THE STATE OF SCREENING

2019

Alert Volumes, Regulatory Scrutiny, and Machine Learning

enigma

You need benchmarks.

Sanctions and AML leaders have a critical need for cross-institutional benchmarks for sanctions, politically exposed person (PEP), and negative news screening programs. Program leaders face challenges in trying to understand how their screening program performance compares to those at peer financial institutions. Without this visibility, program leaders can neither fully assess their program's performance, nor can they make strategic program decisions with confidence.

This report has them.

Enigma created The State of Screening to put valuable data into the hands of program leaders and to increase visibility into shared challenges and solutions. The included benchmarks are based on survey responses from program leaders representing a wide range of financial institutions. This report is designed to help you better assess your program performance, set informed performance goals, and make more confident decisions about your program strategy in 2020 and beyond.

About the Survey

INSTITUTION SIZE

CUSTOMER BASE IN MILLIONS	NUMBER OF RESPONDENTS
<1M	18
1M - 5M	3
5M - 10M	4
10M - 20M	1
20M - 30M	4
30M - 40M	6

This report uses insights from a fall 2019 survey of 36 respondents, 64% of whom represent institutions based in the United States. Institution size varied: 50% of respondent financial institutions have fewer than 1 million customers, while roughly 38% of respondent institutions have 20 million or more customers.

RESPONDENT COMPOSITION

TITLES	NUMBER OF RESPONDENTS
Chief Compliance Officer	17
(Global) Head Financial Crimes Compliance	8
BSA/AML/OFAC Officer	3
Regional Head Financial Crimes Compliance	2
Chief Risk Officer	1
Other	5

Chief Compliance Officers and Chief Risk Officers account for 50% of survey respondents, with remaining respondents representing a range of financial crime, AML, or OFAC leadership positions. Respondents oversee programs of various sizes, but roughly half of respondents employ more than 100 full-time employees to conduct sanctions, PEP, and negative news screening and investigations.

42%

of institutions experience higher sanctions alert volumes than they did a year ago.

Transaction screening rates for sanctions, PEP, and negative news reflect significant accuracy challenges.

42% OF RESPONDENTS REPORTED ALERT RATES OF 11% OR HIGHER	53% OF RESPONDENTS REPORTED FALSE POSITIVE RATES OF 76% OR HIGHER

Customer screening alert rates for sanctions, PEP, and negative news trend lower, but false positive rates remain high.

44% OF RESPONDENTS REPORTED ALERT RATES OF 3-5% OR HIGHER	50% OF RESPONDENTS REPORTED FALSE POSITIVE RATES OF 76% OR HIGHER

70%

of institutions agree that they experienced increased regulatory scrutiny with respect to their sanctions compliance program.

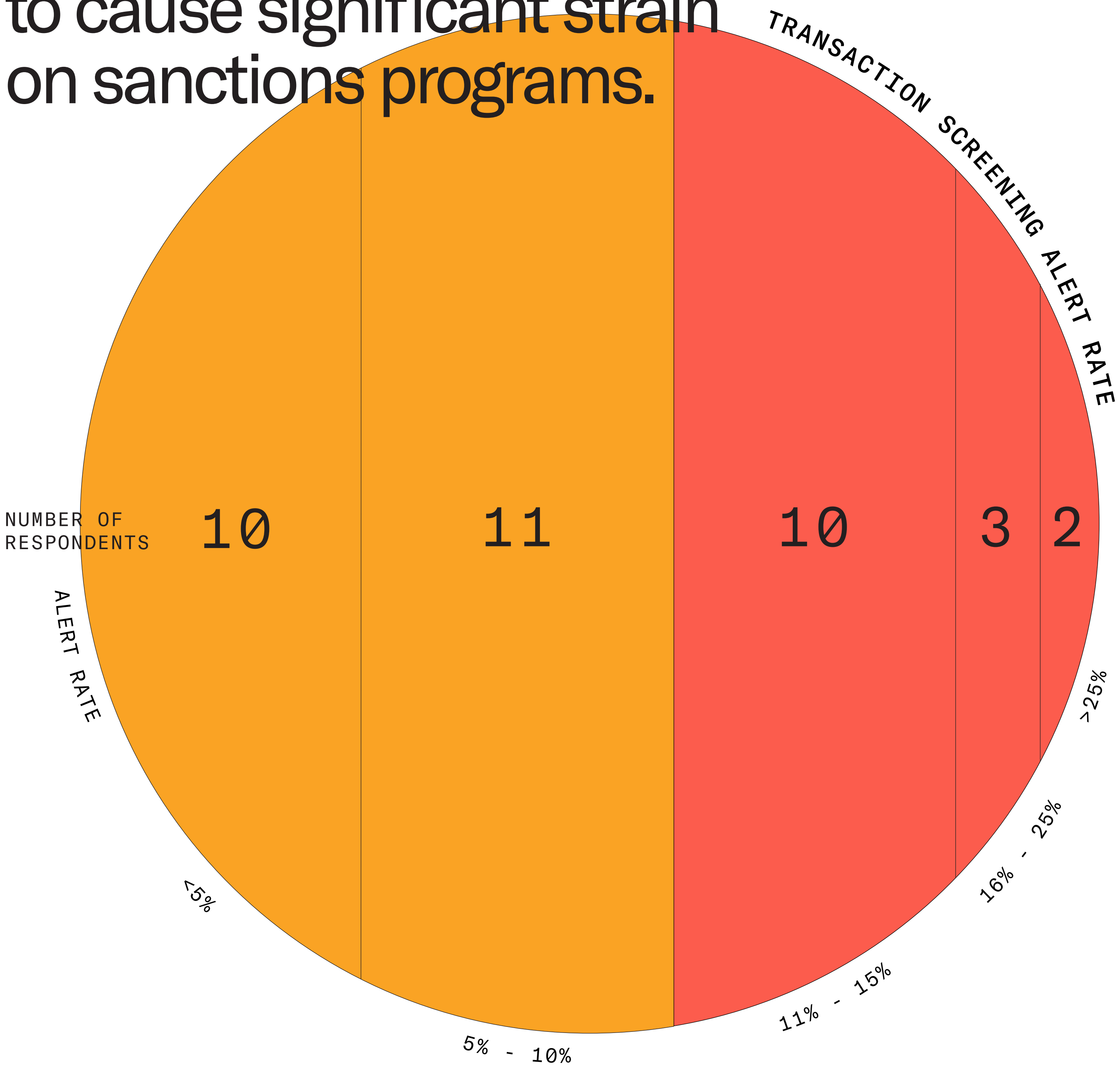
36% of institutions strongly agree that their sanctions compliance program experienced increased regulatory scrutiny.

81%

of institutions are exploring, ready to deploy, or already using machine learning for sanctions screening.

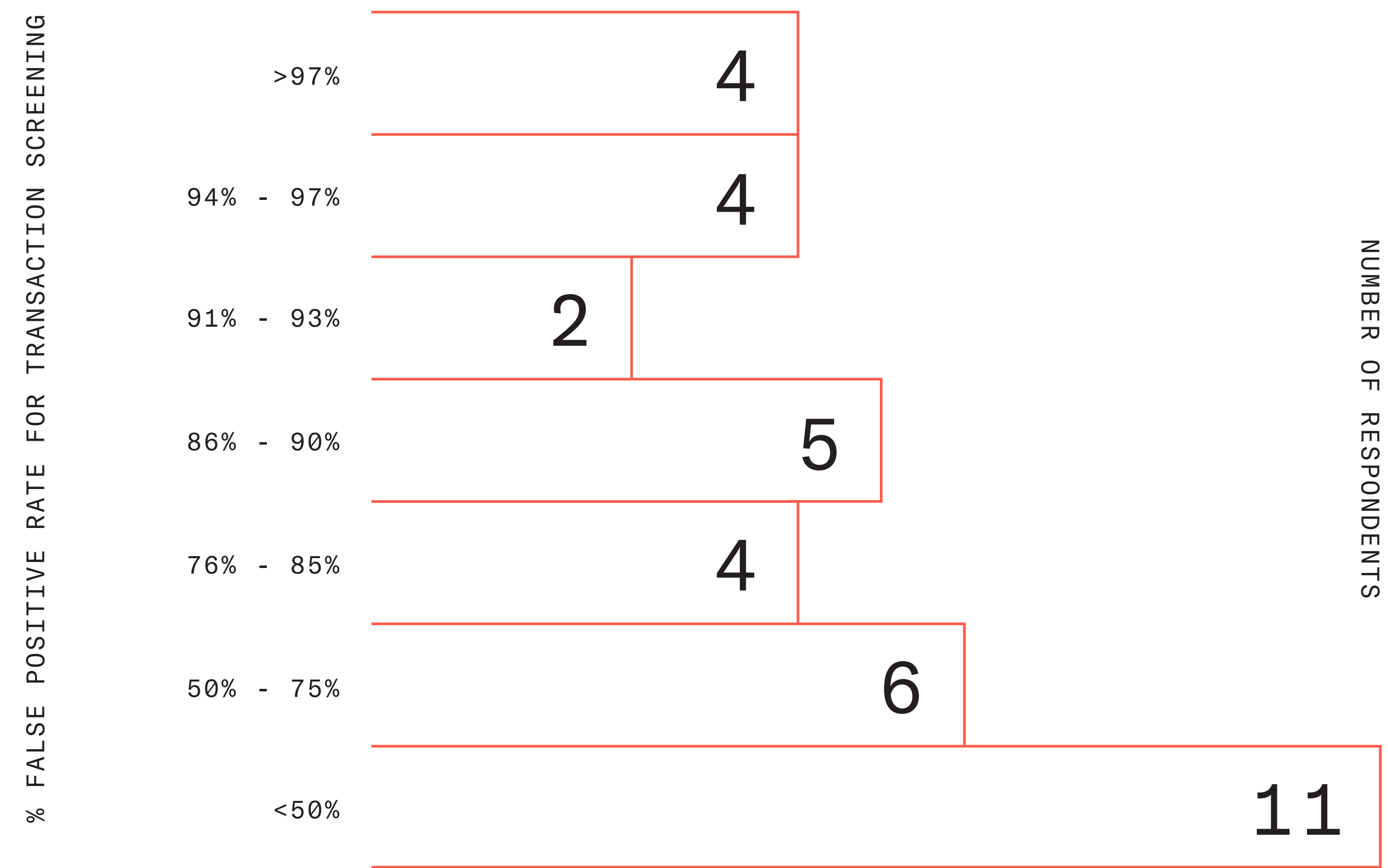
17% of institutions have already built or deployed machine learning capabilities.

Alert volumes continue to cause significant strain on sanctions programs.



One of the more worrying trends we identified is that 42% of institutions are experiencing higher sanctions alert volumes (including customer and transaction screening) than they were a year ago. The shift in alert volumes is primarily one-directional, as only 14% of institutions definitively reduced sanctions alerts last year. We know that many institutions have invested in alert volume reduction, yet these numbers reveal that nearly 50% of institutions are worse off this year than they were last.

TRANSACTION SCREENING FALSE POSITIVE RATE



Increasing alert volumes, combined with sustained high false positive rates, signal pervasive accuracy challenges. Transaction screening is more problematic than customer screening, with nearly half of institutions reporting transaction screening alert rates of 11% or higher. Given that 25% of institutions process at least 1 million transactions annually, and 33% process more than 10 million transactions annually, many institutions are facing hundreds of thousands, if not millions of sanctions alerts each year. These numbers indicate an urgent need for institutions to improve screening accuracy.

Across both transaction and customer screening for sanctions, PEP, and negative news, false positive rates are high. Half of respondents are finding more than 76% of alerts to be false positive after an initial ("level 1") review and about a third of respondents find more than 91% of alerts to be false positive after an initial review. These figures again reveal deep accuracy challenges in existing screening processes that cause these high false positive rates and related alert volumes.

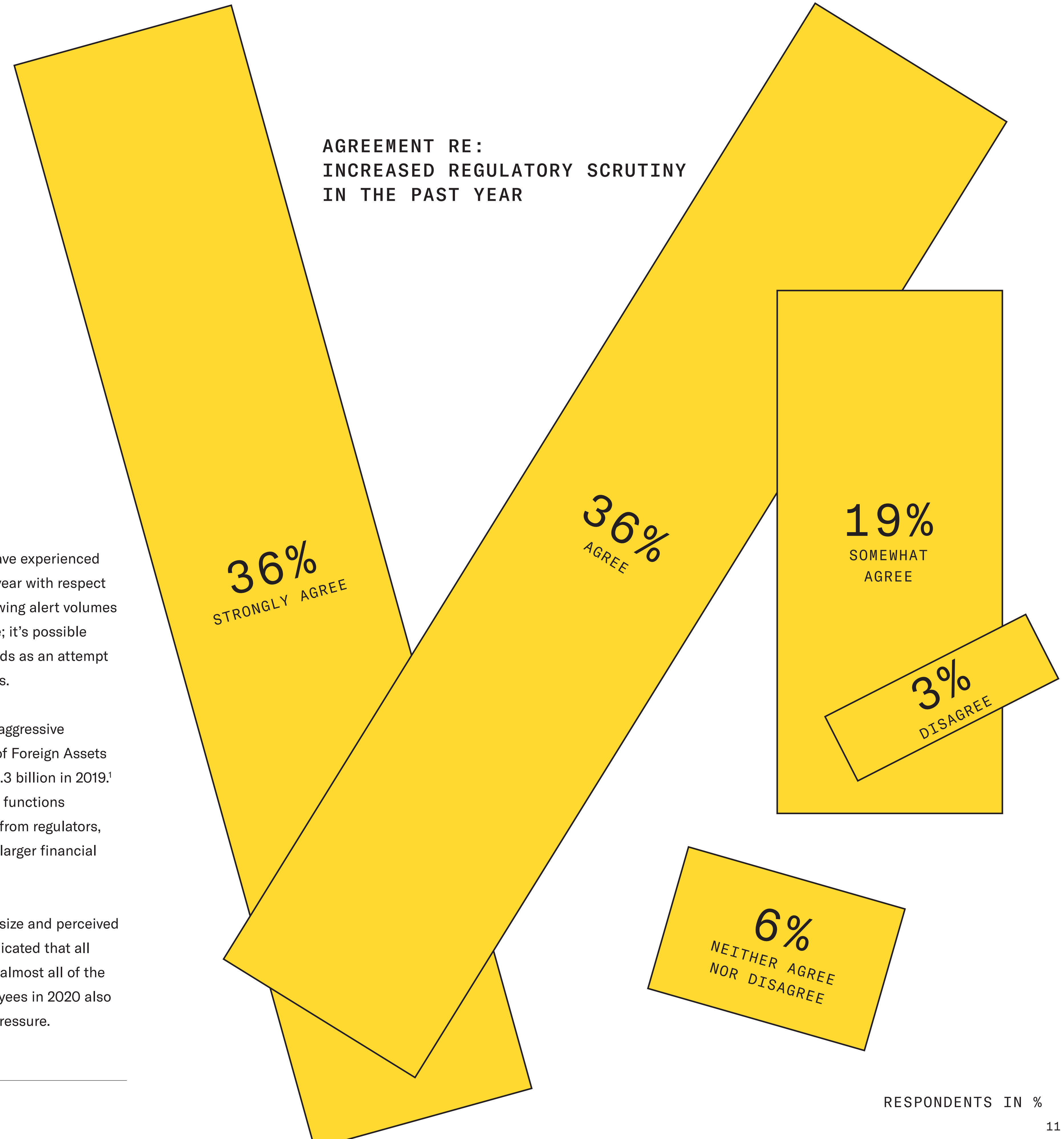
To manage sanctions screening alert rates, 61% of program leaders plan to hire full-time employees or external contractors in 2020, proving that the strain of alert volumes significantly affects program staffing and costs.

Regulatory scrutiny of sanctions programs is on the rise.

Nearly 70% of institutions agree that they have experienced increased regulatory scrutiny over the past year with respect to their sanctions compliance program. Growing alert volumes could reflect heightened regulatory pressure; it's possible institutions are widening screening thresholds as an attempt to prove the rigor of their screening practices.

Increasing regulatory pressure also reflects aggressive regulatory enforcement in 2019. The Office of Foreign Assets Control has issued fines totaling a record $1.3 billion in 2019.[1] As one respondent comments, "Compliance functions are certainly undergoing increased scrutiny from regulators, particularly in the light of many scandals at larger financial institutions."

There were no trends in terms of institution size and perceived regulatory scrutiny, rather the responses indicated that all sizes of institutions felt this strain. Notably, almost all of the institutions that plan to add full-time employees in 2020 also identify as experiencing greater regulatory pressure.

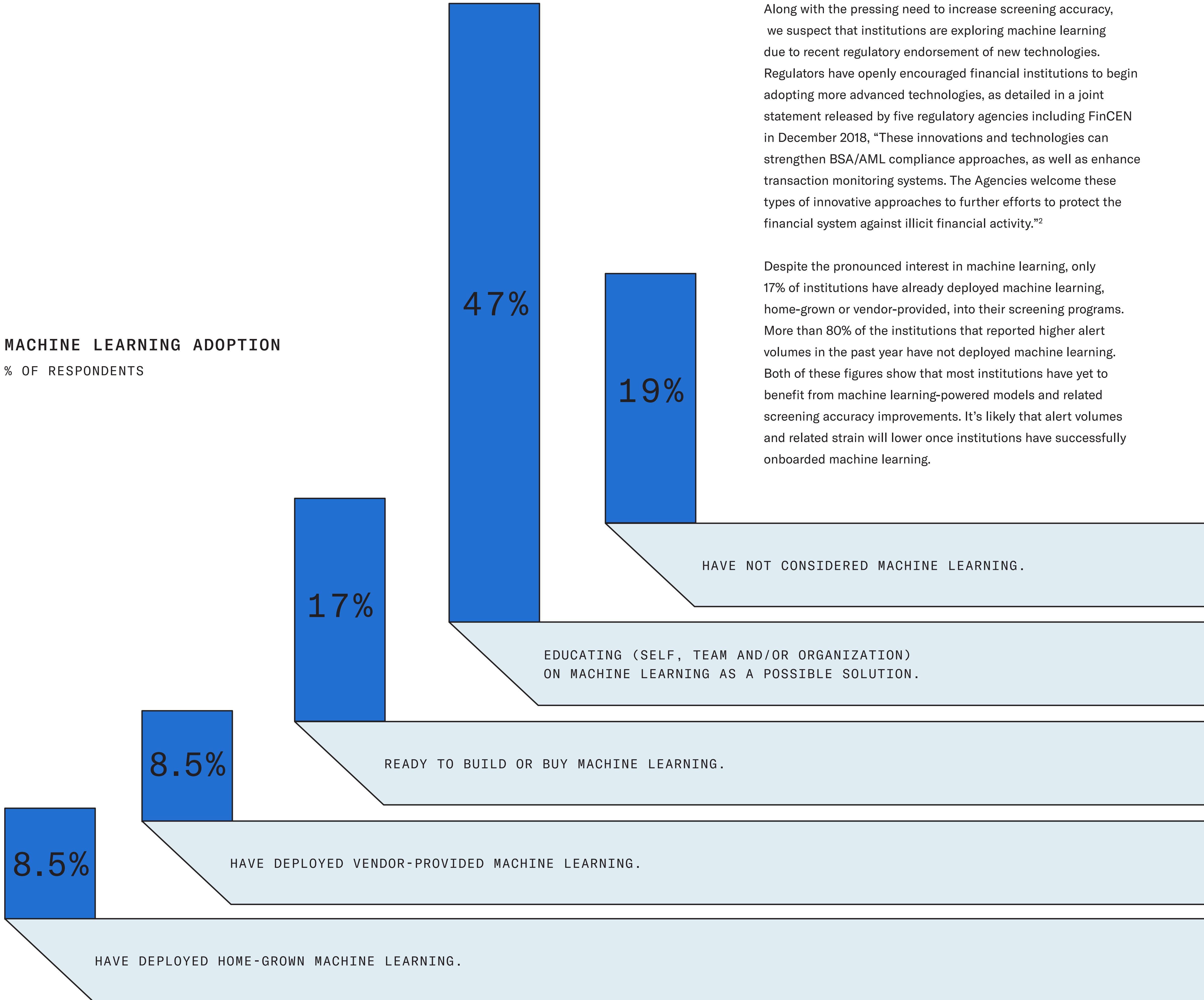


[1] U.S. Sanctions Compliance Fines Hit Decade High, *The Wall Street Journal*, July 25, 2019

The majority of institutions are turning to machine learning.

Program leaders view machine learning as a solution for sanctions program challenges. 81% of respondents identified as exploring machine learning, ready to build or buy machine learning, or already using machine learning. Deploying machine learning can address high false positive rates and increasing alert volumes, and can be a strategy for engaging with increasing regulatory scrutiny.

Multiple program leaders listed machine learning as the number one change they would make to their current sanctions compliance program or technology. Several noted wanting to use machine learning in initial screening processes to reduce false positive rates and alert rates.



Along with the pressing need to increase screening accuracy, we suspect that institutions are exploring machine learning due to recent regulatory endorsement of new technologies. Regulators have openly encouraged financial institutions to begin adopting more advanced technologies, as detailed in a joint statement released by five regulatory agencies including FinCEN in December 2018, “These innovations and technologies can strengthen BSA/AML compliance approaches, as well as enhance transaction monitoring systems. The Agencies welcome these types of innovative approaches to further efforts to protect the financial system against illicit financial activity.”[2]

Despite the pronounced interest in machine learning, only 17% of institutions have already deployed machine learning, home-grown or vendor-provided, into their screening programs. More than 80% of the institutions that reported higher alert volumes in the past year have not deployed machine learning. Both of these figures show that most institutions have yet to benefit from machine learning-powered models and related screening accuracy improvements. It’s likely that alert volumes and related strain will lower once institutions have successfully onboarded machine learning.

[2] **Joint Statement on Innovative Efforts to Combat Money Laundering**
Financial Crimes Enforcement Network, December 3, 2018

Conclusion

It would be easy to review this report's statistics and feel concerned about the state of sanctions, PEP, and negative news screening programs at financial institutions. The combined strain of increasing alert volumes and regulatory scrutiny indicate that screening program leaders face significant challenges as they seek to maintain compliance. Yet we're also seeing a growing trend in empowerment amongst institutions as they pursue machine learning in great numbers. If institutions continue to capitalize on technological advancements, these same benchmarking metrics could look very different in the years to come.

ABOUT ENIGMA

Enigma is focused on making risk frictionless so that our customers can focus on growing their businesses and radically improving their products and experiences.