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Compliance as Business Development Potential in the Credit Institution Sector*

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Regulatory compliance, often perceived as a burden by organisations, offers untapped opportunities for business development. By adopting, implementing and improving relevant standards and good practices, companies can increase stakeholder confidence, improve organisational reputation and reduce the legal, financial, business and reputational risks arising from various non-compliances. Drawing on literature research, the paper shows that compliance with regulations typically fosters an internal organisational environment and culture where innovation, excellence and sustainable growth can be created. Complex compliance management activities can help identify market opportunities, stimulate product development and improve customer experience. Compliance and innovation are compatible approaches that support long-term success.

Journal of Economic Literature (JEL) codes: G28, G32

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1. Introduction

In the past decade, several international and Hungarian studies were published (*Benedek 2014; Doyle et al. 2014; Ambrus – Farkas 2019; Braun 2019; Jacsó 2020; Kocziszky – Kardkovács 2020*), which link the concepts of compliance management, risk management and innovation and help companies to understand them, creating effective cooperation between these areas. The English-language content is typically based on the rules of the United States and England, and the Anglo-Saxon regulatory and business environment. The use of resources should therefore be geared towards

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the transposition of experience in line with Hungarian and EU standards, and the careful adaptation of international approaches and best practices.

Ensuring that companies operate in compliance with the laws is not only a social and economic imperative, but also in the public interest. At the same time, the operation of a company is threatened and endangered not only by conduct that is legally prohibited, but also by attitudes that are morally reprehensible. The goal of compliance management goes beyond compliance with the current legal frameworks in force, because compliance with ethical principles is also a key part of it. The question arises as to whether compliance helps or hinders business development and how its objectives can be reconciled with the objectives of business development. Can we confirm that compliance and business development actually serve a common purpose? In practice, the concept of business development is often confused with customer acquisition, and in this paper we will try to clarify and answer these questions.

The structure of the paper is as follows: the second section presents the methodology, followed by an explanation of the theoretical background, including the relevant regulations and risk-based compliance management. We then describe innovation and business development trends, and finish up with a summary of the results and recommendations, as well as the conclusions.

2. Methodology

Drawing on a range of academic, legal and business sources, this paper seeks to describe, compare, analyse and combine the existing knowledge and insights on the subject. In light of the interdisciplinary nature of the topic, it is also appropriate to explore the literature in related disciplines. Relevant scientific publications, books and online sources were selected and analysed according to a systematic procedure. In addition to the description of the relevant regulations and international standards, we selected the relevant scientific publications, primarily using the Scopus digital database. The keywords in the search were compliance management, innovation, risk management and business development. The search was extended to include reports and documents published by business development consulting companies. This approach not only provides a theoretical basis, but also includes practical business experiences and perspectives. Our goal is to provide business resources with practical guidance for companies to select and apply best practices and solutions.

3. Theoretical background

The simplified, narrowly defined concept of compliance means observing and complying with the rules and following the letter (and not necessarily the spirit) of the laws and rules. Compliance in a broader sense also includes more complex requirements. The aim should be to ensure that the operation of organisations is not only profitable in the short term, but also sustainable in the long term. This requires that abuses in the context of company operations, legally prohibited acts (e.g. fraud, embezzlement, misuse, money laundering, corruption) and behaviours that violate ethical standards (e.g. religious mockery, defamation) are detected, investigated and, if possible, prevented (*Ambrus 2020*).

Compliance management is the set of processes that aim to guarantee "regular, effective and efficient operation and the achievement of reliable reporting" (*Benedek 2019a:17*). A compliance department defines the framework of the operation, based on legal requirements and moral and ethical principles, and supports the achievement of the company's objectives by ensuring compliance with the framework and by providing the necessary and proportionate sanctions for overstepping the boundaries of the framework. The expectation today is more of an organisation-wide compliance awareness and culture, which has many elements. This includes, among other things, the commitment to compliance on the part of both top management and employees, the creation of company-level compliance documents (organisational and operating policies, conflict of interest regulations, code of conduct, data protection regulations, whistleblowing policy, etc.), the establishment of processes for the application and enforcement of standards, the integration and operation of compliance checks, continuous monitoring, correction and improvement of the system (*Ambrus 2020; Törcsváry 2023*).

3.1. Significant regulations in the area of financial compliance

The first legislative steps on corporate compliance were taken in the United States of America. Financial scandals in the corporate sector have undermined investor confidence in the credibility of financial reporting. As it later turned out, the cases of fraud that came to light in the early 2000s (e.g. Enron, Tyco, Worldcom) were made possible by the contingencies of internal controls, shortcomings in corporate governance and the intertwining of auditors and company management. The realisation that corporate governance problems could also threaten the stability of the national economy prompted the US Congress to adopt the Sarbanes-Oxley Act (SOX) in 2002. The law was primarily aimed at strengthening accounting discipline for publicly listed companies to which it applied. It made it mandatory for the CEO and CFO to deposit a statement audited by an independent auditor together with

the annual balance sheet declaring, aware of their legal and financial responsibility, that the company's internal financial control system had been audited and that the procedures used during the audit worked effectively (*Liber 2009*).

The development of corporate compliance in the US has both a direct and an indirect impact on the daily lives of European companies. In the case of the US Foreign Corrupt Practices Act (FCPA) and SOX compliance processes of business partners subject to the FCPA/SOX Act, Hungarian companies may also be affected (*Ambrus – Farkas 2019*). The provisions introduced by SOX and subsequently transposed into the legislation of European countries and the European Union are based on the recognition that "in the corporate sector, the disclosure of not only business results but also of misconduct and failures enhances overall business confidence" (*Benedek 2019a:18*).

Compliance first came to the fore in the banking sector – not coincidentally, as the first significant framework regulations were introduced in this area. In 2004, Directive 2004/39/EC of the European Parliament and of the Council on Markets in Financial Instruments,[1] known as the Markets in Financial Instruments Directive (MiFID I), was adopted with the aim of regulating the financial markets in the region, increasing transparency and protecting investors, as well as establishing compliance as a mandatory function. MiFID focused on stock exchanges, and thus the transparency of OTC transactions remained low. It also placed the regulation of third countries and their institutions under the jurisdiction of Member States, creating inequalities in the regulatory environment that were difficult to accept. The recognition of these shortcomings, together with the financial meltdown caused by the 2008 economic crisis and practical experience, made it necessary to review the regulation. Directive 2014/65/EU of the European Parliament and the Council[2] (MiFID II), adopted in 2014 and applicable from 3 January 2018, and its companion rules, including Regulation (EU) No 600/2014/EU[3] (Markets in Financial Instruments Regulation, MiFIR), aim to create a single financial market. The common regulatory requirements are defined for authorisation, operating conditions, the operation of data providers and oversight by the authorities to ensure that investors are adequately protected. The scope of these legal acts also extends to third-country companies providing investment services in the EU. The MiFIR's trading and

[1] *Directive 2004/39/EC of the European Parliament and of the Council of 21 April 2004 on Markets in Financial Instruments amending Council Directives 85/611/EEC and 93/6/EEC and Directive 2000/12/EC of the European Parliament and of the Council and repealing Council Directive 93/22/EEC*. OJ L 145, 30.04.2004, pp. 1–44. http://data.europa.eu/eli/dir/2004/39/oj (Repealed from 2 January 2018).

[2] *Directive 2014/65/EU of the European Parliament and of the Council of 15 May 2014 on Markets in Financial Instruments and amending Directives 2002/92/EC and 2011/61/EU (recast) (recast) Text with EEA relevance*. OJ L 173, 12.06.2014, pp. 349–496. Amended text in force from 28 March 2024. http://data.europa.eu/eli/dir/2014/65/oj.

[3] *Regulation (EU) No 600/2014 of the European Parliament and of the Council of 15 May 2014 on Markets in Financial Instruments and amending Regulation (EU) No 648/2012 Text with EEA relevance*. OJ L 173, 12.06.2014, pp. 84–148. Amended text in force from 28 March 2024. http://data.europa.eu/eli/reg/2014/600/oj.

regulatory transparency requirements are directly applicable to all investment companies operating in the EU by virtue of the form of the Regulation.[4] In Hungary, Act CXXXVIII of 2007 on Investment Enterprises and Commodity Exchange Service Providers[5] (hereinafter: 'Bszt.') was amended to incorporate the innovations introduced by MiFID II into domestic law. Financial supervision regulations have also necessarily changed.

In 2013, Recommendation No 6/2013 (III.11.) of the President of the Hungarian Financial Supervisory Authority (HFSA)[6] provided guidance on the establishment and operation of internal lines of defence and the implementation of governance and control functions of financial institutions, and included expectations regarding the compliance function. With the merger of HFSA, the Magyar Nemzeti Bank (the central bank of Hungary, MNB) revised and published its Recommendation No 5/2016 (VI. 6.) on the establishment and operation of internal lines of defence, and the governance and control functions of financial institutions.[7] Further changes were brought about by the 'Best Practice Code' published by the Hungarian Banking Association[8] and Recommendation No 27/2018 (XII.10.) of the Magyar Nemzeti Bank,[9] which provides guidance for credit institutions on the practical operation of the compliance management system. The summary material aimed to help with the identification and effective management of legal violations and compliance risks (*Dénesné Orcsik 2023*), and both the Banking Association and the MNB advocate for the establishment of a compliance function in order to strengthen the legal awareness and voluntary compliance of financial institution employees. The aim

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[4] Fenyvesi, R. (2015): *A pénzügyi eszközök piacairól szóló szabályozásban várható változások (a MiFID I és MiFID II közötti főbb változások és a MiFIR tartalmi elemei)* [*Expected changes in the Markets in Financial Instruments regulation (main changes between MiFID I and MiFID II and the content of MiFIR)*]. https://www.mnb.hu/sajtoszoba/sajtokozlemenyek/2015-evi-sajtokozlemenyek/fenyvesi-reka-a-penzugyi-eszkozok-piacairol-szolo-szabalyozasban-varhato-valtozasok-a-mifid-i-es-mifid-ii-kozotti-fobb-valtozasok-es-a-mifir-tartalmi-elemei. Downloaded: 6 June 2024.

[5] *2007. évi CXXXVIII. törvény a befektetési vállalkozásokról és az árutőzsdei szolgáltatókról, valamint az általuk végezhető tevékenységek szabályairól* (*Act CXXXVIII of 2007 on Investment Enterprises and Commodity Exchange Service Providers, and the Rules Governing their Activities*). https://net.jogtar.hu/jogszabaly?docid=a0700138.tv.

[6] *A Pénzügyi Szervezetek Állami Felügyelete elnökének 6/2013. (III. 11.) számú ajánlása a belső védelmi vonalak kialakításáról és működtetéséről, a pénzügyi szervezetek irányítási és kontroll funkcióiról* (*Recommendation No 6/2013 (III.11.) of the President of the Hungarian Financial Supervisory Authority on the establishment and operation of internal lines of defence, and the governance and control functions of financial institutions*). https://www.mnb.hu/letoltes/2013-iii-11. Downloaded: 18 March 2024.

[7] MNB (2016): A *Magyar Nemzeti Bank 5/2016. (VI.06.) számú ajánlása a belső védelmi vonalak kialakításáról és működtetéséről, a pénzügyi szer-vezetek irányítási és kontroll funkcióiról* (*Recommendation No 5/2016 (VI.06.) of the Magyar Nemzeti Bank on the establishment and operation of internal lines of defence, and the governance and control functions of financial institutions*). https://www.mnb.hu/letoltes/5-2016-belso-vedelmi-vonalak-kialak-es-muk.pdf. Downloaded: 7 August 2024.

[8] *A compliance (megfelelőség biztosítási) funkció működtetésének legjobb gyakorlata* (*Best Practice Kódex*) [*Best practice in the operation of the compliance function (Best Practice Code)*]. https://www.bankszovetseg.hu/Content/alapdokumentumok/Compliance_Best_Practice_Kpdex_HUN_ENG.pdf. Downloaded: 18 March 2024.

[9] *A Magyar Nemzeti Bank 27/2018. (XII.10.) számú ajánlása a belső védelmi vonalak kialakításáról és működtetéséről, a pénzügyi szervezetek irányítási és kontroll funkcióiról* (*Recommendation No 27/2018 (VI.10.) of the Magyar Nemzeti Bank on the establishment and operation of internal lines of defence, and the governance and control functions of financial institutions*). https://www.mnb.hu/letoltes/27-2018-belso-vedelmi-vonalak.pdf. Downloaded: 18 March 2024.

is therefore to ensure that employees not only comply with legal requirements for fear of supervisory control, but also that they develop a natural desire for moral and ethical behaviour, and that compliance awareness and culture permeate the entire organisation and its ethos (*Ambrus 2020*).

Subsequently, the introduction of the compliance system was also regulated at the legislative level in Act CCXXXVII of 2013 on Credit Institutions and Financial Enterprises[10] (hereinafter: 'Hpt.'), which entered into force on 1 January 2018. All organisations subject to Hpt. are required to have in place an independent compliance function, i.e. a compliance management system.

The next milestone was the MNB's Recommendation No 12/2022 (VIII.11) on the establishment and operation of internal lines of defence, governance and control functions of financial institutions[11] (hereinafter: 'MNB Recommendation'). The MNB Recommendation is a means of transposing a non-binding legal instrument, which at the same time serves as a means of transposing the guidelines and recommendations of the European Supervisory Authorities (European Banking Authority – EBA, European Securities and Markets Authority – ESMA, European Insurance and Occupational Pensions Authority – EIOPA, European Systemic Risk Board – ESRB). The purpose of the Recommendation is to increase the predictability of the application of the law, to promote the uniform application of the relevant EU and domestic legislation and to present the principles and methods proposed by the MNB. The recommendation requires financial institutions to establish and maintain internal lines of defence that, in respect of the organisation in question, support:

- its operation in a reliable, prudent and efficient manner, in accordance with legislation and internal rules;
- the protection of its assets, its social function and of the economic interests of its owners and customers; and
- the full maintenance of confidence in the financial organisation and its control functions.

Three lines of defence can be distinguished and it is essential that there is a clear separation between the different control functions, including their respective roles and levels of responsibility. The first line of defence is management controls integrated into the process, followed by controls focusing on risk identification and

[10] *2013. évi CCXXXVII. törvény a hitelintézetekről és a pénzügyi vállalkozásokról* (*Act CCXXXVII of 2013 on Credit Institutions and Financial Enterprises*). https://net.jogtar.hu/jogszabaly?docid=a1300237.tv

[11] *A Magyar Nemzeti Bank 12/2022. (VIII.11.) számú ajánlása a belső védelmi vonalak kialakításáról és működtetéséről, a pénzügyi szervezetek irányítási és kontroll funkcióiról* (*Recommendation No 12/2022 (VI.11.) of the Magyar Nemzeti Bank on the establishment and operation of internal lines of defence, and the governance and control functions of financial institutions*). https://www.mnb.hu/letoltes/12-2022-belso-vedelmi-vonalak-ajanlas.pdf. Downloaded: 18 March 2024.

assessment, including the compliance function. The third is internal control, which also serves to control the first two lines of defence (*Dénesné Orcsik 2023; IIA 2020*).

Compliance management has a prominent role in the financial sector, as credit institutions are in direct contact with their customers' financial assets and the financial market. The activities of financial institutions entail significant risks, for example in the areas of anti-money laundering and counter terrorism financing, market manipulation, data protection and data security (*Stevens et al. 2020*). The risks can have serious legal and reputational consequences for customers and the financial world. Compliance management helps financial organisations to ensure that all aspects of their activities comply with the applicable laws and regulations.

In summary, the first major regulatory milestone in corporate compliance in the United States was the Sarbanes-Oxley Act of 2002, which came in response to major financial scandals. The SOX Act aimed to strengthen accounting discipline and internal controls by requiring CEOs and CFOs to certify the accuracy of financial reports. This legislation had a major impact on global corporate compliance and prompted European countries to adopt similar measures for transparency and investor protection. For example, MiFID I of 2004 was designed to regulate financial markets and protect investors in the EU. It was later revised by MiFID II and MiFIR to address the deficiencies and improve consistency in the financial sector. As a result of the EU level regulations, several laws affecting financial institutions and credit institutions in Hungary were amended and recommendations were prepared to present good practices (MNB Recommendation, Banking Association Best Practice). The continued development of compliance regulations underlines their importance in promoting ethical behaviour, preserving financial stability and strengthening public confidence in financial systems.

3.2. Compliance risk management

In general, risk management aims to proactively mitigate potential threats and minimise damage from adverse events. A risk is the occurrence of an adverse event that is accidental, that threatens to cause us danger or harm, or the damage caused when it occurs. Risk management includes the activities and preventive measures that aim to reduce the likelihood of a threatening event occurring or mitigating the severity of the impact (*Jenei 2016*). A risk management strategy is a structured approach to managing risks, risk exposures and risk events applicable to any industry.

Compliance risk is the risk to an organisation's business, financial results and reputation arising from a breach of laws, regulations or internal rules and policies. A risk event may be non-compliance with industry-specific laws and regulations, such as those applicable to credit institutions, or breaches of internal rules and policies. Assessing compliance risks is of crucial importance for banks and other

financial institutions. These risks may arise from the activities, business model and regulatory environment of the credit institutions concerned. Within the banking sector, compliance risks arise from possible breaches of legal and ethical standards. Risks in the financial domain can be interpreted mainly in relation to legal, financial, business and reputational environmental impacts (*Benedek 2019b; Jacsó 2019*). Effective risk management includes the systematic identification and assessment of these risks, the application of prioritisation methods and the development of appropriate mitigation strategies (*Esayas et al. 2015*). The methods generally focus on assessing the severity and probability of risk and analysing the effectiveness of preventive measures. In addition, it is also important to identify risks in time and take appropriate measures to reduce them. Credit institutions can strengthen their resilience and protect themselves against the risks inherent in their operating environment by applying robust risk management frameworks.

Risk management tools include a range of methods and frameworks designed to effectively identify, assess and mitigate risks:

1. Risk assessment methods help to identify and assess different risks, including the severity and probability of risks. These include risk maps or matrices, PRIZMA maps, SWOT analysis, risk indices, risk assessment questionnaires and statistical models (*Bognár et al. 2023*).

2. A risk management plan is a document that sets out the risks, the related measures and responsibilities. It helps organisations to manage risks in a structured and traceable way.

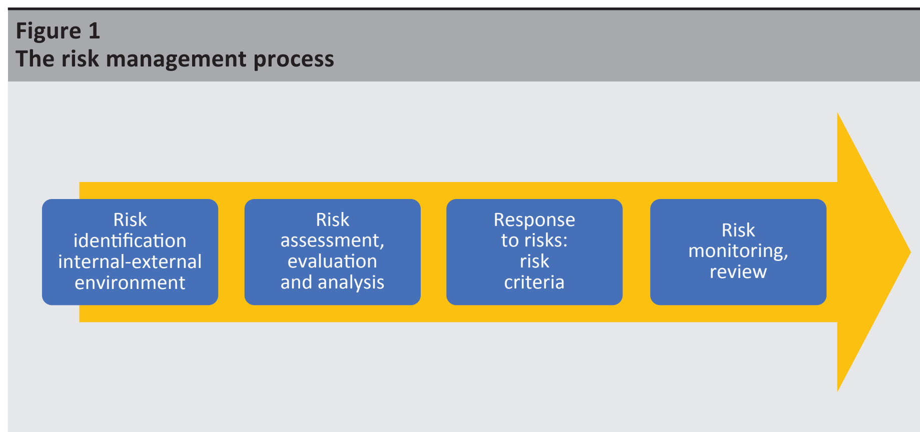
3. Early warning systems are crucial for identification and indication of potential risks and problems in due time. These include automated monitoring systems, event logging, monitoring systems and regular reports.

The development of robust risk management practices is a legal obligation and is particularly important for credit institutions, given the financial risks associated with their operations. However, individual risks are highly dependent on factors such as the business model of the organisation, market environment and customer behaviour. Credit institutions and financial enterprises need to have complex risk management strategies in place to maintain their economic stability and reputation and to comply with legislative requirements. Appropriately developed and effective risk management models and systems can contribute to this (*Mishchenko et al. 2021*).

Effective risk management is not simply compliance with legislation and a series of development steps, but an iterative process characterised by the continuous identification, assessment, management and monitoring of emerging and ongoing

risks (*Homolya 2012*). The risk management process is illustrated in *Figure 1.* This process allows assessments to be updated and reviewed when new, unexpected events occur (e.g. fraud, abuse), so that timely action can be taken to protect persons and assets.

Figure 1
The risk management process



The role of risk management within an organisation's compliance system is defined by frameworks such as the Three Lines Model (*IIA 2020*) of the International Organization of Internal Auditors (IIA), which was revised and updated in 2020. This model places compliance management in the first and second line. In this context, monitoring and control tasks serve as the oversight function. The second line of defence includes risk management and the third line of defence is the internal control function. According to the 2022 MNB recommendation,[12] the implementation of responsible internal governance is ensured through an appropriate organisational structure, the establishment and operation of an appropriate board system, and the exercise of management and supervision functions. The MNB recommendation underlines the importance of a well-defined governance framework.

Compliance risk management within domestic credit institutions is divided between the governance and supervisory functions, in line with the three lines model, embodying the dual function. In this, risk management acts as an operational first line of defence and an individual second line of defence. Internal control systems within credit institutions, are primarily designed to combat money laundering and terrorism financing, prevent market abuse, outline financial and investment services, mitigate fraud risks and protect personal data.

[12] See footnote 9.

Risk management can strengthen and facilitate predictable operations from several perspectives. Risk management processes promote advance planning and preparation for unexpected events and uncertain situations. Risk management must also respond to technological changes.[13] Regular risk assessments and updates help organisations monitor and manage risks, thereby increasing organisational resilience. Finally, risk management processes provide transparency to organisations, stakeholders and markets, which promotes market confidence and stability in operations (*Arellano-Gault – Del Castillo 2023*).

Like companies in all kinds of industries, the operation of credit institutions is subject to a number of standards approved by the International Organization for Standardization (ISO). Among the standards, the ISO 37001:2018 standard on anti-corruption management systems and the ISO 37301:2021 standard on compliance management systems are worth highlighting. (The latter is a further improvement of the 2014 ISO 19600:2014 recommendation on the establishment and operation of a compliance management system.) Both standards require a risk-based approach and both follow the four-step Plan-Do-Check-Act (PDCA) process development cycle. The PDCA model, which is an improved version of the 'Shewhart learning and development cycle' associated with Deming, supports organisations in improving their performance through standardisation (*Demeter et al. 2008*). While ISO 37001 focuses on one aspect, i.e. anti-corruption management, ISO 37301 takes a holistic approach to compliance management. An important part of ISO 37301 is the development of corporate culture and the transfer of ethical and business values into practice. The introduction of ISO 37301 helps to standardise and systematise compliance processes and increase transparency, proportionality and accountability.

Banks and other financial enterprises play an indispensable role in the functioning and operation of economic systems. Large institutions pose an increased risk to the financial system as a whole, as their potential bankruptcy has serious spill-over consequences (*Móra 2019*). Effective risk management in credit institutions contributes to economic stability in several ways. On the one hand, it helps minimise potential losses by proactively preparing for and preventing risk events. In this way, economic systems may mitigate negative impacts. On the other hand, robust risk management promotes a sense of trust and stability within organisations and in the wider market. This increased confidence serves as a defence against panic and market volatility, contributing to market stabilisation efforts. Furthermore, by ensuring compliance with the relevant legislation, organisations enhance their reputation, reduce the probability of sanctions for non-compliance and increase the level of social responsibility in the world of financial markets.

[13] *Staying ahead of change: Real-time compliance management*. https://www.pwc.co.uk/audit-assurance/assets/pdf/2018-state-of-compliance-study.pdf. Downloaded: 18 March 2024.

In summary, the overall aim of risk management is to proactively mitigate potential threats and minimise the damage caused by adverse events. Compliance risk due to non-compliance with laws, regulations or internal policies can jeopardise the business activities, financial results and reputation of financial institutions. Effective risk management for credit institutions includes the identification, assessment and mitigation of these risks. Tools such as risk assessment methods, risk management plans and early warning systems are crucial to the process. The three lines model ensures the continuous identification and mitigation of risks, while following the requirements of the ISO 37001 and ISO 37301 standards increases transparency, which together help financial organisations to comply with the rules and thus facilitate the predictability and stability of the financial system.

4. Innovation and business development trends and challenges

Business development in the most general sense refers to strategies to promote business growth. The toolbox varies from sector to sector, and often from company to company, but the literature distinguishes between business development processes for financial and non-financial organisations. The basis for the distinction is the method of risk assumption. The risk for traditional manufacturing and service provider companies is that they will lose the proceeds of their work in the case of non-performance. By contrast, financial service providers transfer financial assets and therefore also run the risk of not receiving back the assets delivered (*Imreh 2005*).

Business development rests on three pillars: (1) strengthening market position; (2) improving performance; and (3) ensuring future sustainability. The purpose of business development is to assess the current situation and market potential of the business in light of the prevailing environment (social, legal, economic and political conditions), to monitor and respond to changes, to adapt to international trends, to seek new business opportunities and to develop services, products and processes in a manner that ensures the business is successful in a continuous and sustainable way. For credit institutions, innovation and business development are key factors in maintaining and increasing competitiveness. Business development is framed by a dynamically changing regulatory and technological environment (*Doyle et al. 2014*).

The emergence of new technology-based business models (including artificial intelligence, blockchain and extensive data analysis) and the rise of digital financial services both hold enormous business potential and raise new regulatory demands[14] (*Gerlach et al. 2017; Van den Broek – Van Veenstra 2018; Mishchenko et al. 2021*).

[14] *Compliance on the forefront: Setting the pace for innovation*. https://www.pwc.ch/en/publications/2019/ch-pwc-2019-state-of-compliance-study-final-secured-en.pdf. Downloaded: 18 March 2024.

The introduction of the General Data Protection Regulation (GDPR) and the increasing frequency of cyber-attacks targeting financial market participants also present new security challenges and obligations.

The collection of data, the use of artificial intelligence and the information and knowledge asymmetry between the credit institution and the customer involve a number of ethical issues. The values and ethics of each credit institution influence the operation from product development to product information and investment policy to product sales and customer relations. The compliance management function plays a major role in enforcing ethical principles and encouraging and enforcing ethical behaviour among employees and managers.

Understanding and managing these challenges and trends is crucial for companies to ensure sustainable, successful business operations (*Table 1*).

Table 1
Current challenges and trends affecting the operation of credit institutions

Challenges	Trends
Rapidly changing legislative environment	Electronic system for cooperation with regulatory authorities
Increasing data volume and complexity	Data protection and GDPR
Technological challenges, digitalisation, disruptive technologies and business models	AI and chatbot applications, digital products
Formal and informal Environmental, Social and Governance (ESG) requirements	Responsible lending and investment, community economy (sharing), reporting in line with the UN Sustainable Development Goals (SDGs)

The spread of distributed ledger technology (DLT) and cloud-based services creates new opportunities for credit institutions. Unlike traditional databases, distributed ledgers do not have a central repository or administration function. In the distributed ledger, each node processes and checks all items, thereby registering each item. A shared general ledger can be used to record both static data, such as records, as well as dynamic data, such as financial transactions. One new option is the smart contract, which facilitates the smooth execution and settlement of commercial transactions along with cross-border payments. A smart contract is a self-service computer program that automatically creates a transaction without the involvement of a third party when the conditions for concluding a contract are met. Its use allows for a more flexible management of resources, but it also requires the introduction of appropriate technological improvements and compliance with data protection requirements (*Mishchenko et al. 2021*).

The field of cryptocurrencies, which is widespread, deserves special attention. In decentralised financial systems, new actors and business models have emerged alongside traditional actors such as credit institutions and central financial institutions, to which current traditional financial regulation cannot be effectively applied. The philosophy behind the EU's digital finance strategy is innovation-friendly, with EU legislative initiatives seeking to unlock the potential of new technologies while reducing risks to financial stability and consumer protection (*Pavlidis 2021*).

In 2023, Regulation (EU) 2023/1114 of the European Parliament and of the Council on Markets in Crypto-Assets (MiCA)[15] entered into force, laying the foundations for uniform EU regulation. Regarding the Hungarian implementation of the Regulation, a bill is already before Parliament, according to which the implementation of MiCA and the supervision of Hungarian-based crypto service providers will fall under the MNB's competence after a grace period lasting until 1 July 2026. It is expected that crypto service providers, like other financial service providers, will be able to operate as cross-border service providers in other Member States (subject to registration) if they are licensed in an EU Member State. This means that the host country's central bank (including the MNB) has only limited powers to act; in their case, it can exercise prudential and consumer protection supervision.[16]

Regulation (EU) 2022/2554 on Digital Operational Resilience[17] (Digital Operational Resilience Act, DORA), issued by the European Commission, aims to contribute to increasing the resilience of credit institutions and financial companies to various operational risks and to respond more quickly to them, including cyber threats, IT disruptions and other technology-related risks. Digital technology presents new risks and challenges for operational flexibility (*Grima – Marano 2021*). The European Supervisory Authorities (EBA, EIOPA and ESMA) also published four draft Regulatory Technical Standards (RTS) and one draft Implementing Technical Standard (ITS). These standards are intended to provide a uniform and harmonised legal framework in the field of risk management involving information and communication technologies, major incident reporting and third party risk management. Following DORA, financial enterprises will also be responsible for the compliance of the fintech

[15] *Regulation (EU) No 2023/1114 of the European Parliament and of the Council of 31 May 2023 on Markets in Crypto-Assets, and amending Regulations (EU) No 1093/2010 and (EU) No 1095/2010 and Directives 2013/36/EU and (EU) 2019/1937 (Text with EEA relevance) L 150/40*, 09.06.2023. https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:32023R1114. Downloaded: 6 June 2024.

[16] *Fokozott befektetői kockázattal járhatnak a kriptoeszközök, kriptotőzsdék* (*Crypto-assets and cryptocurrency exchanges may involve increased investor risk*). MNB, press release. https://www.mnb.hu/sajtoszoba/sajtokozlemenyek/2024-evi-sajtokozlemenyek/fokozott-befektetoi-kockazattal-jarhatnak-a-kriptoeszkozok-kriptotozsdek. Downloaded: 18 March 2024.

[17] *Regulation (EU) No 2022/2554 of the European Parliament and of the Council of 14 December 2022 on Digital Operational Resilience in the Financial Sector and amending Regulations (EC) No 1060/2009, (EU) No 648/2012, (EU) No 600/2014, (EU) No 909/2014 and (EU) 2016/1011 (Text with EEA relevance)*. PE/41/2022/INIT. https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX%3A32022R2554

companies that provide them with services. This extended responsibility can have a number of effects on financial innovation. We assume that stricter due diligence and verification procedures will ensure that only robust and safe innovations are implemented. This may initially slow down the pace of financial innovation, but in the long run it is likely to lead to safer, more reliable and sustainable financial innovations, while increasing customer confidence in innovative financial solutions.

Financial technology is undoubtedly the fastest-changing area of financial services, posing significant challenges for market participants, legislators and supervisors. It is revolutionising money flows, credit management, equity markets, regulatory compliance and virtually every segment of financial services. Meanwhile, regulators and supervisors, lagging several steps behind, are struggling to catch up with the latest innovations. Although legislative progress is being made (for example, the Council of Europe approved a regulation on the harmonisation of rules on artificial intelligence on 21 May 2024), the current situation is that the principle of 'same risk, same regulation' is not yet applied in all areas[18] (*Kerényi – Müller 2019*).

The use of technology-based solutions to support business processes, such as data mining, data analytics and artificial intelligence, requires the application of several ethical considerations. In principle, data protection should be ensured by complying with rules similar to GDPR, while maintaining transparency on data collection and use. Automation can significantly increase the efficiency of credit institutions, but it does not relieve them of their decision-making responsibility, and accountability must still be pursued. Automated systems are tools that support, but do not replace, human decision-making. For this reason, the role of ethical practices in the organisational culture and procedures of financial organisations and credit institutions will remain and is expected to become increasingly valuable in the future.

Business development includes strategies to promote business growth, which vary from sector to sector and from organisation to organisation. The main pillars include strengthening market position and improving efficiency and future stability. Technological developments such as AI, blockchain and digital financial services present both opportunities and regulatory challenges. Adapting to and complying with GDPR, MiCA, DORA and other relevant regulations are all business challenges that trigger product and process improvements in individual organisations and their supplier networks.

[18] Council of the European Union (2024): *Artificial Intelligence Act: Council gives final green light to the first worldwide rules on AI* – Consilium (europa.eu). Press release. https://www.consilium.europa.eu/en/press/press-releases/2024/05/21/artificial-intelligence-ai-act-council-gives-final-green-light-to-the-first-worldwide-rules-on-ai/. Downloaded: 6 June 2024.

5. Results, proposals

In the financial sector, the compliance function was originally introduced for regulatory control; however, its importance has expanded and it has become an integral part of everyday business operations. The constantly evolving legal and regulatory environment has made compliance management an increasingly complex activity, and traditional approaches need to be reassessed. Over the last two decades or so, a risk-based approach to compliance has come to the fore, with resources being focused on the most risky compliance issues and areas of law (e.g. consumer protection). A structured and systematic methodology to identify, assess, mitigate and monitor compliance risks is essential to allow for consistent intervention, back-testing and data re-use (*Esayas – Mahler 2015*).

The rapid evolution of the regulatory framework and its increasing importance is (also) logical from a business perspective and offers opportunities for financial institutions that are reflected in business performance. Effective compliance management significantly increases business development potential by strengthening reputation across different markets (e.g. customers, suppliers, investors, employees), business confidence, service quality and customer experience. Compliance helps to build goodwill by fostering trust and credibility among stakeholders, thereby strengthening the reputation of the company. In practice, this is achieved by operating in accordance with standards, guidelines and regular audits, while the impact of compliance-driven product or process improvements can be measured through brand perception and stakeholder feedback. By meeting industry standards, service quality, consistency, timeliness and punctuality regarding performance are increased. This can also be measured and monitored through customer satisfaction measurements and compliance audit results. The improvement of customer experience can be quantified through indicators on complaints handling, customer retention and problem incidents. Among other things, these indicators can demonstrate the impact of compliance management on business performance.

One should also not ignore views that highlight the dangers of over-regulation. There is no doubt that both in the European Union and in Hungary, a robust set of rules has been put in place to prevent money laundering and to combat terrorism financing, or more recently, to comply with the sanctions and laws against Russia. Compliance with these rules is one of the core areas of financial institution compliance. There are, however, indications that financial institutions are sometimes overly elaborate in their customer due diligence. This is particularly true for customers with foreign ownership, management or business activities that can be considered atypical, even if there is no specific risk element in their case.

Banks, fearing that their practices will subsequently be found unsatisfactory by the supervisory authority, will sanction customers (for example, by refusing to open an account). The problem for businesses can be a lack of transparency or demonstrable operational activity. Businesses therefore often see compliance required by financial institutions as an obstacle, as a ‘deal breaker’, especially when they see a dichotomy in practice. For example, a business branch refuses to open an account, but a retail branch is willing to open an account for the same customer at a much higher cost (*Fogarasi 2022*). The solution to the problem is predictable, transparent regulation that customers can understand. The European Banking Authority pointed this out in its 2022 report, stressing that “unwarranted de-risking and ineffective anti-money laundering practices can result in the exclusion of legitimate customers”.[19]

To promote compliance and business sustainability, we propose the following:

1. Managers should strive for strategic commitment to compliance systems, while at the same time developing procedural alignment that links these functions to the company’s business objectives. Secondly, the experience and established systems of the credit institutions operating in the same segment, in this case credit institutions, should be shared in a partnership to ensure the coherence of the system. However, group reciprocity is also needed in the development of common surveillance systems, which allows information exchange and cooperation between organisations. It seems contradictory to suggest sharing compliance practices while arguing that they contribute to a company’s competitive advantage. The reality is that compliance and risk management systems are highly organisation-specific, tailored to the needs, objectives, values and environment of each organisation. The principles of compliance are similar, but the implementation of the principles is unique and can vary significantly between organisations. Furthermore, sharing best practices in compliance is a common goal among business actors, as it promotes a stable and reliable market environment. Information exchange can mitigate systemic risks. A collaborative approach benefits the market as a whole, contributing to a more robust, flexible business ecosystem.

2. Technology can be used and exploited to reduce compliance risks. Through technological innovation and innovative approaches, organisations are able to manage compliance processes effectively and improve performance (*Deloitte 2015*). Automation (data analysis, questionnaire research, data aggregation, troubleshooting, etc.), the use of chatbots and artificial intelligence may reduce

[19] EBA (2022): *Opinion of the European Banking Authority on ‘de-risking’*. EBA/Op/2022/01. European Banking Authority, 5 January https://www.eba.europa.eu/sites/default/files/document_library/Publications/Opinions/2022/Opinion%20on%20de-risking%20%28EBA-Op-2022-01%29/1025705/EBA%20Opinion%20and%20annexed%20report%20on%20de-risking.pdf . Downloaded: 6 June 2024.

time-consuming and costly tasks and reduce human errors and mistakes. The latest technologies may provide statistical indicators that can be incorporated into risk prevention systems and help measure the impact of changes on business development (for example, in the areas of product development, consumer protection or customer relations).

3. In addition to observing external and internal rules and standards, the corporate compliance function is also responsible for enforcing the ethical standards set by the company (e.g. ISO 37301). The usual compliance tools – such as compliance procedures, labour law sanctions, etc. – do not always detect and address ethical problems (*Törcsváry 2023*). Collecting and analysing employee feedback supports the management in fostering a culture of integrity, aligning employee interests and promoting long-term organisational success.

6. Conclusions

A compliance department defines the framework for operations, based on legal requirements and moral-ethical principles, and supports the achievement of the company's objectives by ensuring compliance with the framework and by imposing necessary and proportionate sanctions for overstepping the boundaries of the framework. Our study sought to highlight the links between compliance, risk management and innovation and the contribution of such to business development. In addition to regulatory compliance, a compliance mindset may add business value that can be reflected in corporate strategy, product development, risk assessment, customer experience and outcomes. Examining credit institutions, we demonstrated that compliance with regulations typically fosters an internal organisational environment and culture where innovation and sustainable growth can be created. An internal environment that focuses on innovation and excellence, taking into account external and internal regulations and the dynamic nature of the related compliance processes, may contribute to the stabilisation and development of financial institutions and thus the economy (*Novak et al. 2015*).

In today's business environment, effective compliance risk management, intertwined with innovation and business development, is essential for all companies, including credit institutions. These interrelated management areas have a significant impact on a company's performance, long-term reputation and business sustainability. It is important to take an organisation-wide approach (*Haelterman 2022*). The scope of compliance risk management extends to all areas of the business and supporting back-office areas.

We called attention to the phenomenon of financial institutions engaging in 'unwarranted de-risking' or flawed anti-money laundering practices, simply for fear of supervisory action and sanctions.[20] On the one hand, this raises the importance of legislators' and supervisors' roles in ensuring that regulation is transparent, predictable, known and understandable to customers. On the other hand, it calls for a change of approach on the part of financial institutions. They need to realise that banking compliance is not a regulatory activity, but a service activity, designed to be multi-faceted, but in no way to discourage customers. It is also in the interests of economic operators if compliance can effectively screen out those who are actually at risk, but does not unnecessarily complicate the process of persons, businesses and other organisations that do not have a risk element becoming customers (*Fogarasi 2022*).

The key findings of the study are summarised below:

1. Compliance management is an interdisciplinary field, and thus collaboration between legal, business and risk management experts is crucial, in order to effectively identify, assess and manage compliance risks.

2. The continuous review and improvement of compliance processes (e.g. planning, monitoring, incident management, etc.) by managers is essential to keep up-to-date with the changing business environment and regulatory requirements. In addition, decision-makers (regarding civil, labour and criminal law) are accountable for the performance of the company and the information disclosed. Managers have a key role to play in supporting and promoting the development and strengthening of compliance awareness and culture (*Teichmann – Wittmann 2024*).

3. Legislators, regulators and supervisors play a decisive role in ensuring a sound, stable and sustainable financial market environment. Their role includes developing rules, standards and recommendations that support market integrity and transparency and encourage prudent risk management practices, and business leaders and decision-makers need to understand the intersection of compliance, risk management and innovation. To do this, they need to develop fit-for-purpose processes, systems and policies that enable the organisation to meet its legal obligations, mitigate risks and encourage innovation.

[20] See footnote 10.

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