

Future of Compliance

September 2020

Foreword

The compliance landscape in the financial ecosystem is one of the most dynamic and therefore challenging area that brings together different stakeholders under the umbrella of technology. Banks, Fintechs, Regtechs, regulators and other financial institutions are all striving for a better and more secure financial environment. Therefore, the digitalization and the reformative power of technology are playing a vital role in the financial world as they provide the most effective solutions to the financial crimes and regulatory requirements.

In this White Paper, we review and discuss the 8 trending topics that are associated with the future of compliance in the world of finance under the light of technological developments and the emergence of new methods to deliver the best financial solutions in the digital era. To adopt a fully inclusive approach in the demanding compliance atmosphere, financial institutions consult to the support of RegTechs, artificial intelligence, machine learning, blockchain and similar digital solutions as a means to enhance operations, reduce costs and develop fraud-detection processes.

Additionally, the effects of unprecedented phenomenon COVID-19 on the financial landscape are explored in this paper focusing on the accelerated move towards the cashless society, new consumer trends and changes in the payment or money circulation habits within the framework of the 'new normal'.

As Fineksus's all efforts are to offer pioneer technology for financial institutions, we aim to offer the best financial services solutions with our software products concentrating on financial messaging, Anti-Money Laundering (AML) compliance processes, cloud-based solutions, implementation of SWIFT systems and fighting financial crimes by placing technology and its transformative power at the center. We hope that the insights and trends presented in this paper will reinforce and encourage the processes of digitalization in the financial industry while at the same time will illuminate the area of financial compliance.

Ahmet Vefik Dinçer, CEO



Index

Foreword	2
Summary	3
Index	3
1. Emergence of RegTechs	4
2. Stricter regulations require more from AI technology	5
3. Covid-19 effect on financial ecosystem	6
4. How fintechs interrupted financial payments industry	7
5. Role of RegTechs for digitalization of banks' compliance	8
6. All-in-one AML solutions for all institutions	9
7. Digital KYC / CDD via integration of biometrics and AI	10
8. Are AML compliance vendors ready for blockchain technology? ...	11
References	12
Contact Us	13
About Us	14

This White Paper explores the popular trends in the payments industry which have direct or indirect effect on the evolution of the compliance processes. The digitalization in financial solutions are transforming the way financial institutions (banks, regulators, FinTech companies and other stakeholders) operate. The concepts of RegTech, AI (artificial intelligence), blockchain, AML (Anti-Money Laundering), KYC (Know Your Customer), the effects of COVID-19 on the financial ecosystem are among the topics that are discussed in this paper under the light of compliance.

1. Emergence of RegTechs



RegTech provides the financial institutions with both compliance-related and operational advantages such as scalability, cost-effectiveness, security and flexibility with its cloud-based structure.

Just as FinTech plays a vital role in the way financial services are delivered, RegTech (Regulatory Technology) has emerged as a new means of streamlining the regulatory compliance in the financial services industry and supporting FinTech companies to remain thoroughly-informed about the regulatory requirements which may directly or indirectly affect their businesses. RegTech can be shortly defined as the incorporation of the necessary technologies to facilitate the fulfillment of regulatory requirements.

RegTech provides the financial institutions with both compliance-related and operational advantages such as scalability, cost-effectiveness, security and flexibility with its cloud-based structure. As for the compliance processes, the affordable and functional nature of RegTech enables a smoother and more successful functioning because it solves issues related to customer identification, real-time monitoring, affordability and stay updated on the new regulations.

As a result of rapid technological changes, regulatory landscape has been facing a transformation from protecting customers to protecting data. Therefore, there is a tendency to move towards the notion of Know Your Data (KYD) which will soon seem to be replacing its predecessor KYC (Know Your Customer). RegTech aims to provide support in this new technology-focused financial atmosphere that instead of regulating people is now interested in regulating data which embodies digital processes, automation and algorithms. The technological developments in the fields of artificial intelligence (AI) and machine learning (ML) allow for new methods to meet the challenges, to monitor the market, to report processes and to remain compliant with the regulations. This trend eventually requires a new mindset and approach from regulators in order to be able to ensure the regulatory side is always up-to-date and comprehensive. The effective use of analytics, machine learning, artificial intelligence and other related technologies increase the overall functionality and efficiency of the financial businesses.

2. Stricter regulations require more from AI technology



The false positives can be reduced by 60% with the implementation of machine learning technology and it is expected that this ratio is to rise up to 80% as by nature, this technology continues to learn.

As one of the natural outcomes of digitalization, the rise in mobile payments and in necessity to offer better customer experience, payments have become one of the most digitized parts of the financial world. While this technology promises to bring in many benefits to the industry, it also creates a possible threat to the payments making them more vulnerable to digital financial crimes. To prevent criminal activity, regulatory requirements have become even more severe and strict and the financial institutions are faced with the fact that they will not be able to ensure a full compliance to the new regulations by manual operational solutions.

Unfortunately, many financial institutions are still using rule-based, manual fraud detection systems which are failing to keep up with the real-time data and to realize the correlations or risky activity in the transactions. Banks are competing with each other to offer the best customer experience and they are trying to achieve this by lessening the number of verification procedures which actually diminishes the overall effectiveness of rule-based systems.

However, with the help of artificial intelligence and machine learning, financial institutions can fight with fraud more effectively and remain compliant with the regulations at the same time. Machine learning enables banks to both check and analyze the existing data about the customers and their financial activities. As a result, the false positives can be reduced extensively as it constantly continues to learn and rationalize and as opposed to rules-based systems it can easily detect fraudulent behavior. According to a case study conducted by Teradata, the false positives can be reduced by 60% with the implementation of machine learning technology and it is expected that this ratio is to rise up to 80% as by nature, this technology continues to learn. Another finding is that machine learning solution increased the detection of real fraud by 50%.

The rise in the need to use the help of AI and technology in financial landscape and in the severity of the regulatory requirements have occasionally raised the bar for RegTech services and AI solutions. In areas like data protection and privacy, legal and regulatory compliance, cost-efficiency, transparency, fraud prevention, operational efficiency, handling of customer complaints and many more artificial intelligence is being effectively used now. As compliance is one of the most challenging issues that the financial institutions have been dealing with, while at the same time ensuring customer satisfaction, the regulatory solutions AI offers can be listed as the most favorable one for banks and since the regulations constantly evolve with the technological developments in the financial world, the expectations from AI technology will likely to be increasing as well.

3. Covid-19 effect on financial ecosystem



The Organization for Economic Co-operation and Development (UOECD) forecasts that the global economic growth rate may be reduced by 1.5% in 2020 as a result of the international lockdowns.

The pandemic resulting from the COVID-19 outbreak caused many businesses an operational disruption. The reflections of this showed themselves in the financial ecosystem as a transition towards a more digitalized and zero-touch environment. The concept of cashless society has become a rising trend as people refrain from using cash and tend to use methods that require less contact like digital wallets and credit/debit cards. Just as the consumer behavior is shifting, digitalization processes, regulations and global markets are being affected and changed, consequently, the money circulation habits and the businesses depending on them evolved in line with the new standards of the 'new normal'.

When important sectors and markets like retail, food-chain and transportation faced pauses and terminations, the global stock market crashed on February 20, 2020 which resulted in the serious contractions in most global markets, namely an economic recession. The "Coronavirus recession", that is the name given to this phenomenon, indicates the economic downturn the world economy is dealing with in 2020 due to the coronavirus pandemic. The impacts of this recession are expected to reflect themselves in the long-run and in severe consequences although the pandemic may end sooner. The Organization for Economic Co-operation and Development (UOECD) forecasts that the global economic growth rate may be reduced by 1.5% in 2020 as a result of the international lockdowns.

In terms of consumer side, the spending trends have been changing and digital options are mostly preferred since the no-contact methods do not pose threats related to spreading of the virus as much as the traditional payment options do. The rates in the use of mobile devices for payment-related services and online shopping are on the rise unsurprisingly.

4. How fintechs interrupted financial payments industry?

FinTech (Financial Technology) is basically the intermixture of technology and financial services which aims to support companies to operate more efficiently in their financial businesses by using digital solutions like new software and applications or processes. FinTech sector is mainly dominated by the technology-driven start-ups via the innovation of the traditional services and products used in the financial services industry. By offering an end-to-end transaction processing via cloud-based services, the FinTechs have become highly popular within the financial world and actually have started to cause innovative disruptions in the financial payments industry by re-defining the competitive atmosphere in the Financial Services sector.

Actually, FinTech is not a new phenomenon; its existence goes as early as the financial services, although it had different forms virtually. However, with the global financial crisis in 2008, the evolution of FinTech has gained a momentum and it has begun to play an important role in reforming areas of financial payments, investments, customer experience, commerce, insurance and even money itself (cryptocurrencies). In a very short period of time, FinTech companies have seized the power to identify the changes themselves as well as their form, direction and speed in many sub-fields of the financial services. Simply put, FinTechs have succeeded in fields where traditional financial institutions failed.

The disruptive nature of FinTech can be summarized as:

- Online shopping trends are growing rapidly and leading to a tendency towards cashless solutions for transactions.
- There is a clearly visible shift of power from the traditional services offered by banks towards better customer experiences provided by the FinTechs and other technology firms that find digital and practical solutions for customer engagement.
- In data-collection and management, new trading platforms suggest a holistic approach by using analytical tools and technologies like AI (Artificial Intelligence).
- Infrastructural investments like transaction process improvement or adoption of software are expensive. As a solution, most of the traditional financial services companies are looking for FinTech partners to ensure less costly solution and to refrain from an extra budget to be spent on the refurbishing of the infrastructure.

Among many other fields, it is expected that consumer banking and payments will be the ones that will be the most affected by the disruption of the FinTechs. Together with the appearance of online platforms enabling both individual users and businesses to exchange, lend and borrow among each other, new credit models have emerged. Also, the new digital payment processes that mitigate the payment transactions and the higher use of digital and electronic devices and applications that are used for faster money transfers are among the trends disrupting the payments industry. In terms of the customer experience, FinTechs offer improved accessibility, effectiveness and personalized services to recognize and address the customer expectations in a simpler and faster way. Customers getting used to digital solutions now demand services like smoother digital onboarding, faster loan approvals and free of charge payments.

FinTechs have succeeded in fields where traditional financial institutions failed.



5. Role of RegTechs for digitalization of banks' compliance

RegTech enables a more automated and digitized ecosystem together with the AI so that the financial institutions can both perform their legal obligations by minimizing the risks and maintain the trust of institution in the customer in a sustainable way.



The concerns related to costs, compliance and consumer satisfaction are driving banks to invest in technological solutions faster than ever before.

The unpredictable and unstable nature of the financial ecosystem resulting from the emergence of the recent challenges leaves no other option for financial institutions but to adapt themselves to the new circumstances and to be more agile for better efficiency and relevancy.

The need to transform the way banks operate, which can be defined as the traditional way of operation, was actually understood better when the innovative start-ups brought digital financial solutions into the picture. The digital products and services have proven that they can improve the business in many ways: regulatory framework, customer experience, data protection, costs, overall efficiency etc.

As the financial world is moving towards a more digitalized landscape, the regulations is becoming more formidable to ensure the safest and the most risk-free financial environment. The traditional methods used for compliance controls are no longer adequate and effective. In addition to their assistance in decreasing the compliance-related costs, the AML compliance software technologies also offer banks and financial institutions more than 50% improvement in operational workload when compared with the traditional methods.

One of the advantages of the RegTech solutions is that they can be easily integrated in the existing IT infrastructure. The cloud-based nature of RegTech actually provides companies with the best compliance offer because it enables them to monitor and track the most recent regulations in certain areas, regions or countries and manage the audits accordingly. Taking the contributions of the artificial intelligence (AI) in the AML compliance technology into consideration, which will be explained in detail in chapter 7, RegTech enables a more automated and digitized ecosystem together with the benefits of using AI in AML technology so that the financial institutions can both perform their legal obligations by minimizing the risks and maintain the trust of institution in the customer in a sustainable way.

6. All-in-one AML solutions for all institutions

4 concepts to prioritize in fighting money-laundering

1.
Know Your Customer (KYC)

2.
Real-time transaction monitoring

3.
Reporting

4.
Keep abreast of policies

The fight against the money laundering is one of the most challenging topics in the financial services industry and the traditional methods, which are manual and time-consuming, used currently in the AML (anti-money laundering) compliance procedures do not lend any assistance to make the issue any easier as they remain insufficient in combatting the money laundering activities. On the other hand, with the digitalization of financial services and new online options, the risks and threats are getting more complex and higher. In order to prevent the money laundering activities, the regulatory landscape have been readjusted with more stringent and demanding requirements from the financial institutions. In the 4th and 5th Anti-Money Laundering Directive, it is highlighted that a more detailed identity checks and a more improved understanding of customers are crucial to minimize the risk. Also, rigid customer due diligence, better control on customer identity and sharing data with central administrations are other requirements that are added.

To be able to ensure a successful AML functioning, banks and institutions need to put these 4 points at the center:

1. Know Your Customer (KYC): Collecting and storing the data about the customer's identity, citizenship, profession, source of income, financial activity etc. to help prevent and detect illegal activities like money laundering or financing of terrorism. Banks are responsible for applying the KYC procedures and for being completely compliant with KYC regulations.

2. Real-time transaction monitoring: In order to be able to interfere and prevent the money laundering activities on time, it is essential and crucial for banks to keep the surveillance processes up to date all the time.

3. Reporting: Financial institutions by law are entitled to monitor, investigate and report the suspicious transactions.

4. Keep abreast of policies: Proper risk management, training mechanisms and inspection of the controls within the institution that are demanded by the policies form the fundamental part of the AML deterrence.

Artificial intelligence (AI), by encapsulating the solution to numerous challenges in one means, has become a prominent method for the financial institutions to execute a successful AML compliance in this compelling financial environment. As for the KYC procedures, AI offers a useful identity verification system that plays an instrumental role in combating cybercrimes and remain compliant to the regulatory requirements at the same time. Also, technologies like data analytics software are conducting more frequent monitoring of the transaction than any other way while the AI technology is able to analyze and learn how to detect regular or risky behaviors by anomaly detection and clustering customers for creating intelligent profiles. For the reporting, most of the time, for an accurate one, it would be necessary to bring data together from different sections and should be analyzed. AI reduces false positives by learning user activities and decisions and detect anomalies without defining scenarios.

7. Digital KYC / CDD via integration of biometrics and AI



The benefits of AI integration in identity checking processes:

Improved verification and authentication

Enhanced detection of fraud

Cost-reduction

The financial institutions are struggling to comply with strict KYC (Know Your Customer) and AML (Anti-Money Laundering) requirements recently; however, with AI integration, related processes like identity checks and customer due diligence (CDD) are automated and processed in a shorter period of time and with much less errors. AI-powered technologies are able to conduct digital identity verifications, AML screening and real-time transaction monitoring in seconds by making sure that the documents submitted are free of any falsifications or photoshops. Biometric verification has become smarter together with the integration of AI and it is possible to prevent face spoofing tricks by 3D liveness detection.

Basically, AI integration in the processes of identity check can help with:

- Improving the speed, accuracy and scalability of ID verification and authentication
- Enhancing the of ID verification system to detect and respond to the possible fraud risks
- Cost-reduction

As the requirements of KYC and AML compliances are constantly changing and evolving, it is highly challenging for institutions to keep abreast of them unless they attain help from an AI-driven system. Natural Language Processing (NLP), a subfield of Artificial Intelligence, can read and extract meaningful details from a text which in turn assist businesses in quickly and effectively adapting to the evolving regulatory compliances. AI also offers a useful identity verification system that plays an instrumental role in combating cybercrimes and remain compliant to the regulatory requirements at the same time.

It is an undeniable fact that adopting smart biometrics and AI for digital ID verification and authentication is the cutting-edge solution for financial institutions to improve their business operations. However, the AI's contribution to fraud prevention and compliance is also highly essential because without the intelligent identity verification technology, it is probable that criminal financial activity will increase while at the same time data breaches and other security problems will occur. With the machine learning aspect, many fraudulent crimes including deceiving biometrics systems or cracking passwords are prevented and consequently customer confidence and overall experience is enhanced. So, it is important to incorporate an AI-based technology during digital onboarding process to ensure improved ID verification and Customer Due Diligence and reduce the risk of fraud and money laundering to the minimum.

8. Are AML compliance vendors ready for blockchain technology?



The features of immutability, transparency and instantaneousness of blockchain give opportunity to register data in shared accounts and to make them available in almost real-time which enables the stakeholders to be parts of the real-time processes.

Blockchain technology is one of the hot topics of the financial industry with a big potential to enhance the financial processes by increasing the availability of data, the transparency, speed and security. The technology also helps diminish the operational costs while at the same time prevent delays and failures. Among the possible uses of blockchain technology, risk management, regulatory compliance and fraud prevention are the core themes that are applicable. The features of immutability, transparency and instantaneousness of blockchain give opportunity to register data in shared accounts and to make them available in almost real-time which enables the stakeholders to be parts of the real-time processes.

In terms of compliance, the practical immutability of blockchain is one of the most appealing aspect because it basically ensures that when data is encrypted to the chain, it is not possible to alter or delete it. This feature is especially valuable for compliance because it can be used as a valid proof for the digital transaction and a record of physical property. Since blockchain's immutability also records and provides the steps of the process, it is useful in keeping track of these steps which are the needed for compliance purposes. Regulators are able to access private blockchain of financial organizations as read-only and almost real-time which gives them the chance to take an active role in the financial processes and to analyze the real-time data. In the end, the overall effectiveness of the business is enhanced with reduced time, effort and cost spent in reporting for compliance purposes.

Onboarding processes of the financial institutions require many procedures, tasks and operational work as the regulatory requirements for processes like KYC (Know Your Customer) and AML (Anti-Money Laundering) are extremely demanding and challenging. Data collection, validation, verification and confirmation steps are to be completed without any errors to prevent any financial crimes. Therefore, most of the time this process takes tremendous time and effort; however, with the immutable blockchain system, the information needed for these steps is already collected and stored in an unalterable and safe infrastructure.

Another advantage of using blockchain in regulatory compliance processes is that it is possible to use it as a digital identity management chain which stores all individual data needed for monitoring and compliance. So, processes related to KYC and AML can be automated on a market-wide level. It is possible that decentralization of all existing customer data may lead financial institutions to access to necessary information without any verification processes from the consumer side, hence more effective and secure financial infrastructure can be achieved.

With the understanding of the constructive side of blockchain in building a fully trusted and secure digital financial infrastructure, the integration of this technology has been taken more seriously and has become more widespread.

References

- Bristow, Colin. (2019, November). How is AI augmenting compliance practices?. Banking Technology (November 2019 issue).
- Buckley, Ross & Arner, Douglas & Barberis, Janos. (2016). The Emergence of Regtech 2.0: From Know Your Customer to Know Your Data. Journal of Financial Transformation. 44. 79-86. 10.2139/ssrn.3044280.
- Craig, Patrick. (2019). How to trust the machine: using AI to combat money laundering. https://www.ey.com/en_gl/trust/how-to-trust-the-machine--using-ai-to-combat-money-laundering
- Deloitte. (2016). How Agile Regulatory Technology is Helping Firms Better Understand and Manage Their Risks. https://www2.deloitte.com/content/dam/Deloitte/ie/Documents/FinancialServices/IE_2016_FS_RegTech_is_the_new_FinTech.pdf
- European Banking Federation. (2019, July 1). EBF position paper on AI in the banking industry. https://www.ebf.eu/wp-content/uploads/2020/03/EBF-AI-paper-_final-.pdf
- FindBiometrics. (2020). Enhancing Trust with AI-Driven Biometrics. <https://www.fintechfutures.com/files/2020/08/jumio-find-biometrics-ai-whitepaper.pdf>
- Gomber, Peter & Kauffman, Robert & Parker, Chris & Weber, Bruce. (2018). On the Fintech Revolution: Interpreting the Forces of Innovation, Disruption, and Transformation in Financial Services. Journal of Management Information Systems, 35, 220-265. 10.1080/07421222.2018.1440766.
- Mejia, N. (2019, October 04). AI-Based Fraud Detection in Banking – Current Applications and Trends.
- Naheem, Mohammed Ahmad. (2019). Exploring the links between AML, digital currencies and blockchain technology. Journal of Money Laundering Control, 22(3), 515-526. <https://doi.org/10.1108/JMLC-11-2015-0050>
- PWC. (2016, March). Blurred lines: How FinTech is shaping Financial Services. https://www.pwc.com/il/en/home/assets/pwc_fintech_global_report.pdf
- Raj, Deepak Amirtha. (2017). Spotlight on the Remarkable Potential of AI in KYC (Know Your Customer). KD Nuggets, 17 (26). <https://www.kdnuggets.com/2017/07/spotlight-remarkable-potential-ai-kyc.html>
- Samuelson, Robert J. (2020). What Crash 2020 Means. Washington Post. <https://www.washingtonpost.com/opinions/2020/03/11/what-crash-2020-means/>
- Stanford, Jim. 2008. Economics for Everyone.

Contact Us

Get in touch with our industry expert executives for further details.



 **Tuncay Çoruh**
Product Manager
tuncay.coruh@fineksus.com



 **Murat Kurtulmuş**
Implementation & Support Manager
murat.kurtulmus@fineksus.com



 **Necati Yavaş**
Sales Director
necati.yavas@fineksus.com



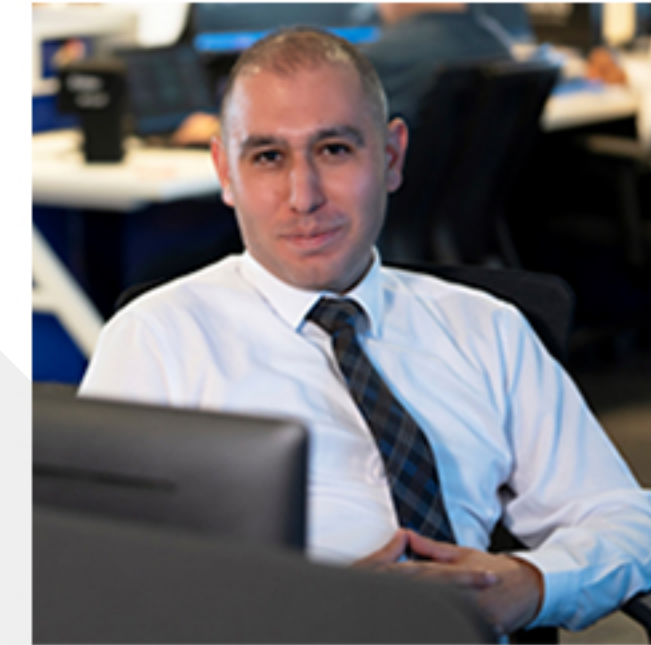
 **Serkan Arslan**
Head of Sales, MENA
serkan.arslan@fineksus.com




 **Gökçe Gence**
Head of Solution & Project
gokce.gence@fineksus.com



 **Burçin Güney**
Account Manager
burcin.guney@fineksus.com



 **İbrahim Başer**
Software Success Supervisor
ibrahim.baser@fineksus.com

About Us

Milestones

Fineksus was founded in Istanbul, Turkey in 2002 as a software and professional service provider to deliver technical consultancy, outsourcing services, standalone / SaaS AML and payment software solutions for banks, brokers and corporations. In the beginning of 2013, Fineksus started managing its ongoing GCC Region operations at its new office in Dubai, UAE.

Fineksus is the market leader of compliance and financial messaging solutions in Turkey by providing its products and services for more than 95% of the banking industry, and aims to expand its offerings global wide which makes the company at the forefront for providing AML solutions and financial messaging tools.

PayGate™ Suite as AML trademark

Fineksus provides products and services across 29 countries from Hong Kong to the UK with offices in Istanbul, Dubai and Qatar. By meeting ever-changing demands of RegTech industry with 18 years of know-how, Fineksus develops cutting edge tools to bring value for more efficient and effective way of AML compliance and financial messaging. PayGate™ Compliance package covers all the fundamental operations based on AI and machine learning to maintain surveillance of financial systems.



PayGate™ KYC
Know your customer.
Know your risk.



PayGate™ Analyzer
Next generation
transaction monitoring.



PayGate™ Inspector
AI-powered blacklist
filtering.

Follow us on
Social Media!



www.fineksus.com

[Request a Demo](#)

Copyright © 2020 Fineksus

All rights reserved. No part of this publication may be reproduced, stored in a retrieval system, or transmitted, in any form or by any means, electronic, mechanical, photocopying, recording, or otherwise, without the prior permission of the copyright owners.