Financial Crime And Compliance in a Socially Distanced Economy

By Thomas Andrews

Economic Factors Driving Change

In light of recent events, the U.S. economy is experiencing a dramatic and fundamental change in how businesses operate. Many employees have shifted to remote work, while some have been furloughed or laid off. Businesses, large and small, are being forced to implement social distancing measures while remaining profitable. Regulators are scrambling to balance these changes with long-standing policies not well suited for the current environment.

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As working from home has become the de facto office environment, financial institutions must shift their operating models to facilitate this change. Compliance and customer onboarding teams must collaborate to assess the risk of customers and transactions remotely while not sacrificing the quality of work. To deliver on this, financial institutions must focus on expanding the capabilities of the firm to efficiently onboard and assess the risk of customers in a virtual work environment.

Moreover, many businesses have shifted to a cashless transaction model, opting for payments to be made with credit and debit cards rather than cash to limit hand-to-hand contact with customers. The cashless trend was already coming; however, prior to the pandemic, cash was still a primary means of payment for smallto medium-sized transactions. According to a Federal Reserve Board report in 2019, consumers used cash in 26% of transactions, down from 30% in 2017. The movement toward a cashless economy, accelerated by the pandemic, has a multitude of effects for anti-money laundering (AML) compliance. Financial institutions' failure to incorporate this trend into AML compliance methodology will leave them behind the curve.

It is important to mention that these shifts in business practices are not just contained to the U.S. economy. As we saw in 2007-2008, economic slowdowns, regulations and business practices have rippling international effects.

Virtual Onboarding

Although financial institutions are not bearing the forefront of the economic impact, they are exposed to the changing regulations, customs and actions of bad actors. One way financial institutions can dynamically adapt to the change in social norms is a greater focus on virtual onboarding or electronic know-your-customer (eKYC) processes. EKYC is the remote, paperless process of customer onboarding, which increases efficiency and minimizes costs associated with the traditional KYC process.

As the KYC verification process becomes more digitized, however, a corresponding increase in the risk of identity and signature falsification emerges. Preventative measures must be embedded within the eKYC process, such as facial recognition and machine learning (ML) signature verification, to ensure bad actors do not slip through the cracks.

Huron's Facial Recognition Solution

In 2019, Huron's financial crime and compliance consulting team developed a new solution that leverages facial recognition technology to verify a picture or video of one's face against a government-issued ID. This verification was then integrated into KYC case management software, enabling the virtual onboarding and investigation process. Verification thresholds may be set and adjusted to incorporate face masks, winter outerwear and photo quality. Additionally, verification measures must be put in place to ensure the authenticity of IDs submitted online. Financial institutions should consider implementing a similar process to enhance their eKYC capabilities to expose and identify individuals looking to fraudulently benefit from virtual onboarding.

Time to Act

In a world where events happen and regulations follow suit, it is paramount that financial institutions are at the cutting edge of eKYC and preventative money laundering measures. Financial institutions will set the pace for preemptive measures in the digitalization of fraud for the rest of the world. Huron's financial crime and compliance consulting team is ready to advise financial institutions on the implications of this pandemic. Compliance regulation is not an option, and investing in these enhancements will strengthen the compliance capabilities of financial institutions in the age of digitalization, cashless transactions and yes ... social distancing.

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Cashless Payments and Implications for AML

In addition to an emphasis on virtual onboarding, another effect of the pandemic on banking compliance is a concerted effort by businesses to limit cash transactions. This move toward a cashless payment model naturally leads to changes in traditional AML methodology. AML scenario threshold logic must be altered to account for this change in behavior and a shift in product utilization. Refinements of these thresholds will lower the false positive rate for legitimate transactions while accounting for adjustments in criminal activity. Legitimate businesses may see a change in their typical cash use, thus triggering AML alerts relating to changes in behavior. Adjustments to these scenario thresholds will lessen the burden on financial institutions' AML investigation departments. On the other hand, a cashless society may open the door for more savvy criminals with knowledge of AML to circumvent the placement stage, which has been historically ruled by cash. Thus, it is important for financial institutions to understand the following:

- How their customers have been affected by the COVID-19 pandemic and subsequent economic slowdown.
- Where new and existing customers' funds are ultimately originating from.

The product of this focus will make it increasingly more difficult for bad actors and criminals to legitimize their funds while accounting for the economic implications of a global pandemic.

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