A perfect storm

FX-MM's AML roundtable brings together industry experts at a time when the focus on anti-money laundering has never been more acute. We examine the key trends and technologies that are being developed to strengthen anti-money laundering measures, and to help the fight against bribery, organised crime and the financing of terrorism in the financial landscape.

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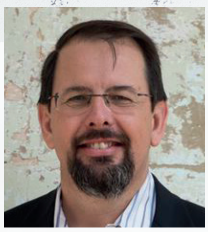

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PETER GARNHAM: What has prompted the increased regulatory focus on AML in recent years? To what extent has it been caused by a perfect storm of global austerity, security fears and an increased popular awareness of tax avoidance and corruption?

BEN MARSH I think the question perfectly frames the key drivers behind the increasing regulatory focus on KYC (know your customer) for AML and other purposes. Historically the drive to implement KYC and AML regimes has been driven by work done by the United Nations to highlight the costs to the global economy, and particularly emerging nations, of systematic corruption and theft of state assets, in addition to the efforts of law enforcement agencies to deal with the proceeds of crime.

From a security perspective 9/11 provided the impetus to address the financing of terrorism and the increasing use of financial and trade sanctions by Western powers as a non-military weapon to combat unwanted behaviour by other nation states. Good KYC is the key to ensure that persons trying to use the financial system for these nefarious means are identified, reported and stopped.

Post-2008, austerity politics have driven governments to focus on tax evasion as a driver for the KYC process, and we have seen the definition of financial crime extended under recent legislation to include tax evasion, as well as new client classification requirements affecting KYC, such as FATCA and CRS, designed to identify and report nationals who hold accounts outside the jurisdiction of their tax authorities.

MATT TAYLOR The focus on AML in the financial services sector has been around for over 25 years following the formation of the Financial Actions Task Force (FATF) and the subsequent release of the First EU Money Laundering Directive in 1991. Regulators and law makers have increased the depth, breadth and scope of money launder requirements ever since, with AML now considered to include counter-terrorist financing, bribery and corruption, narcotics trading, and most recently, tax evasion. Recent events, including terrorist attacks in Europe, the leaking of details relating to offshore company structures and prosecution of institutions who have been found to provide banking to narcotics traders has merely ratcheted the focus yet further on an already highly complex and publically visible area of regulation.

WAYNE JOHNSON Tax avoidance, tax havens and their uses have been big news in recent years and the public outcry over issues such as the Panama Papers have highlighted this issue further. When you consider that in 2009 the UN published a report stating that 3.6% of the planet's GDP came from criminal activity, and of that $1.6 trillion came from laundered money, it's clear the issue is significant. This money and risk represent a threat to the banking sector, international finance, and ultimately, governments and institutions.

PETER GARNHAM: Are banks bearing too much of the regulatory load? How much more can they take as far as compliance spending is concerned?

PAUL TAYLOR Recent studies suggested that global spending by financial institutions on AML compliance is set to grow to more than $8 billion in 2017, a compound growth rate said to be in the region of 9%. Over half of more recently surveyed individuals within financial crime compliance suggested that compliance spending will continue to increase.

Clearly, this is a huge spend on just one aspect of financial crime compliance, many in the industry are working hard on not only improving their controls, and stopping more bad actors, but also trying to find a balance to ensure that efficiency of process – and therefore cost – can be driven out.

It is clear that spending on the present scale cannot continue forever, and there continues to be a concern about a real battle for talent – and increase in salary costs – within this part of the industry.

PETER GARNHAM: So how can new technology, such as Hadoop, machine learning or distributed ledger initiatives, combine to reduce the cost of compliance and help in the AML fight? How can regulatory concerns over such technology be overcome? Or is the technology already fit for purpose?

BEN MARSH Machine learning and robotic process automation offer significant opportunities to reduce the cost of many operational processes within financial firms. This technology is new but emerging case studies show promising use cases in the KYC process such as the automation of collection of data from public sources to evidence KYC, and also reduction in managing false positives in the screening process.

Distributed ledger or blockchain offers the opportunity to create a network of trusted data that will remove some of the existing areas of manual data collection. Interestingly this technology also offers opportunities to deal with the challenges of forthcoming European data protection legislation as well.

WAYNE JOHNSON I have been at the UK Department of International Trade's first 'RegTech Mission' to New York this week and I'm excited to see the amazing technology we have at our disposal to combat issues like this. Technology will always progress, that much we know. One question to answer here is will it be adopted more quickly by those looking to deter crime or by those looking to commit crime?

Those using RegTech including technologies like automation, AI and machine learning have been able to cut costs. For example using the power of automation to complete client due diligence for AML compliance during standard onboarding is technology available today and it's already freeing up the time of humans to work on more complex cases.

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Banks and financial institutions will also be all too aware that utilising technology solutions will be considerably cheaper than some of the fines that are being handed out currently.

PETER GARNHAM: Is there a case for an industry-wide utility style AML solution? To what extent could increased collaboration within the industry help in the fight against crime?

MATT TAYLOR Certain aspects of the AML jigsaw, particularly relating to KYC efforts, can readily be addressed by shared technology. KYC is focused on being able to demonstrate the identity of your customer, that you understand where their assets came from and what they intend to do with them. The sharing and pooling of data between firms on these subjects can only be beneficial – the sum of many firms' data is better than one.

BEN MARSH Industry utilities offer a good solution to the lower risk, multi-banked clients where it makes sense to centralise the documents needed by financial institutions into one place. This both saves time and effort on the part of the financial institutions and their customers.

Separate to utilities, sharing of data amongst financial institutions provides a huge opportunity to identify nefarious activity and persons. Money launders and criminals are often involved in a web of companies and entities, so the opportunity to share this information provides a much greater chance of exposing these networks and their participants.

PAUL TAYLOR There is a case for further utility approaches within financial crime compliance domains, be that KYC, sanctions and indeed fraud and AML.

The very basic idea of the utility approach is to drive out efficiency of process and cost savings, but they also seek to promote community, collaborative approaches to challenges that all institutions face, a field that over time is increasingly being seen as non-competitive.

With plenty of reports these days of banks and public sector bodies trying to work together on financial crime challenges, utilities and collaborative approaches to these challenges have to be the way forward.

PETER GARNHAM: How have new regulations such as the UK bribery act changed the game in regard to corporate bribery?

MICAH WILLBRAND The reason bribery was sometimes seen as a cost of doing business in certain jurisdictions was that under the FCPA, the legislation globally enforced by the US, there is a loophole called a facilitation payment. A bribe is giving someone money for economic gain – to win a contract. But a facilitation payment is giving someone money to do their job better.

So if you gave a clerk in India, which is notorious for its bureaucracy, $1,000 to put your planning approval at the top of the pile instead of the bottom for instance, that is a facilitation payment which is not illegal under the FCPA. For years, that is how such gifts were classified: as a facilitation payment, not a bribe.

The UK bribery act changed all that, outlawing facilitation payments. In addition, it really took on private bribery. The FCPA is really concerned with bribing public officials to get government contracts and is very unlikely to be enforced on private companies. So the loophole where business to business gifts were unlikely to be investigated was closed. That has really helped in the fight against bribery and corruption.

WAYNE JOHNSON The UK Bribery Act has been in force since July 2011. However, it would seem that businesses are still not doing enough to prevent bribery, particularly in relation to the risks posed by third-party agents and intermediaries. The continued increase in investment opportunities in high-risk jurisdictions means that companies need to ensure their policies on bribery preventions are set accordingly.

Recent years have seen the escalation of corporate fines imposed by the UK and US regulatory and criminal authorities. The LIBOR and FX scandals alone generated fines in the billions. However, attention appears now to be focused more on the individuals involved in the wrongdoing rather than the corporates. In March 2016 the FCA and PRA implemented the Senior Managers and Certification Regime (SMCR), a range of policy changes to increase individual accountability within the banking sector. The changes have been put in place to ensure that individual responsibility is at the heart of how firms conduct themselves. One year on, the FCA has seen firms taking their responsibilities more seriously. But we recognise culture change takes time and there is still more to do.

PETER GARNHAM: Are banks taking on too much of the burden as far as corporate compliance is concerned? What can corporates do to ensure their own compliance?

BEN MARSH I don't see there is any way round the burden of compliance falling on the financial institution, especially given the fact that these are after all the regulated parties in the business relationship. I do, however, see many financial institutions looking closely at the profitability of their customer relationships in the context of their compliance costs and actively looking to exit those which are not economically viable.

MICAH WILLBRAND In the wake of the FIFA scandal we are starting to see a push from the banks into corporates. Banks are now saying to the corporates that as part of their conditions of banking, they have to have various anti-bribery and corruption controls in place.

At the same time, regulators are recognising the position of banks that are dealing with corrupt organisations. Corporates are now starting to be pushed from the Serious Fraud Office in the UK and the Department of Justice and SEC in the US to have controls in place because they are going to be held to the same scrutiny that the banks are.

PETER GARNHAM: Can the AML fight ever be won? What do you consider would constitute a victory?

BEN MARSH Given that criminals are often highly resourceful and that there are significant rewards for their success, I think it unlikely that this is a fight that can ever be truly won, though we can make it ever harder for them. In my mind a victory is one where culture and attitudes prevalent in the financial industry do not tolerate this activity.

MATT TAYLOR Money laundering has been around for over 2,000 years, so assuming that the AML fight can be won is somewhat foolhardy. As cash transactions are becoming increasingly less prevalent, criminals are having to find alternative means to layer, clean and place their assets. This is leading them to operate on a global scale with laundering activities now often built on complex international schemes with many layers of deception and movement.

What could be constituted as a victory is hard to define, but having firms operating similar control standards in a consistent manner, making best use of the technologies available, and at a price tag that does not represent a barrier to business, would be a significant stride forwards.

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