COVID-19 implications: navigating the impacts of the pandemic on financial crime compliance

Minds made for protecting financial services

Introduction

The COVID-19 pandemic has triggered unprecedented change, forcing major lifestyle adjustments and turbulence in the financial markets. Financial crime across the globe is expected to rise in response to the uncertainty[1] resulting from the ever-changing landscape. Organizations must work together to mitigate financial criminal activity and adapt processes and controls, not only to meet regulatory requirements but also to support customers, while protecting the financial system and minimizing negative impacts on society.

This has also been highlighted in the 2020/21 FCA Business Plan. It's immediate focus has been on: protecting the most vulnerable in society, highlighting the increased risk of scammers looking to exploit the situation and remaining vigilant to potential misconduct in the financial markets.

Organized crime will diversify, and organizations across all sectors will need to adapt to manage new risks

The simultaneous supply and demand shocks to the global economy, and widespread closure of borders across the world, are dramatically impacting the ability of organized crime groups to continue normal operations. According to the think tank Royal United Service Institute (RUSI), organized crime groups will not stop; instead, they will diversify rapidly to negate the restrictions imposed by COVID-19. The financial services industry therefore has a responsibility, more so now than ever, to ensure that financial crime compliance remains a focus and adverse impacts to society can be limited at an already challenging time.

Despite the challenges, financial services will play a crucial role

In the current climate, financial services has a critical role in providing financial stability, enabling relief from humanitarian organizations to the worst-affected countries and facilitating various stimulus packages issued by governments to help economies cope with the pandemic. As a result, financial crime compliance will play an important role. For example, humanitarian-aid organizations should not be hindered by sanctions restrictions. Although licenses for humanitarian aid have always been part of the global sanctions' environment, and given the clear benefit of facilitating the flow of humanitarian aid during the COVID-19 epidemic, further clarity in the form of more specific licenses for the current circumstances would give banks greater confidence in deciding which transactions are permissible.

This article examines these financial crime challenges as the industry responds to the impact of COVID-19 in supporting its consumers and workforce, along with possible mitigating solutions. It focuses on areas such as the increased stress on business-as-usual (BAU) operations and emerging challenges arising from COVID-19 that must be considered as organizations adapt and overcome the immediate risks.

Organizations should consider when and what compliance activities can be undertaken. While focus on sustaining business activity is important, steps can be taken to reduce exposure to potential financial crime risk. EY has a number of relevant offerings to ease the burden of the increasing challenges and can help facilitate the crucial role that financial services will play in protecting our financial system and overcoming this global pandemic.

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- Bribery and corruption risks
- External fraud
- Internal fraud
- Market abuse
- The internal investigation process
- The whistle-blowing function

> 39% of board members admit that their organizations are facing challenge in maintaining controls and operation*

> One thing is for certain – organised crime groups will not stop.

RUSI

> Periods of crisis have a tangible impact on levels of exploitation and human trafficking – and Covid 19 will be no different.

STOP THE TRAFFIK

> Criminals have been quick to seize opportunities to exploit the crisis.

Europol

[1] https://www.europol.europa.eu/newsroom/news/how-criminals-profit-covid-19-pandemic.

*based on EY Financial Crime Compliance webinar 30 March 2020.

Challenges that are likely to be faced

Immediate consideration

- **Lower morale and loss of incentive to perform competently or uphold ethical standards:** There is a risk that employees no longer feel engaged or valued as part of an organization after losing their physical “space” during an unknown or unpredictable timeline.
- **Invalid business continuity plan and reduced staff availability:** There will be unpredictable workforce constraints due to unprecedented levels of illness, self-isolation and additional care responsibilities. These may be further exacerbated by organization-wide recruitment freezes imposed as a result of the ongoing uncertainties.
- **Loss of offshore operations centers and contingency sites:** Increased government-mandated national lockdowns and a lack of remote IT infrastructure are leading to overnight loss or limitation of wide-scale operations in compliance areas such as alert investigations.
- **Growing volume of alerts due to changing customer behaviors:** Sudden lifestyle changes as a result of enforced social distancing and employment-level fluctuations are causing unusual transaction activity profiles, triggering monitoring detection scenario typologies in different industries and regions.
- **Disruption on know your customer (or client) (KYC) operations to demonstrate files are up to date due to changes to business records:** The Department for Business, Innovation, Energy & Industrial Strategy has seen almost double the normal volume of monthly UK business changes. With businesses rapidly changing, KYC information will need updating at the same pace.
- **Volatile news-sensitive markets have created heightened market abuse and conduct risks:** Traders and some clients are seeing increased revenues, but busy markets are creating time-bound risks that existing surveillance controls do not focus on.
- **Market surveillance alert volumes are unmanageable:** Market volatility has led to significantly increased market abuse alerts at a time when resourcing capacity is fluctuating. For many, investigating every alert is not a viable option. Prioritizing key risks and managing these operational challenges has never been more important.
- **Increased insurance claims:** As businesses continue to be impacted by the sudden supply and demand shocks; insurance policies will be relied upon for protection. This surge in insurance claims will burden operations, especially with the added stress of determining the validity of claims.

After the crisis has settled

- **Fraudulent applications for business interruption loans and government grants:** With unprecedented government support on offer in the form of loans and grants, there is an increased risk of fraudulent claims to take advantage of the financial aid (for example, applications from dissolved businesses and dormant accounts). This will trigger further pressure on KYC operations.
- **Uncertainty around regulatory deadlines:** Despite business continuity planning, there is uncertainty around organizations’ ability to meet regulatory deadlines and regulators’ ability to carry out any planned reviews.
- **Increased levels of cyber-related fraud:** As customers become increasingly desperate for certain goods and demand outstrips supply, cyber-related fraud will boom. This not only leads to dissemination of fake goods but also poses a threat to confidential data such as bank details.
- **Organized crime groups will seek new ways to exploit the uncertainty:** Statistics from previous global recessions, such as the 2007–8 financial crisis, indicate a strong correlation with rising crime levels.
- **Increased fluctuations in the labor market may lead to increased counterfeiting and labor exploitation:** One of the leading human trafficking prevention charities, STOP THE TRAFFIK, anticipates that there will be shifts in the balance of power as unscrupulous employers are able to take advantage of newly unemployed individuals who are desperate to find new jobs.
- **Bribery and corruption risk from rapid and high-value procurement:** This is especially true for those industries experiencing rapid increases in unforeseen demand.

What’s needed and how to achieve it

- **Creative leadership:** Employers should identify creative leadership by deploying an agile mindset and a culture of inclusion to protect workforce values during these uncertain environments. Engage in supportive dialogue to discuss flexibility and alternative working arrangements for employee safety aligned with local authorities and regulators.
- **Employees well-being and mental health:** Employers should check in on the well-being and mental health of all employees, including frequent communications with reminders of the values and ethical standards that apply, even if business operations have moved to being almost completely online. Links to codes of conduct, training and guidance may be helpful material to be included for quick reference.
- **Collaborate with third parties:** With increasing resourcing constraints and challenges with staff availability, organizations may look to collaborate across the industry with third parties for resource support and augmentation.
- **Counter the additional market abuse and conduct risks that market volatility is causing:** Some organizations are looking at using additional tactical surveillance or regular look-back reviews to focus on these time-bound risks, as well as taking a risk-based approach to investigating surveillance alerts.
- **Adopt remote anti-money laundering protocols:** Operations may be re-shored and automated by adopting remote anti-money laundering protocols for transaction monitoring, countering the finance of terrorism and sanctions compliance.
- **Backlogs:** May be managed effectively through risk-based scoring and prioritization of alerts.
- **KYC:** May be enriched through the use of technology, analytics and commercial datasets, reducing the need for the physical transfer of documents.
- **Review customer due diligence (CDD) data:** For existing customers and explore what existing data can support remediation of gaps.
- **Extension of the flexibility of loan repayment and liquidity support while also evaluating the risk of default and fraud on loan applications:** This will be done by leveraging open banking data and commercial data-sets.
- **Consistent and open forms of communication with regulatory bodies:** This will be essential to help collaborative navigation of any regulatory action planned prior to the outbreak of the pandemic.
- **Access management governance to meet regulatory obligation:** This will be enabled by using recorded lines when trading as well as giving the employee access to the compliance support they need from remote working.
- **Collaboration with industry, law enforcement and regulators:** This will be used to assess new typologies and to understand trends by region in dynamic risk models.
- **Customers enabled to access cash virtually through financial inclusion:** This will be done by encouraging digital KYC due to challenges in face-to-face interaction during the onboarding process.
- **Collaboration across sectors:** Greater focus on collaboration between private, public and third sectors to increase economic and social opportunities.

Key contacts

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