CHANGING THE RULES OF THE GAME:

Taking AML Analytics Beyond Compliance

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As federal regulators continue to throw a more stringent and broader investigative net over financial crime and potential money laundering violations, banks and other financial institutions are carefully reassessing their Bank Secrecy Act/anti-money laundering (BSA/AML) programs, looking primarily for compliance gaps and inadequacies. Financial institutions have limited resources available for BSA/AML compliance that need to be used efficiently. In addition, the increasingly sophisticated, potentially disruptive tools of so-called big data and the analytics to evaluate and employ information, offer a critical opportunity to dramatically enhance AML capabilities and to do much more.

State-of-the-art data management, beginning with AML and done correctly, can enhance enterprise-wide risk management. Big data, along with analytics that become more sophisticated almost daily, can quickly move an institution from taking a reactive and tactical approach to compliance to identifying and mitigating AML risks in a strategic, proactive and efficient way. Failure to address the growing importance of data analytics, presents a lost opportunity for institutions working to advance their compliance program. Institutions that choose to glean useful information from the massive volumes of data available will obtain a more sustainable single customer view and a better understanding of their customers, the transactions taking place and their financial crime risk. As a result, the organization will be better able to more effectively analyze and eliminate operational inefficiencies. Outside of AML, such analysis can also improve profitability by sharpening insights into customer transactions and preferences, and upgrading the range and quality of new financial product offerings.

Any AML program enhancement must begin, however, with a carefully considered assessment of existing AML efforts, the data inputs that make it run, the output and reports it produces, and, perhaps most important, the organization’s risk appetite, management strategy and support for the program itself. The way in which each program reaches its goals must be uniquely tailored to the institution’s risk profile, culture of compliance and data inventory.

Building an Analytics Program: A Different Way to Think About AML Compliance

An AML analytics function provides an opportunity to make an AML program more efficient through the effective use of information already available in the institution. The increasingly rich amount and variety of data available to an AML program can be the engine that changes a modern analytics program from an isolated, reactive banking system to a full strategic partner in an institution’s decision-making arsenal.

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Four primary steps are involved in the adoption of an effective AML analytics program:

1. **Document the program’s purpose.** As an organization, establish the goals of the analytics program.

2. **Inventory the data.** Document and understand the availability, completeness, accuracy, and challenges of the data.

3. **Define the data usage.** Align the program’s purpose and data inventory to effectively define and implement how the data will be used and converted into information such as key risk and performance indicators.

4. **Evaluate and adjust the program.** Make your program sustainable through ongoing evaluation and enhancement.

A value-driven, cost-effective AML analytics program is developed through a thorough understanding of the institution’s available and potential data sources and by clearly defining AML and enterprise goals. This effort must be designed so that it is an ongoing process that facilitates continuous improvement, sustainable evaluation and customized solutions. It also must be flexible enough to identify appropriate AML-specific enhancements as well as those that can feed into and complement risk management, customer product development and other critical operations. This is a process with objectives that can be tailored to financial institutions of any size.

Objectives of an AML analytics program include more accurate, efficient, reliable and timely identifying and reporting of financial crime, as well as the creation of sustainable and more insightful risk management tools and processes. An effective analytics program can also help an institution establish a sharper or targeted understanding of customers, their risk factors and their relationships with the institution.

### Document Program Purpose

Defining an AML analytics program starts with understanding the institution’s risk profile, vision and appetite, and establishing goals consistent with them. Goals of an analytics program might include some of the following general examples as well as others that are specific to the organization and environment:

- Increased program efficiency
- Reduced compliance costs
- Enhanced management reporting
- Increased institutional knowledge and understanding
- Advanced customer risk identification
- Advanced transaction monitoring through predictive analytics
- Dynamic risk evaluation and management

While it is necessary to stay true to the analytics program’s defined mission, the program charter should be flexible and dynamic, allowing the institution to mature and evolve over time. The charter should also focus on defining the primary players, roles and responsibilities. Executing the charter will begin to tie together the data governance within the organization, or at least set the stage for it.

### Inventory Data

Inventorying its data helps an institution know what data it truly has and the complexities associated with accessing it. As a result, an effective analytics program must assess the breadth, depth, and quality of data already being collected and generated as well as the way it is being used. This data usually includes:

- **Customer data:** This refers to the customer identification program (CIP), know your customer (KYC), customer due diligence (CDD) and enhanced due diligence (EDD) information that might be collected on a customer. It can include identification information, credit and business histories, demographic and business categories, and risk ratings as well as information about the customer’s complete relationship with the institution. Demographic information can be used for understanding and analyzing peer groups, assessing the risk impact of a customer segment and enhancing the customer risk rating model. It can also include customer product preferences and how and where customers interact with the institution.

- **Transactional data:** This refers to the detailed transactional information that is available through a variety of data sources. It includes source system information for various transaction types as well as any data warehouses and databases used by the organization’s AML models. Although the data in the inventoried sources might be duplicative, it is important to understand the true sources of the data, so that the most appropriate data is used. For instance, if the analytical task is related to monitoring the inputs to the transaction monitoring system as a triggering event for conducting tuning, then the monitoring system’s input or staging database might be the best source of data that is based on any predefined data filters for internal accounts or low-value transactions. On the other hand, analytics related to monitoring a new product or service might require data from the source system to
accurately understand the transactional population and the associated monitoring risks.

- **Alert data:** This is generated by the AML program itself, based on the results of customer and transaction monitoring. This can include suspicious activity alerts, watch-list screening reviews, due diligence flags, and other internal and external events or profiles that require review. Alert data includes components of customer and transactional information relevant for the alert and the associated disposition. Upon review and investigation of an alert, an AML-based decision is made about an alert.

- **Reported data:** This refers to the government-reported activity specific for a jurisdiction, such as the suspicious activity reports (SARs) and currency transaction reports (CTRs) that go to the U.S. Treasury Department’s Financial Crimes Enforcement Network (FinCEN). These can also include an analysis of industry SAR metrics published by FinCEN, which can be benchmarked against the institution’s own performance and factored into the institution’s assessment of program risks.

- **Data from other parts of the organization:** This can include financial, marketing, personnel, and other information critical to assessing the operations and state of the institution.

- **External data:** This can include news sources, industry reports and metrics, and other publicly available sources of information. The wealth of information available today at the click of a button can be an important, though potentially overwhelming source of supplemental data for an AML analytics program, particularly as it relates to a single customer view and organizational benchmarking.

The data in each of these categories must be reviewed to understand its completeness, accuracy, timeliness and availability. The assessment also should include a careful review of how each of the data streams is used in each segment of the AML program.

The data inputs for suspicious activity monitoring, for instance, might be used and integrated differently from how those for a CDD evaluation would be. The metrics and analytics will need to be customized for their specific function.

### Define Data Usage

A program’s purpose and the inventory of available data will largely determine how the data is used. The program’s purpose is to serve as the filter through which the data is passed in order to achieve the ultimate analytical reporting, monitoring and metrics program. An institution needs to identify how different data streams can be sliced and analyzed for the same AML program segment and how the metrics change when a single data source is designed as an input for more than one segment. Is the volume, type and breadth of data adequate for the data’s assigned purpose, for example? Is the data static or dynamic, reviewed regularly or stored and ignored? How often is the information reviewed and processed? Who does that and why? What reports are generated from each data stream and how often? How widely circulated and used is this data?

Just as critical, is determining whether the full value of each data stream is being captured. The analysis must look at how various data streams can be integrated not only into the entire AML program but also into the institution’s risk management practices. Transactional data, for instance, may be ideal for identifying how specific customer segments interact with the bank. Which customers are most likely to use and want seamless mobile access to their accounts? How can that access be better monitored for security and other problems? Are branch bank visits trending up or down, and for what purposes are they? How does this change in behavior affect the organization’s BSA/AML risk assessment?

### Evaluate and Adjust

All of the data collected, and the analytics that make it useful, can become important resources for making more timely risk management decisions that are based on consistent and accurate metrics. For example, analytics can help reduce false positives that lead to greater efficiency of the AML resources. To achieve this, though, the information itself must be of the highest quality and generated in a way that can be sustained. When data sources and availability are changing, for instance, that must be accommodated in any ongoing AML effort. Data must be capable of being constantly and continuously refreshed, with the refresh periods being adjusted as program objectives shift. Monthly reports and semiannual reviews, for example, almost certainly will prove inadequate for meeting many key objectives and programs as the availability of raw data and the computing power to analyze it grow exponentially.

### Barriers to Change

Developing an AML analytics program is not without its challenges. An institution will have to manage potential barriers to be able to establish a program that can have lasting impact on the efficiency and effectiveness of its AML efforts. Following are some such barriers that could prevent an institution from establishing a strong analytics program.

- **Leadership.** The success of any new analytics program always depends on the resources—human and financial—devoted to it. That support must come
Financial institutions can face serious staffing and expertise limitations when they try to overhaul older systems on their own. Top management might feel locked into outdated budget constraints that fail to recognize the full potential value of a comprehensive data analytics program. Senior leadership must have the vision and foresight to recognize the impact that effective analytics can have, not just on AML compliance but also on the entire financial institution.

- **A narrow response to regulatory pressure.** When the primary priority is only compliance, value-added and strategic thinking falls to the sidelines. Bank examiners driving the priorities of a program too often leads to quick patches and shortsighted solutions. Compliance can never be ignored. It can, however, become part of a holistic solution that provides the entire enterprise with invaluable big data and its analytics.

- **Budget constraints based on incomplete cost-benefit analysis.** The shift from compliance to strategic thinking can happen only when an institution begins looking at the full complement of benefits that high-functioning, enterprise-wide analytics offer. From aggressive and proactive AML compliance to sharply accurate transaction and customer profiles to more insightful risk management, up-to-date analytics offer an entirely new range of capabilities.

- **Aging AML systems.** Legacy AML systems and compliance strategies can be badly outdated. They can also be a fragmented patchwork of procedures and policies that no longer serve an institution effectively. Data might be poorly assembled, inaccurate, or collected too infrequently to offer an efficient platform for decision-making. Old systems, which can include recent products in some cases, might be incapable of producing timely, accurate, and reliable alerts and reports. At the same time, the people who run these systems might not have the experience or expertise needed to enhance them. Financial institutions can face serious staffing and expertise limitations when they try to overhaul older systems on their own. The right governance and an appropriate technology road map will help address this challenge.

A sustainable analytics and AML program requires an investment in the right human capital and technology, with sufficient resources to manage for regulatory changes, institution growth and diversification, business and operational shifts, changing roles and responsibilities, and employee turnover. An institution must have management that is capable of evaluating and appreciating these opportunities and is willing to allocate budget for the appropriate staff and technology to make both work at the highest level.

**Benefits Beyond Compliance**

Financial institutions are working in a new and extremely promising era of digital capabilities. Because an effective and sustainable AML program is optimized by digital analytics and management, the rapidly shifting environment offers a crucial doorway for critical tactical and strategic planning. With the development of a sustainable, flexible and insightful compliance effort, a bank possesses an invaluable tool for guarding against financial crime and abuse, and for meeting examiner expectations and avoiding regulatory actions, fines and reputational risk.

At the same time, via an effective AML analytics program, a bank develops a large body of knowledge and the means to use it to make the institution more competitive, insightful and efficient. That is why AML analytics and compliance management, when approached holistically, can reach beyond fine-tuning a single isolated program to serve the entire institution. For example, a bank with a strong analytics program can reduce costs and focus its resources more efficiently. By generating insight into certain types of customers—for instance, those that consistently wire money to foreign countries—AML analytics might flag risks more quickly, focus inquiries more specifically, and save valuable staff time and effort. By allowing banks to isolate patterns and exceptions rather than requiring them to put large numbers of unexceptional customers and transactions (such as false positive alerts) through the system, AML analytics can identify customers that make certain transactions in unusual ways and help compliance staff to work more effectively.

Enhancing AML data analyses can also reduce false positive transaction monitoring alerts, cut the number of EDD inquiries required and reassure bank management concerned about potential regulatory fines. The entire AML alert framework becomes more reliable and productive as a result.

At the same time, targeted and timely reporting gives management some tools and capabilities that previously were unavailable. Customer transaction patterns can lead to new product development, and a more reliable and predictive alert system can be a critical tool for risk managers. Holistically integrated, sustainable AML analytics provide the decision-making tools that enable managers to be confident and proactive. Ultimately, these enhanced capabilities across the organization will increase efficiencies and reduce costs, and will be received well by examiners and external auditors.

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