CLARITY™ INSIGHTS

EXECUTIVE BRIEF:

Anti-Money Laundering 2018;

A Risk Reward Perspective

Value Proposition

Anti-money laundering compliance has become a significant concern for banking and financial institutions in recent years. Reports of suspicious financial activity are on the rise, and with them increasing overall costs of anti-money laundering compliance initiatives. Companies are examining how to better manage these costs in a society where security concerns are paramount, but there are risks and rewards to consider when thinking about either increasing or decreasing anti-money laundering spend.

Hidden Costs

There are many contributing factors to the costs of anti-money laundering compliance. Some are clear and well understood by financial institutions, such as fines paid when companies are not in compliance, and the costs to staff a team committed to maintaining compliance.

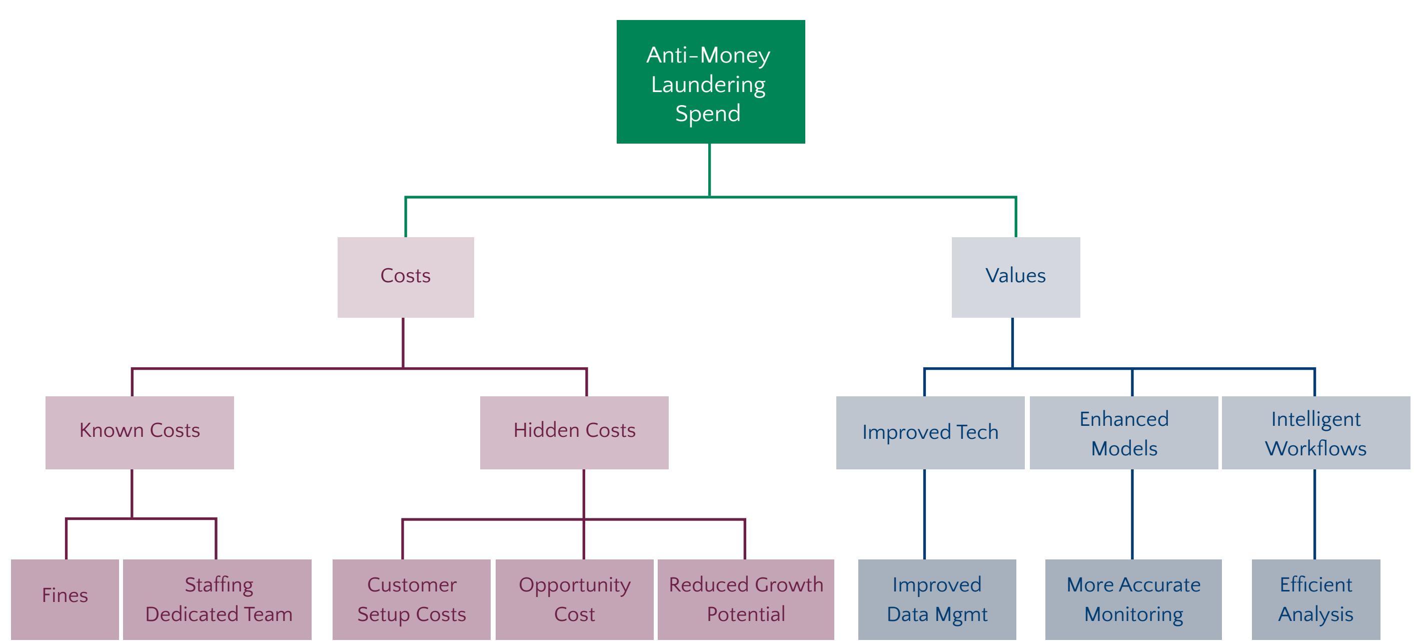
Some examples of hidden costs:

- **Opportunity Cost**
- **Higher Cost of Customer Set Up**
- **Reduced Growth Potential**

A [LexisNexis study](#) of anti-money laundering spend in Asian markets revealed that almost half of companies surveyed have a team between 30 and 99 employees dedicated to anti-money laundering activities.

In addition to known costs, there are also costs that are less quantifiable. For example, there are opportunity costs associated with the time it takes for onboarding new customers. This process can be extended as financial institutions are required to do their due diligence and handle any alerts, resulting in higher set up costs, and delays is account openings for new customers.

Another hidden cost could potentially be reduced growth potential in the long term for financial institutions who choose to avoid risk in their organizations rather than invest in strong anti-money laundering controls. For example, banks with higher false positive rates may be missing out on business due to the extra time spent addressing alerts. Companies who choose to strengthen their anti-money laundering capabilities in the short term will be well equipped to pursue opportunities in the long term that other institutions may view as too risky.



Values

While there are significant costs to anti-money laundering and compliance, there are also values. Investing in these activities builds trust and confidence in your customers. Financial institutions also report that it improves data management and helps them understand their customers.

What can you do about it?

So, what can be done to combat the rising cost of anti-money laundering compliance? **The following are some strategies to consider:**

- **Improved Technology**
- **Enhanced Models**
- **Intelligent Workflows**

Each of these can go a long way in increasing efficiency and effectiveness of anti-money laundering activities. Financial Institutions surveyed by LexisNexis report that an increased usage of unstructured data analysis, machine learning, and cloud based technologies have helped overcome some challenges. Moving to a more relational model rather than transactional model of storing data can improve accuracy of monitoring systems. Workflows that are well documented and repeatable make it easier to analyze alerts more efficiently, and can lead to optimization of transaction monitoring systems.

The Expanded Ecosystem and AML/Financial Crimes Value Chain

There are many components to the anti-money laundering and financial crimes analysis framework, all of which have opportunities for optimization to improve cost effectiveness.

Data Infrastructure

Data is stored in a layer that is accessible by monitoring software. Data should be properly cleansed and profiled to establish accurate business rules. These rules are then applied to generate alerts based on certain criteria. The data infrastructure may also include a report generation engine that is used to power dashboards and other presentations required by the financial institution.

Analysis

Analysis is a crucial and unavoidable step in the anti-money laundering compliance process. No matter how many alerts may be generated by transaction monitoring software, each individual alert must be viewed by a human to separate out the transactions that could pose a risk from those that do not. An analyst should look at the 'Who?', 'What?', 'Where?', 'When?', 'How?', and 'Why?' of each alert-triggering transaction to really determine if it should be investigated further.

Case Management

Case Management is utilized to manage alerts that are triggered that need further investigation. This is important not only for case tracking in the present, but also for future analysis. Looking at past cases can help analysts determine course of action for similar alerts and in addition to that, can identify when individual customers or organizations are becoming repeat offenders.

Reporting and Monitoring

Reporting and Monitoring should follow a well-defined workflow. Alerts should be prioritized so that the highest risk alerts to an organization are addressed first, and by those with the proper experience. Results of analysis should be used to optimize which transactions trigger an alert. Reporting should satisfy compliance requirements, as well as allow organizations to view all information relevant to an alert and make sound business decisions.

Turning Superior AML Performance from a Cost Center into a Profit Center

Investing in and improving a financial institutions anti-money laundering value chain can create additional revenue as well as savings opportunities. Two ways this can be done is through the ROI value chain and through the productivity value chain. For instance, a bank that invests in anti-money laundering activity is reducing their risk in the long term. This frees up Tier 1 capital for investment therefore providing opportunity for additional revenue. In terms of productivity, financial institutions may find that improving operational effectiveness provides more of a savings opportunity than improving models. Model improvement is not as easy as it was a few short years ago, so investing may not provide as much 'bang for your buck'. Companies should look for ways to measure and improve their analysis and case management processes either through automation or other means.

> Impacts of even small improvements can be felt across the entire value chain.

New Approaches

There are several new approaches that can be applied to improve anti-money laundering activities in financial institutions.

Cloud

Cloud data storage is rapidly becoming a more popular way to store data and for good reason. Cloud storage can save hardware costs for financial institutions, while also making data more accessible. When combined with machine learning techniques to more accurately predict and identity suspicious activity, this can really improve an organization's anti-money laundering compliance.

Graph Database/Algorithms

Graph databases differ from traditional relational databases in that they classify data in according to the relationships between different subject areas. This brings context into a transaction to shed more light on it. For example, a transaction between two parties can be identified as between an employer and employee, a customer and a vendor, or between two individuals that may actually be the same person. Identifying relationships may help to reduce false positive alerts, keeping the backlog of alerts manageable, and investigation costs low.

Machine Learning

Advancements in the field of machine learning, such as algorithms for high dimensionality data, deep learning and sparse learning can also improve anti-money laundering practices. New models have been developed to improve performance on data with many fields and dimensions. Deep learning enhances models by applying many layers that serve as inputs into the next layer. Models are also being developed to address sparse data.

Case Management Automation

In the past, case management has been a largely manual and cumbersome process for Financial Institutions. It is now possible to automate case management. The company Narrative Science provides technology that will automatically generate language to transform data into a narrative.

Qualifying Impact

Better Models

To quantify the impact of implementing an improved model and applying to anti-money laundering, consider what benefits a one percent decrease in the number of false positives would provide. Reducing the rates of false positives in turn reduces risk and eases the process of case routing and case management. With less cases to analyze and investigate, the process is streamlined and more thorough.

Better Servicing

To quantity the impact of improving servicing alerts, consider what benefits a one percent decrease in case management would provide. Manual case management in expensive, time consuming, and not optimal. Implementing automation or using a cognitive interface improves accuracy and efficiency as well as frees up time that can be dedicated elsewhere. Using software to generate natural language reports rather than manually provides similar benefits.

Conclusion

In summary, while costs of anti-money laundering and compliance are on the rise for financial institutions, there are many opportunities and levers that can be applied to improve the process and introduce cost savings. Impacts of even small improvements can be felt across the entire value chain.
New technologies such as cloud storage, machine learning, and case management automation are available and customizable for each organization's specific needs. Investing in these technologies, while potentially increasing costs in the short term, will reduce risk and increase optimization of the process in the long term, leading to increased growth and revenue.

Why Clarity

At Clarity Insights, we use data strategy, engineering, science and visualization to help companies action their insights.

Why? Because a majority of Chief Analytics Officers say that their biggest challenge is overcoming cultural barriers to new insights, as well as getting business buy-in. It is no longer enough to take an “if we build they will come” approach when it comes to insight systems—be it a data lake or a machine learning model. It takes an approach that will help build an insights driven culture.

How do we help clients do this?

We start any project by understanding our client’s business strategy, then understand how data can make it a success. This way we are always focused on the business outcomes and not what data actually exists. This approach also ensures business buy-in.

When we help you find the insights to achieve those business outcomes, we don’t own our tools. Rather, we help you embed them in your processes, and use change management to obtain adoption. We also focus heavily on knowledge transfer to our clients, ensuring they are empowered to take action faster and with more confidence.

These are just some of the reasons that more than 80% of Clarity’s customers hire us for additional engagements. We have been trusted partners to the most exacting, data-intensive organizations in the nation for years.