Information paper

Overcoming AML challenges in correspondent banking

Advanced data analytics plays critical role in supporting compliance and enhancing transparency
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Executive summary

Correspondent banking plays a crucial role in the global financial system, facilitating global trade and investment flows and enabling individuals and businesses to access products and services which might otherwise be unavailable to them.

However, as regulators and governments combat money laundering and terrorist financing, they are introducing more stringent rules for correspondent banks – accompanied in some cases by hefty fines and complex remediation processes.

These factors challenge the parties in a correspondent banking relationship in different ways. Stricter regulatory requirements and the threat of significant fines have prompted global transaction banks, which provide services to regional and domestic banks, to adopt a more rigorous approach to their own compliance measures, resulting in additional costs. Global transaction banks have also increased their expectations regarding their counterparties’ compliance measures.

In some cases, these developments have prompted large banks to terminate some of their correspondent banking relationships in an exercise known as de-risking. Banks may adopt this approach if their respondent customers lack sufficient volume, are located in higher risk jurisdictions or cannot show they have the right controls in place. When relationships are terminated, regional and domestic banks may find that they are no longer able to provide overseas payments services, with negative consequences for them and their customers.

In general, banks of all sizes with correspondent banking activities have seen compliance costs become prohibitive. Beyond this, global clearing banks often expect their respondents to comply with regulation in the global banks’ home jurisdictions. This means respondents in developing markets may have to comply with requirements that are stricter than those mandated by their own local regulators.

In both cases, utility solutions can help reduce costs and level the playing field by facilitating the development of global compliance standards and best practices.
Challenges for large correspondent banks

The challenges associated with anti-money laundering (AML) activities are more arduous than ever before. Banks have to go to considerable lengths to identify a small number of suspicious or illicit transactions from amongst the millions of legitimate transactions processed each day. “The best analogy that I’ve heard around AML is that you are trying to find one rotten tree in a forest in the size of the Amazon,” comments Anthony Fenwick, Global Head of AML for Treasury and Trade Solutions at Citi. “This makes it very difficult to identify the few problematic payments in a cost-effective way.”

In this climate, correspondent banks face a number of specific challenges around AML compliance.

Lack of purpose-built monitoring solutions

The AML monitoring systems typically used by large correspondent banks were often developed for retail banking. These monitoring systems tend to look at payment instructions in and out of customer accounts in order to detect anomalies in behaviour. They do not always take into consideration the complexity inherent in the correspondent banking model. Unlike retail banking, correspondent banking AML needs to consider entire payment chains, paying specific attention to the countries and counterparties involved. This means looking at the upstream and downstream banks in the payment chain, as well as where those banks – and the individuals or organisations moving the money – are located.

High volumes of false positive alerts

Existing AML monitoring systems also tend to generate high volumes of false positive alerts – and low volumes of worthwhile alerts. The result is not only massive cost for the industry, but the very real danger of missing truly illicit transactions in a forest of “false positive alerts.” Ultimately, the model may fall short of the underlying goal of AML – protecting the integrity of the financial system, cutting off the resources available to terrorists, and making it more difficult for those engaged in crime to profit from their criminal activities.

Use of indirect structures

For global clearing banks, challenges can also arise as a result of the indirect structures adopted by some domestic and regional banks in order to act as aggregators for smaller banks that no longer have access to major clearing services due to “de-risking” exercises. This type of structure, which involves downstream clearing or nested relationships, can make it more difficult for the global clearing banks to identify and monitor such indirect activity. It may also mean that banks need to deploy additional resources to identify whose payments are being processed.

Challenges for domestic and regional banks

Domestic and regional banks also face challenges where AML monitoring is concerned. The AML systems and processes which can benefit the world’s largest banks may not be necessary or appropriate for smaller domestic or regional banks – and vice versa.

Smaller institutions are typically quite varied in their approach to AML, using a mixture of internally-built systems and vendor solutions. Although such banks do need robust AML processes and tools, for cost reasons they may put a greater emphasis on human intervention. Future technological developments and utility solutions may give smaller banks additional opportunities to reduce the compliance costs through more efficient and effective data-driven approaches.

Addressing the challenges

AML does present challenges for correspondent banks of all sizes. However, some of these could be addressed more effectively by making better use of analytics in the area of compliance, as well as by providing specialised, robust training for compliance professionals.

Separate systems

For one thing, banks are increasingly moving away from a one-size-fits-all approach in terms of their monitoring systems. Instead, they are complementing their main scenario-based solutions with additional point solutions, recognising the benefits of having separate systems in place to cover their monitoring for correspondent banking, retail and trade flows, as well as market platforms.

Data analytics

As correspondent banks look for ways to manage risk and identify problematic transactions in a more targeted and efficient way, one development that looks promising is data analytics. Without data analytics, an AML transaction monitoring system will simply issue alerts generated at transactional level, which then all need to be analysed manually.

On the other hand, data analytics can help by identifying and prioritising areas which the bank may wish to investigate further – for example, by examining patterns of transactions between different jurisdictions, applying risk scoring, and then tasking a human analyst with carrying out the final part of the exercise. This can give banks better information about their exposures and a clearer understanding of how their networks operate.

Compliance Analytics from SWIFT is a data analytics tool that many of the world’s largest correspondent banks use to gain a global view of their activity across all group entities. Institutions can use the tool to understand their exposure and activity share in high-risk countries and payment corridors, as well as to generate alerts flagging up unusual behaviour or possible policy breaches.

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“Before I had Compliance Analytics, if I wanted to look at our transaction flows with a certain institution, it might take days or even weeks to collect, standardise and analyse the data. Now I can turn on my computer and access that data immediately. I can also share the data globally because it doesn’t have the remitter/beneficiary information so there are no data privacy issues."

Knowledge and training

While data analytics can enhance AML processes by carrying out the heavy lifting, human intelligence also plays an important role in completing the exercise. As such, it is essential to employ well-trained compliance professionals who understand the business environment. The international payments landscape is highly complex: while some countries have open currency regimes, others have currency controls in place whereby government approval is needed before overseas payments can be made.

“Correspondent banking is simple at 30,000 feet, but complicated at ground level unless you really understand the nuances of certain countries,” comments Fenwick.

SWIFT messages (including MT 103, MT 202 and MT 202COV) play a vital role in correspondent banking activities. Compliance officers will therefore need to understand these messages in some detail, including the way that bad actors have tried to manipulate message details in order to circumvent AML monitoring. In today’s fast-paced environment, having the requisite knowledge and tools to identify potential issues is crucial in order to ensure timely reporting and action.

Understanding local market practice is also important. For example, some countries stipulate that local banks need to seek regulatory approval before they can respond to requests for information (RFIs) issued by their correspondents. High volumes of RFIs can lead to considerable delays in receiving the necessary information.

This means that correspondent banks need to be judicious when sending queries to banks in these markets – not by avoiding sending queries, but by making sure they are asking the right questions.

All of this requires robust training and knowledge. In some markets for example, daily transaction limits mean that it is not unusual for a large payment to be split into a number of smaller payments which are then sent on consecutive days. While splitting large payments into smaller amounts may be done to launder money, experienced analysts with a clear understanding of the local market practices will take these into account when deciding whether or not to issue an RFI. By ensuring that the RFIs they do send are appropriate and justified, banks can avoid unnecessary delays, improve customer interactions and reduce the burden faced by foreign banks. As a result, correspondent banks are increasingly recruiting former business people with a thorough understanding of the business environment and are training them to fulfil key compliance roles.

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Collaborative solutions
As regulators increasingly focus on transparency and on applying AML processes to counter terrorist financing, there is growing interest in industry solutions that streamline correspondent banking AML. With the world’s banks set to spend $8 billion on AML monitoring this year according to figures from WealthInsight, there is a lot to gain by increasing efficiencies in this area.

Collaborative solutions such as SWIFT’s Correspondent Monitoring service have much to offer. Part of SWIFT’s Compliance Analytics portfolio, Correspondent Monitoring is purpose-built to help banks fulfil their AML obligations specifically for their correspondent banking activities. The analysis focuses on the international payments that go over the SWIFT network.

“This is all about breaking up the AML monitoring ‘black box’ by adopting point solutions that focus on specific areas of risk,” says Brigitte De Wilde, Head of Financial Crime Intelligence and Services, SWIFT. “SWIFT is in an ideal position to do this for correspondent banking, as the majority of correspondent banking transactions are conducted using SWIFT.”

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Head of Financial Crime Intelligence and Services
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**Conclusion**
While utility solutions can help banks overcome AML challenges, the path to improvement is not necessarily straightforward. Opportunities for greater transparency and efficiency are emerging, but may require banks to re-engineer the way in which they receive and analyse data.

“Banks need to try and turn the super tanker around so that they can send it in a different direction,” Fenwick observes. “This will involve spending a lot of time re-tooling and changing certain processes and interactions.”

In practice, banks may also need to run parallel processes in order to keep using existing monitoring systems while other options are being developed. Analytics and the extended use of utility solutions could additionally be used to help tune/focus existing AML solutions to be more effective in their detection capabilities.

In this way, banks may be able to begin harnessing the power of analytics and utility solutions while making the necessary changes behind the scenes.

Correspondent Monitoring takes a top-down approach, looking at each institution’s global SWIFT transaction activity based on the counterparties they do business with, their message flows and any nested relationships. This holistic view enables correspondent banks to apply a risk-based approach to their AML compliance programmes.

Brigitte De Wilde
Head of Financial Crime Intelligence and Services
SWIFT

Advanced analytics solutions
With advanced analytics playing an ever-growing role in compliance programmes, SWIFT’s Compliance Analytics portfolio helps correspondent banks leverage their SWIFT message data to identify, monitor, analyse and address potential sanctions, know your customer (KYC) and AML compliance risks.

Correspondent Monitoring helps you apply a risk-based approach to correspondent banking AML by highlighting higher-risk payment flows with specific counterparts for additional monitoring and investigation. When you identify an area of concern, you can use Compliance Analytics to drill down further into the data to gain a more complete picture of activity involving specific counterparties and their banking groups.

Compliance Analytics helps you uncover anomalies in payment flows, unusual patterns or trends, hidden relationships, and consistently high levels of activity with high-risk countries and entities. You can compare your message traffic with global aggregated SWIFT traffic, highlighting for example your share of payments traffic in high-risk countries.

For more information, visit www.swift.com/correspondentmonitoring or contact your SWIFT account manager.

About SWIFT

SWIFT is a global member-owned cooperative and the world’s leading provider of secure financial messaging services.

We provide our community with a platform for messaging, standards for communicating and we offer products and services to facilitate access and integration; identification, analysis and financial crime compliance.

Our messaging platform, products and services connect more than 11,000 banking and securities organisations, market infrastructures and corporate customers in more than 200 countries and territories, enabling them to communicate securely and exchange standardised financial messages in a reliable way. As their trusted provider, we facilitate global and local financial flows, support trade and commerce all around the world; we relentlessly pursue operational excellence and continually seek ways to lower costs, reduce risks and eliminate operational inefficiencies.

Headquartered in Belgium, SWIFT’s international governance and oversight reinforces the neutral, global character of its cooperative structure. SWIFT’s global office network ensures an active presence in all the major financial centres.

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