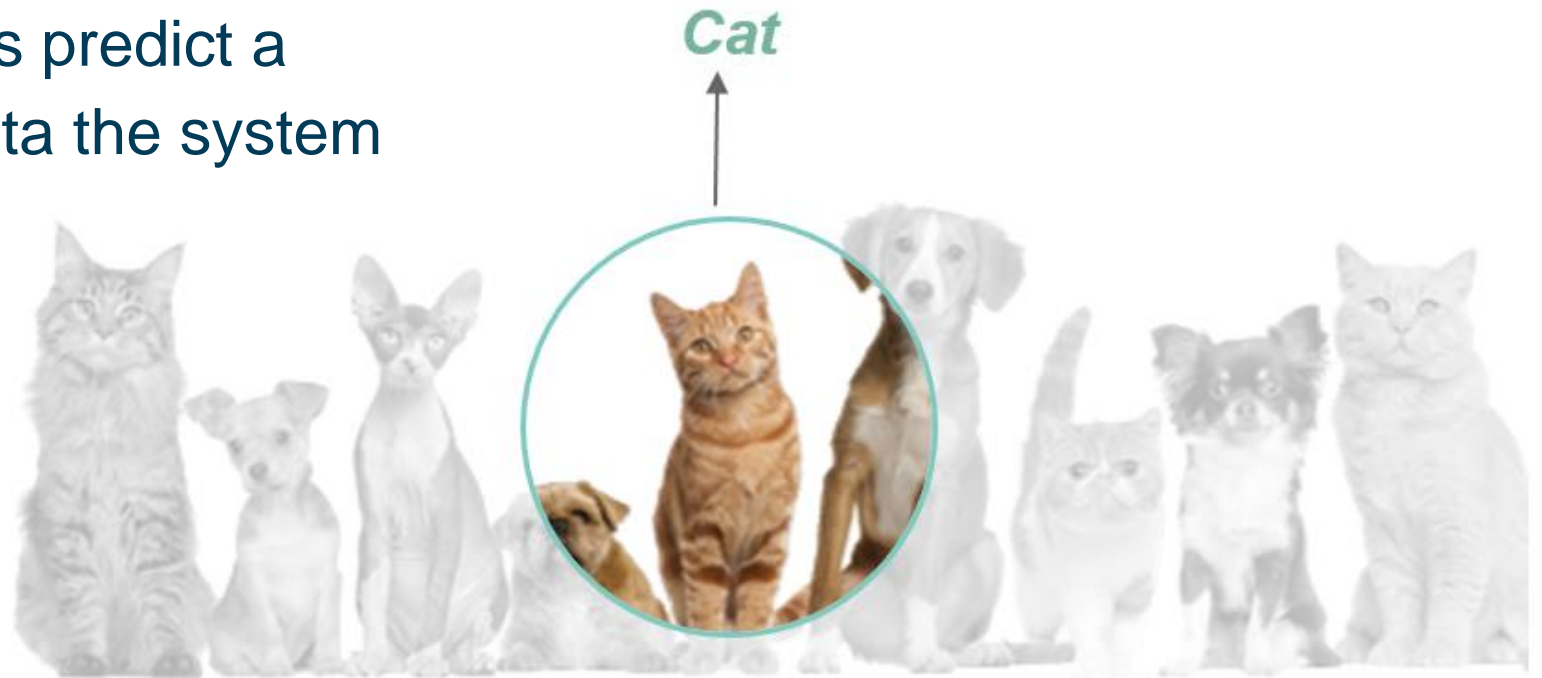
Machine Learning – What's it good at?
Prediction

ML can help us predict outcomes,
or actions, as with YouTube's
Watch Next.
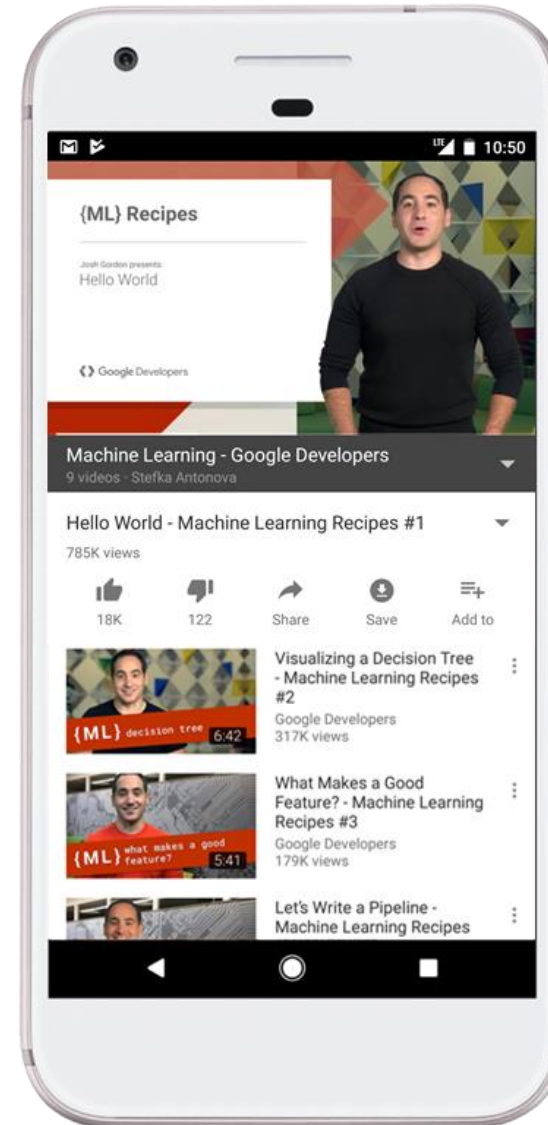
Machine Learning – What's it good at?
Generation

Machine learning can help us create entirely new outputs.
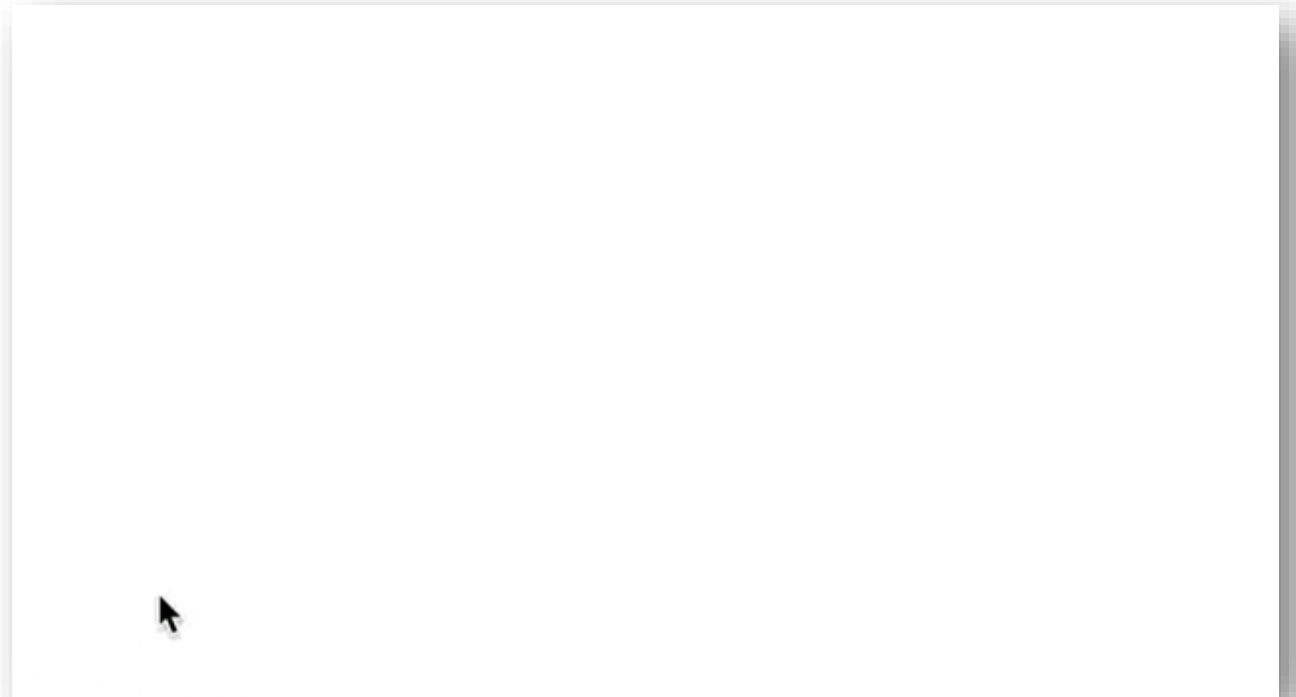
Machine Learning – What's it good at?
Understanding

Machine learning is key to making computers comprehend speech and language.
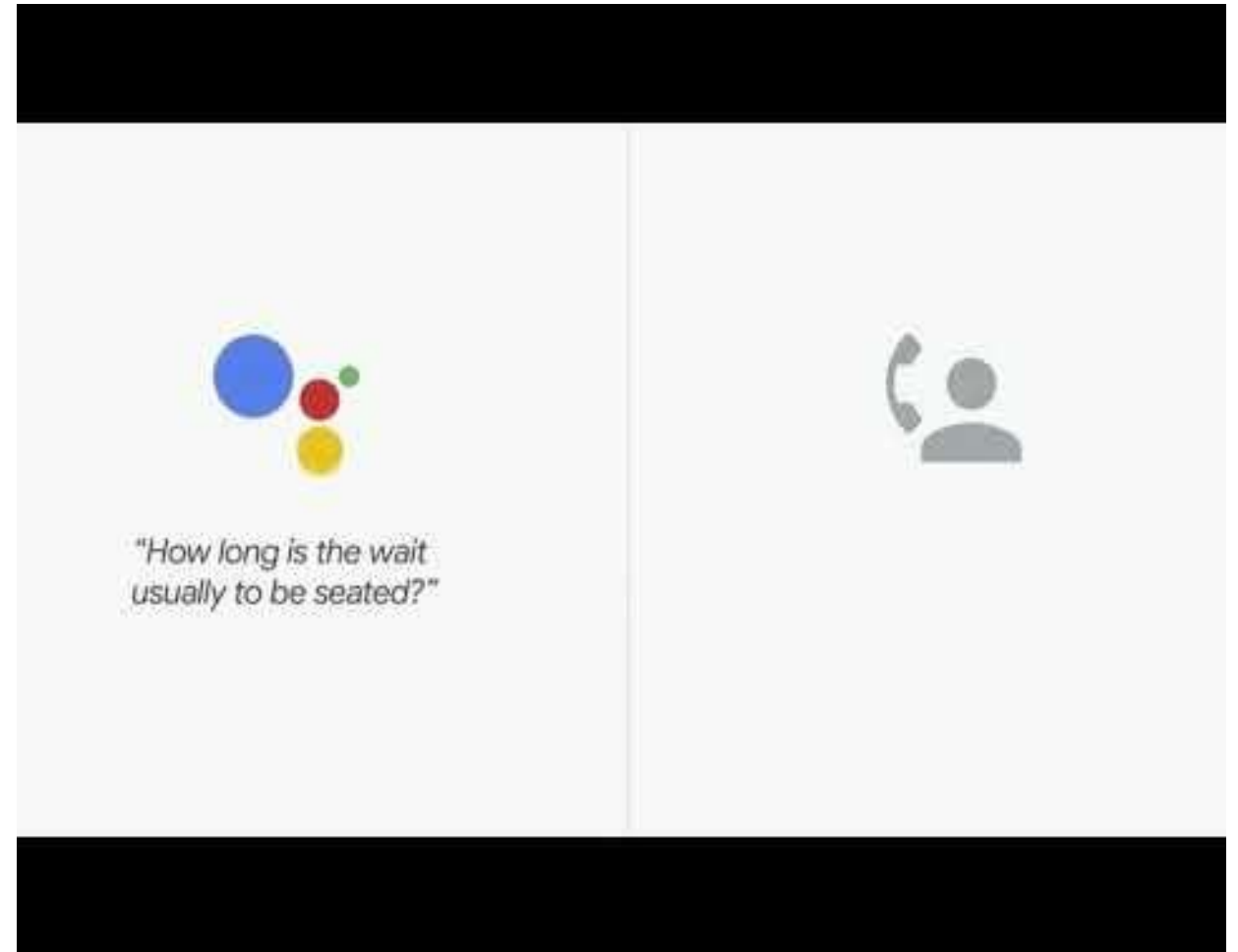
Regulated advice

What is advice?

- A recommendation of what the customer should do, e.g. to buy or sell a particular investment
- Personal to the customer
- Based on their specific circumstances and financial objectives
- Only authorised firms can provide this kind of advice

The advice gap	Advice models	The promise of AI

The advice gap

- The average advised customer has over £150,000 of assets under advice

- Of UK adults with £10,000+ of investible assets:

    - **54%** (around **8.4 million people**) did not receive any formal support to help them make investment decisions over the 12 months to December 2020

    - **37%** did not have any investments at all and were holding their assets entirely in cash

    - A further **18%** were holding more than 75% of their investible assets in cash
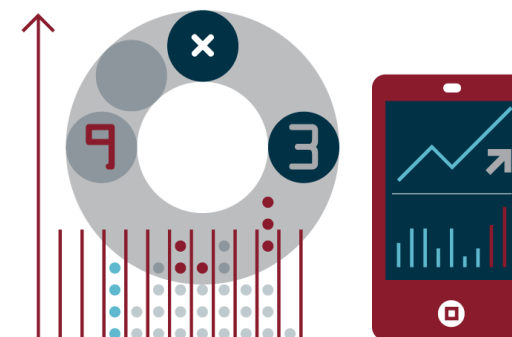
"*Many consumers do not seek, or receive, the sort of help with their finances that would equip them to make better investment decisions*"

FCA, Evaluation of the impact of the Retail Distribution Review and the Financial Advice Market Review, December 2020

Advice models

- Traditional, holistic advice

- The fully automated future / hybrid models / tools to bring efficiencies

- Information and guidance / advice

- Established players / new entrants to the market

- Standalone advice / link to other services

The promise of AI

Low cost

Reduce mis-selling

Audit trail

Fast and convenient

Free from bias

The regulator's historic approach

Financial Advice Market Review

The Advice Unit

Financial Advice Market Review (FAMR)

- Launched in August 2015 – jointly led by HM Treasury and the FCA

- Explored steps government, industry and regulators could take towards a market that provides affordable, accessible financial advice / guidance to everyone

- Final report published 14 March 2016

- Included recommendations aimed at:

  - providing affordable advice to consumers

  - increasing the accessibility of advice

"*While many consumers will continue to seek face-to-face advice, technology-based models are poised for growth. FAMR wants to support the development of mass market automated advice models that have the potential to bridge the advice gap*"

HM Treasury, Financial Advice Market Review, March 2016

The Advice Unit

FAMR Recommendation 9

The FCA should build on the success of Project Innovate and establish an Advice Unit to help firms develop their automated advice models

- Provides regulatory feedback and support to firms developing automated models to deliver lower cost advice and guidance to consumers

- Aims to reduce the level of regulatory uncertainty

- June 2017: expansion to mortgage, general insurance and debt sectors

- Plus to firms not intending to seek authorisation

Taking stock: not there yet?

Demand-side barriers

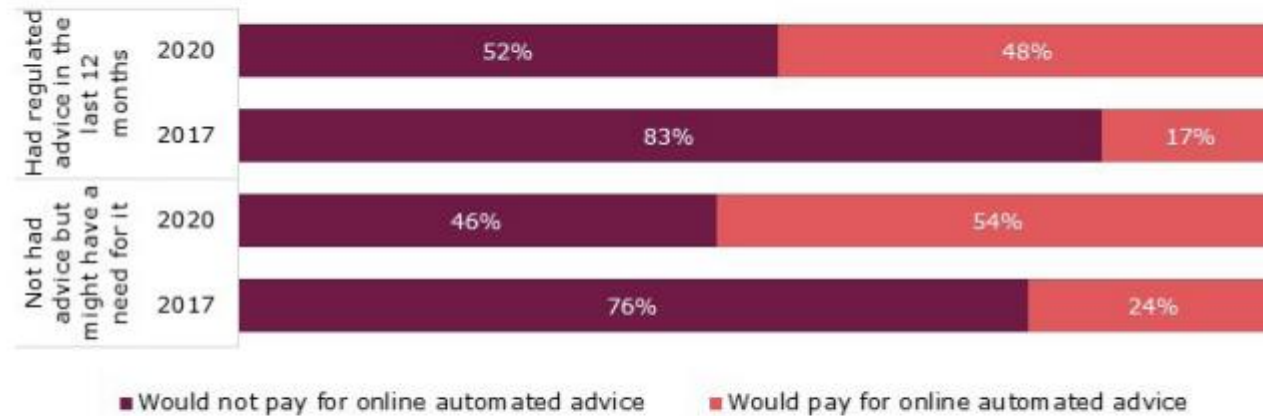Supply-side barriers

Accelerants of change

Demand-side barriers

- Robo-refusers

- Willingness to pay

- Wariness about using unfamiliar brands

- Basic trust in financial institutions

- The human touch

- Generational differences

"… robo advice has a way to go before it is embraced by the majority of consumers"

FCA Insight, Robo Advice – will consumers get with the programme?, 28 November 2019

Demand-side barriers

Figure 3.3: proportion who would not be willing to pay for automated online investment advice in the foreseeable future

		Would not pay for online automated advice	Would pay for online automated advice
Had regulated advice in the last 12 months	2020	52%	48%
	2017	83%	17%
Not had advice but might have a need for it	2020	46%	54%
	2017	76%	24%

■ Would not pay for online automated advice   ■ Would pay for online automated advice

Source: Financial Lives Survey

Base: All UK adults who have received regulated advice in the last 12 months, but not from an automated advice provider (2017: 652/ 2020: 1,328; All UK adults who have not had advice but might have a need for it (2017: 1,213/ 2020: 2,009)

FCA, Evaluation of the impact of the Retail Distribution Review and the Financial Advice Market Review, December 2020

Supply-side barriers

- Technological development

- Lack of competitive pressure

- Profitability

- Regulatory framework

"*Advice firms appear to face little competitive pressure to innovate and offer new, more affordable services, or to try to attract less wealthy consumers. Competition does not appear to be operating effectively in the interests of consumers*"

FCA, Evaluation of the impact of the Retail Distribution Review and the Financial Advice Market Review, December 2020

Accelerants of change

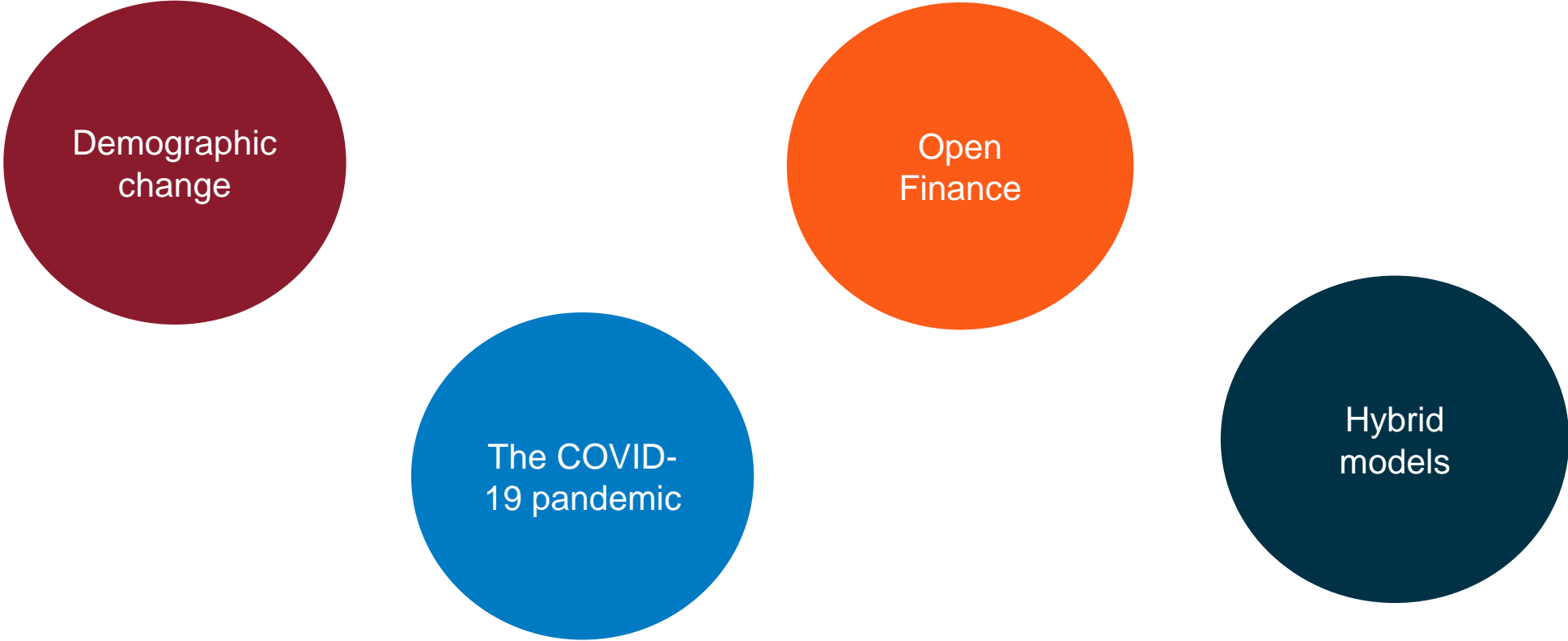**Demographic change**

The COVID-19 pandemic

Open Finance

Hybrid models

Looking ahead: regulatory pressure points

The technology-neutral approach

Governance and accountability

The customer relationship

Operational resilience

The technology-neutral approach

"the position of AI under the existing regulations should be considered further… There should be specific guidance about the application of the PRA and FCA rules. There is a lack of clarity over how the existing rules should be applied in the context of AI"

Kalifa Review of UK Fintech, 26 February 2021

- No separate regime

- Flexibility for the regulator

- Regulatory risk and innovation

- The consumer protection objective

Governance and accountability

- Senior Manager responsibility (SMCR)

- Appropriate oversight

- Management information (MI)

- Risks specific to AI advice

"*There appeared to be confusion within some firms as to the nature of the auto advice service being provided*"

FCA Multi-firm review, Automated investment services – our expectations, 21 May 2018

The customer relationship

- "Explainability" and customer understanding

- Service disclosures and financial promotions

- Vulnerable customers

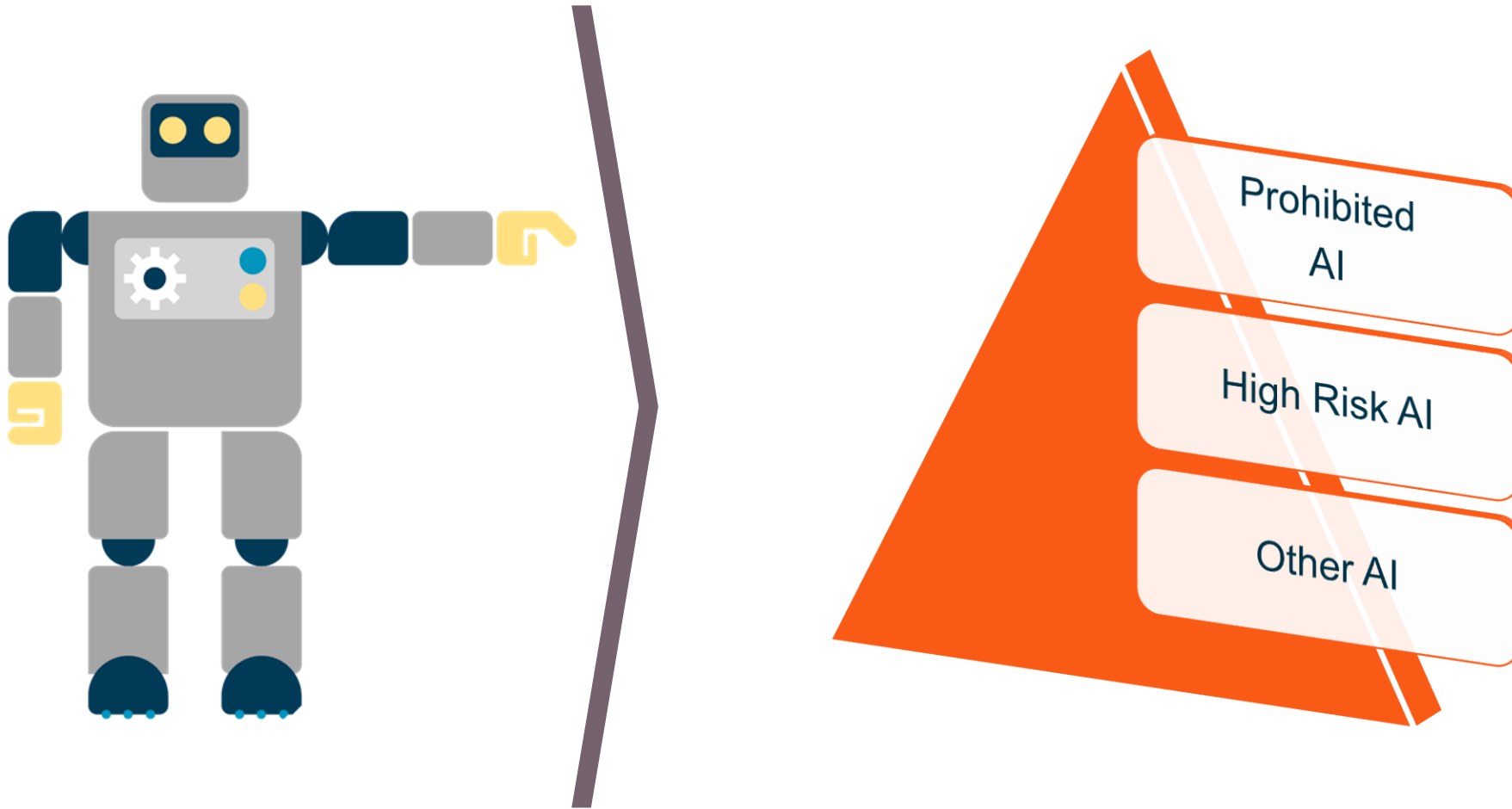- Information-gathering for suitability assessments
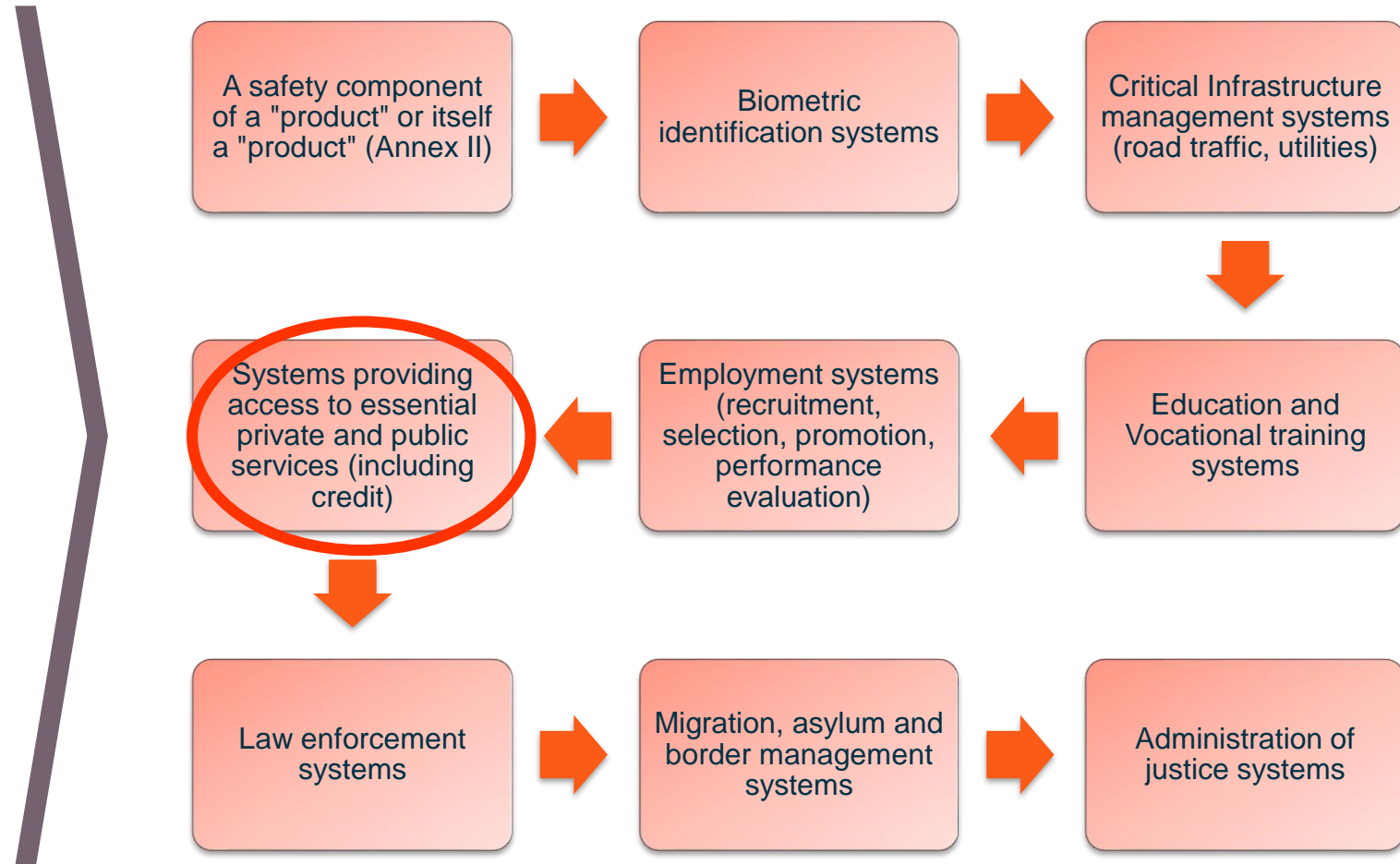
Operational resilience

- Outsourcing and third-party dependency

- Business continuity

- Cyber-security

Looking ahead: The EU AI Regulation

Prohibited AI

High Risk AI

Other AI

High Risk AI - Categories

A safety component of a "product" or itself a "product" (Annex II)

Biometric identification systems

Critical Infrastructure management systems (road traffic, utilities)

Systems providing access to essential private and public services (including credit)

Employment systems (recruitment, selection, promotion, performance evaluation)

Education and Vocational training systems

Law enforcement systems

Migration, asylum and border management systems

Administration of justice systems

High Risk AI – Compliance (Providers)

Lifecycle Risk Management and Quality management

Testing and Conformity assessments

Data Governance

Logging by design (record keeping)

Transparency

Human oversight

Accuracy & robustness

Enforcement & Penalties

Proactive market surveillance (link to EU product safety and compliance legislation)

Full access to system data and documentation (including APIs, training datasets and source code)

Withdrawal from EU market or corrective action within specified periods if non-compliance identified

Prohibitions from use if no corrective actions taken within time limits

Fines: up to €30m or 6% of worldwide turnover – for use of prohibited AI and failing to meet data quality standards

Fines: up to €20m or 4% of worldwide turnover (for any other breaches)

Fines: upto €10m or 2% of worldwide turnover (if a company) for the supply of misleading information

Any questions?

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client-centred approach

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