

Regtech Transforms the Financial Crimes Ecosystem

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A revolution in regulatory technology (regtech) that addresses compliance challenges in the financial services sector has created the opportunity for a “new normal” in anti-money laundering (AML) and sanctions compliance. Artificial intelligence (AI), machine learning, data analytics, and other tools and methods are driving more efficient programs by automating the collection of data used to investigate and identify potentially suspicious activity, evaluate customer risk, and detect and prevent financial crimes. Institutions that lack the knowledge and experience to correctly implement regtech can incur significant costs.

The Growth of Regtech

The number of vendors pushing AI and machine learning has grown dramatically in recent years, and these vendors are expanding into the banking compliance arena. Institutions interested in adopting such solutions have no shortage of vendors from which to choose, but they often are unclear about how to select one, in part because of uncertainty about their own needs.

Many banks quickly realize that single-vendor platforms might not be sufficient and that they need to add a variety of tools to build effective AML and sanctions compliance technology platforms. Although a few leading vendors sell single platforms with several modules, the marketplace is shifting its focus to an ecosystem with multiple applications to enhance existing platforms. For example, a bank with a transaction monitoring system that triggers alerts and a case management system that manages the evaluation of potentially suspicious activity might add a solution that sits between the two and automates the collection of data used in the investigation process.

In this evolving environment, banks face the vexing decision of whether to continue with current vendors and add unproven modules or to turn instead to smaller vendors with proven solutions using new platforms. Banks can also struggle to hire the staff they need to identify the best solution and to work closely with outside vendors. The pool of candidates that can deliver on both the AML and technical expertise necessary is, to put it mildly, limited.

The Translation Dilemma

The lack of internal expertise qualified to select and work with vendors is not the only potential problem for banks hoping to take advantage of the advances in regtech to improve their compliance programs. Banks also need assistance managing the response of regulators to enhanced black-box technology and explaining AI-based decision making to regulators.

Like the technology itself, regulatory reaction is evolving. Regulators are adapting to this new frontier in compliance by actively engaging with technological innovations and hiring examiners with the requisite expertise.

For their part, vendors are tackling the nagging gap between technological capabilities and regulatory acceptance, including minimizing machine learning in favor of process automation and simplifying concepts for greater ease of review. Rather than starting with complex machine learning algorithms, vendors are phasing in AI techniques, beginning with data aggregation and cleansing activities. After these foundational AI elements are in place, financial institutions can move up through the spectrum of AI solutions to the more complex techniques.

The Revolution Is Here

So how should banks proceed? First, they should establish an enterprise data strategy with the end goal of creating a single source of record. The enterprise data strategy serves as the foundation upon which all regtech solutions are built, and it provides the infrastructure necessary to adapt to future advancements in the regtech space. Second, banks should realize that the time to start the integration of these solutions into their ecosystems is now. Banks should build relationships with vendors by starting with less risky automation of data collection and prepare for the introduction of the more advanced and risky capabilities.

The complex regtech environment is difficult to navigate. But regulators' efforts to develop a more comprehensive understanding of how technology can enhance financial institution compliance—and vendors' efforts to make it easier for them to do so—are clear signs that the regtech revolution is here to stay.



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