STRONGER TOGETHER.

WHAT DOES IT TAKE FOR FINANCIAL CRIME COMPLIANCE UTILITIES TO SUCCEED?

Select the right scope, standardise, leverage new technologies, set the right expectations and … 'Think big, Start small, Scale fast'

According to recent Celent estimates, the financial community spends around 30 billion USD every year at global level to fight financial crime. All players (financial institutions, fintechs and increasingly corporates as well) massively invest at individual level to comply with increasingly complex and far-reaching regulations, often with unintended negative side-effects in terms of end-customer experience and pace of innovation. And yet, the outcome is still really disappointing. It is estimated that only 1% of financial crime is actually prevented.

Industry collaboration has the potential to drastically improve effectiveness and efficiency of those processes. The idea is therefore rightfully promoted by the financial community, with the ambition to implement local, regional or global financial crime compliance utilities.

Yet, succeeding in implement these utilities is not easy. One can however learn from past successes and failures and identify the key success factors.

Potential benefits of Utilities

When successful, Utilities can offer multiple advantages to the institutions involved:

- **Higher efficiency**. Provided that the scope of the Utility is one that allows for de-multiplication of tasks, cost efficiency can be massive. As example, for traditional correspondent banking business, where on average every bank has around 100 correspondents, a centralised Know Your Customer (KYC) process can easily achieve 10x savings.
- **Access to best-of-breed technology solutions and talents**. Beyond the efficiency gains, Utilities benefit from significant cost mutualisation and scale economies allowing to invest in and benefit from best-of-breed technology solutions and also access to leading industry resources and skills.
- **Higher standardisation and innovation**. When designing Utilities, institutions need to agree on common processes and practices, which in turn will allow for the emergence of standards (e.g., agreement on the list of documents to request for account opening). This standardisation - as observed in many industries – also subsequently acts as a key enabler for innovation. It is indeed easier (and economically more appealing) to develop new innovative solutions when standards are being used in the market as it maximises the number of players that can benefit from the innovation.

- **More effective compliance**. When institutions work together to create a Utility, they rightfully tend to go for a high bar, by sharing best practices and deriving a process and modus operandi, which take the best of the individual institutions' existing processes. This allows to cost-efficiently raise the bar for the whole community.

Key success factors

Not all financial crime compliance Utilities attempts have been successful though and unfortunately some institutions had negative experience from failed Utilities, for instance in the field of KYC for securities firms or KYC for domestic retail customers. Yet, successes and failures have now allowed to clearly identify the key success factors for such Utilities:

1. **Aim to mutualise a process that allows for significant synergies and scale economies**. As an example, a regional KYC Utility for international corporates will be more likely to succeed than a KYC Utility for domestic retail clients. Indeed, international corporates have more banking relationships than domestic retail customers and often require a more complex on-boarding process, therefore allowing for higher savings through mutualisation.
2. **Standardise extensively**. Gains from Utilities will only be achieved if the outcome of the Utility work can be integrated easily in the existing processes of the institutions using the Utility. If every single institution still needs to significantly rework the outcome of the Utility to adapt it to its own processes and policies, the benefits of mutualisation will vanish quickly. Standardisation toward the highest level of compliance is the only way forward to succeed.
3. **Select best-of-breed technologies**. Selecting the most recent technologies, partnering with innovative companies and adopting a best-of-breed eco-system approach will be instrumental to unlock the expected savings and effectiveness benefits and make it even more attractive for institutions to join. Desire to challenge the status quo and incumbent technologies and processes is key.
4. **Set the right expectations – no shift of liabilities**. Even if this would be ideal, there is no hope that financial institutions would be able to shift their liabilities to Utilities. Regulators will continue to hold individual institutions accountable. Yet, that does not prevent financial institutions from leveraging these Utilities by implementing appropriate controls, as they would do for any outsourced process.
5. **Think big, start small, scale fast**. Utilities must have a compelling and bold vision to incentivise financial institutions to let go their existing individual processes and embrace a common vision and utility. Yet, too ambitious Utilities will face so many issues in their early stages that they will fail to build momentum. Selecting and sticking to a contained scope first, quickly prototyping, demonstrating success and then scaling up fast is an effective way to ensure success.

Regulatory support

In a number of countries, regulators have shown support for such Utilities. This is driven essentially by their desire to improve both the end-customer experience (often heavily impacted by individual banks' processes) and the overall effectiveness of the fight against financial crime. In addition, in Europe for instance, The European Banking Authority (EBA) has published Guidelines on Outsourcing arrangements, which define the rules and expectations for financial institutions to outsource activities to service providers. Such guidelines provide the right context for more Utilities to emerge.

It is only the beginning

We are still in the early days of Utilities and the successful Utilities that have emerged have only covered limited use cases so far, often focused on Know Your Customer (either at global or regional levels) or Transaction monitoring (like the recent Dutch initiative).

Many more potential use cases can already be identified, like the screening of international payments. A typical international payment currently involves on average three financial institutions, and often many more. Each of those institutions screens the same transaction against essentially the same sanctions lists. Why would a Utility not rather orchestrate a process that would screen the international payment only once, against the strictest standards shared by the institutions involved in the transaction and dispatch the alerts among those institutions? Efficiency and user experience would improve substantially.

Likewise, the painful process – during on-boarding or regular risk assessment of corporate clients – of identifying ultimate beneficiary owners and screening those against sanctions or politically exposed people lists would be another good candidate for mutualisation.

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