

Robo Advice and Artificial Intelligence – What is it and what does it mean for your firm?

Who is affected?

Robo advice has the potential to affect all financial services firms as it seeks to provide traditional investment and financial services, both regulated (such as advice) and unregulated (such as guidance), cheaper and quicker than traditional firms. It essentially replaces human interaction and decision-making processes with algorithms.

Summary

With improvements to technology and in particular artificial intelligence, the FCA has had to consider ways in which to regulate these activities – the so called ‘robo advice’. Algorithmic trading has been common place for some time but having a ‘robo advisor’ provide real-time and actionable financial advice has not. The FCA appreciates that artificial intelligence will help customers access affordable advice or guidance but this is not without its challenges. The FCA has considered these challenges as part of its Financial Advice Market Review (FAMR), with a full policy statement expected in December 2017, after consultation. The FCA has also created the Advice Unit to support innovation in this area.

What are the opportunities and challenges?

In many respects, the opportunities cause the challenges. For example, one of the opportunities of artificial intelligence is the reduced overhead cost of staff conducting routine tasks, such as collecting investment information and risk profiling. However, this leads to job losses and in many instances, investors prefer human interaction, clear decision making processes and good customer service.

Some of the opportunities can be grouped as follows:

- (1) Low cost alternative to traditional services (particularly where they are routine tasks);
- (2) On the basis that the advice/guidance provided is based on algorithms, customers will have access to the services 24/7. This increases accessibility for the ordinary customer and allows them to take greater control;
- (3) The FCA is in favour of increasing access to appropriate and affordable advice/guidance and is actively considering how to regulate these services, as can be seen from its FAMR;

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- (4) It could be argued that it removes human biases and will provide consistent advice/guidance based on algorithms from the information disclosed.

Some of the challenges can be grouped as follows:

- (1) Artificial intelligence will lead to job losses and eliminate human interaction. Take the following example: a parent wants to leave their offspring money in the most cost efficient way e.g. by reducing inheritance tax. An automated service may simply tell you to start transferring money to them. However, with a bit of investigation, an advisor may have uncovered that the offspring is irresponsible with money; in such instances the advice would be different;¹
- (2) How do you draw the line between advice and guidance? One is a regulated activity, one is not. Any robo advice must be careful not to stray from guidance to advice if the service provider is not regulated to do so;
- (3) In terms of risk profiling, if a question uses complex language or assumes a basic level of financial knowledge which causes the customer to provide incorrect answers, the algorithm will provide the wrong advice/guidance. In contrast, a financial advisor may have corrected any misinterpretation or provided further guidance to extract the most appropriate answer.

What should you be considering?

If you wish to use artificial intelligence, then you should:

- (1) Determine whether the outcome of the robo advice is actually advice, as this is a regulated activity. It cannot be provided without regulatory permission. Regulated advice is covered by the compensation scheme;
- (2) Ensure that during the fact finding process, any questions used to extract information from the customer are done in layman's terms so as to avoid incorrect answers or misinterpretation;
- (3) Consider using artificial intelligence for a limited purpose. For example, not all customers (especially in these early stages) are comfortable receiving advice in this way and with no face-to-face/advisor contact. Just because the end advice is provided by an advisor, does not mean artificial intelligence cannot be utilised.

Timeline

The next event in this area will be the end of the FAMR consultation period. The FCA will publish their full policy statement in respect of streamlined advice services (which robo advice is captured by).

¹ <http://citywire.co.uk/new-model-adviser/news/fca-hands-advantage-to-human-advice-with-robo-risk-warning/a1009800>

How we can help?

Lawson Conner has worked extensively with its clients to assess the impact of regulatory change. We would be delighted to discuss how we can help support your organisation to meet these new regulatory challenges. Lawson Conner’s team of compliance professionals can assist you at every stage as you seek to comply with the new regime.

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