

Financial crime
operations: the case
for transformation
in wealth and asset
managers

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EY

Building a better
working world

A man and a woman are standing in a server room, looking at each other and talking. The room is dimly lit with red and blue lights. The man is wearing a blue shirt and the woman is wearing a white shirt. They are both wearing lanyards with ID badges.

In a cost-sensitive market,
nothing is more expensive
than a missed opportunity

Introduction

► **Wealth and asset management (WAM) firms have underinvested in financial crime technology compared with peers**

Through EY industry roundtables and our experience in the WAM sector, we have observed that WAM firms have underinvested in financial crime technology compared to peers in other financial sectors. As a result, legacy systems, manual processes and poor data quality have become the root cause of significant operational challenges, which are impacting the efficiency, effectiveness, customer experience and the ability to scale in line with institutional growth plans.

► **Incremental changes are not enough to keep pace with the forces reshaping the sector**

Most technology initiatives, aiming to enhance financial crime operations (FinCrime Ops), are focusing on incremental technology improvements and remediating issues. We have seen industry leaders successfully strengthen operational capabilities by shifting their focus from short-term incident-driven approaches to longer-term transformational strategies. By focusing solely on immediate needs, heads of FinCrime Ops are missing the opportunity to provide a bolder response to the forces reshaping the investment management industry, such as fee compression, evolving regulation and digitization.

► **The way investors interact with WAM firms has changed in the last two decades**

Investor interactions with WAM firms have transformed in the past twenty years. Historically, most investors would be registered as the unit holders of the investment units. But today, most investments are managed by intermediaries acting as the unit holders on behalf of the end investors. Typically,

FinCrime Ops perform due diligence over direct investors and rely on intermediaries for indirect customers. This dilution of responsibility over distribution layers, and a lack of upstream data to conduct due diligence on indirect investors can result in some end investors not being subjected to the appropriate level of due diligence.

► **The investment ecosystem is changing with the increased adoption of blockchain solutions**

The momentum built around decentralized finance (DeFi), where blockchain is used for registering and transferring ownership of investment units, indicates that investment management is trending to disintermediation. This means that it will not take long until off-chain and on-chain investment units start to coexist in the investment ecosystem. This can significantly change how FinCrime processes operate today, meaning that heads of FinCrime Ops will have to rethink their processes and controls to adapt to this new reality.

► **To harness long-term opportunities and secure relevance in the future, WAM firms should consider a transformational FinCrime strategy**

Facing these market dynamics, WAM leaders are increasingly seeking to transform their financial crime operations. Digitization of sustainable processes and controls, enhanced risk management, a focus on people and culture, and the imperative to optimize the customer experience are all key factors driving this agenda. Heads of FinCrime Ops are now, more than ever, needing to align their strategies with the goals of their institutions to deliver the transformation that provides lasting value for the business by placing humans at the center, leveraging technology at speed and innovating at scale.

FinCrime Ops are nearing an inflection point

FinCrime Ops are facing significant pressure to change. There are some key forces driving this change:

- 1 Fee compression and declining assets under management (AUM):** As indicated by the October 2022 EY press release on the UK AUM value trends, fees and AUM are declining at unseen rates in the sector since the 2008 financial crisis, with a modest reversal expected in 2023.¹ In response to this outlook, WAM firms are prioritizing cost-cutting initiatives to reduce revenue impacts. Cost-reduction strategies are becoming a priority in most firms, pushing heads of FinCrime Ops to increase focus on efficiency as a primary goal.
- 2 Increased regulatory focus:** Regulators are becoming more active in the sector. An example is the Consumer Duty published by the FCA, which requires firms to improve their understanding of the characteristics and behavior of retail customers in target markets and provide clearer product and service information to enable customers to make more informed investment decisions.² A discussion paper has also been recently issued by the FCA, requesting inputs for improving the UK regime for asset management. According to this paper, the FCA is considering heightening requirements for engagement between WAM firms, intermediaries and investors.³ Both measures can have a positive impact on know-your-customer (KYC), as improving engagement and knowledge about customers' characteristics and behaviors can contribute to the firm's ability to know their customers and sources of wealth.
- 3 Concerns over obscurity of underlying investor's identity and source of wealth:** In 2023, poor due diligence controls over the relationship managers' engagements with clients contributed to an irreversible impact on a global investment bank's market confidence.

This resulted in an emergency rescue by peers to avoid a major impact on the local and global financial system. Two main thematic issues have emerged as the root cause for these issues:

- 3.1 Relationship management culture:** While there are regulatory requirements to ensure robust monitoring of relationships between relationship managers and investors, WAM firms continue to struggle with implementing effective due diligence controls. Many firms have committed time and investment budgets to customer experience innovation; however, investment in the underlying financial crime controls has failed to keep pace. This can be looked upon as a missed opportunity, as efficient and digital due diligence processes allow and support frictionless customer experience. It is, therefore, critical for FinCrime Ops to change this culture and implement enhanced technology to improve due diligence processes. This will help FinCrime Ops carry out their role and consciously act as a risk owner without jeopardizing customer experience.
- 3.2 Multiple distribution layers concealing ownership:** In the context of KYC, especially in cases where the WAM firms do not engage directly with investors, WAM firms rely on intermediaries for conducting customer due diligence. There are concerns that multiple distribution layers may dilute the responsibility for conducting KYC checks, ultimately resulting in the investor's identity, source of wealth and funds not being checked properly (or at all). FinCrime Ops must be equipped with the right information about underlying investors to undertake its frontline role and prevent those multiple distribution layers that conceal the identity of underlying investors.⁴

¹ "EY Press Release", EY website, [ey.com/en_uk/news/2022/10/economic-uncertainty-to-see-uk-aum-value-fall-this-year-before-a-modest-reversal-in-2023-and-higher-growth-in-2024](https://www.ey.com/en_uk/news/2022/10/economic-uncertainty-to-see-uk-aum-value-fall-this-year-before-a-modest-reversal-in-2023-and-higher-growth-in-2024).

² "A new Customer Duty", FCA website, [fca.org.uk/publications/policy-statements/ps22-9-new-consumer-duty](https://www.fca.org.uk/publications/policy-statements/ps22-9-new-consumer-duty).

³ "Updating and improving the UK regime for asset management", FCA website, [fca.org.uk/publications/discussion-papers/dp23-2-updating-and-improving-uk-regime-asset-management](https://www.fca.org.uk/publications/discussion-papers/dp23-2-updating-and-improving-uk-regime-asset-management).

⁴ "Risk-based approach guidance for the securities sector", FATF website, [fatf-gafi.org/en/publications/Fatfrecommendations/Rba-securities-sector.html](https://www.fatf-gafi.org/en/publications/Fatfrecommendations/Rba-securities-sector.html).

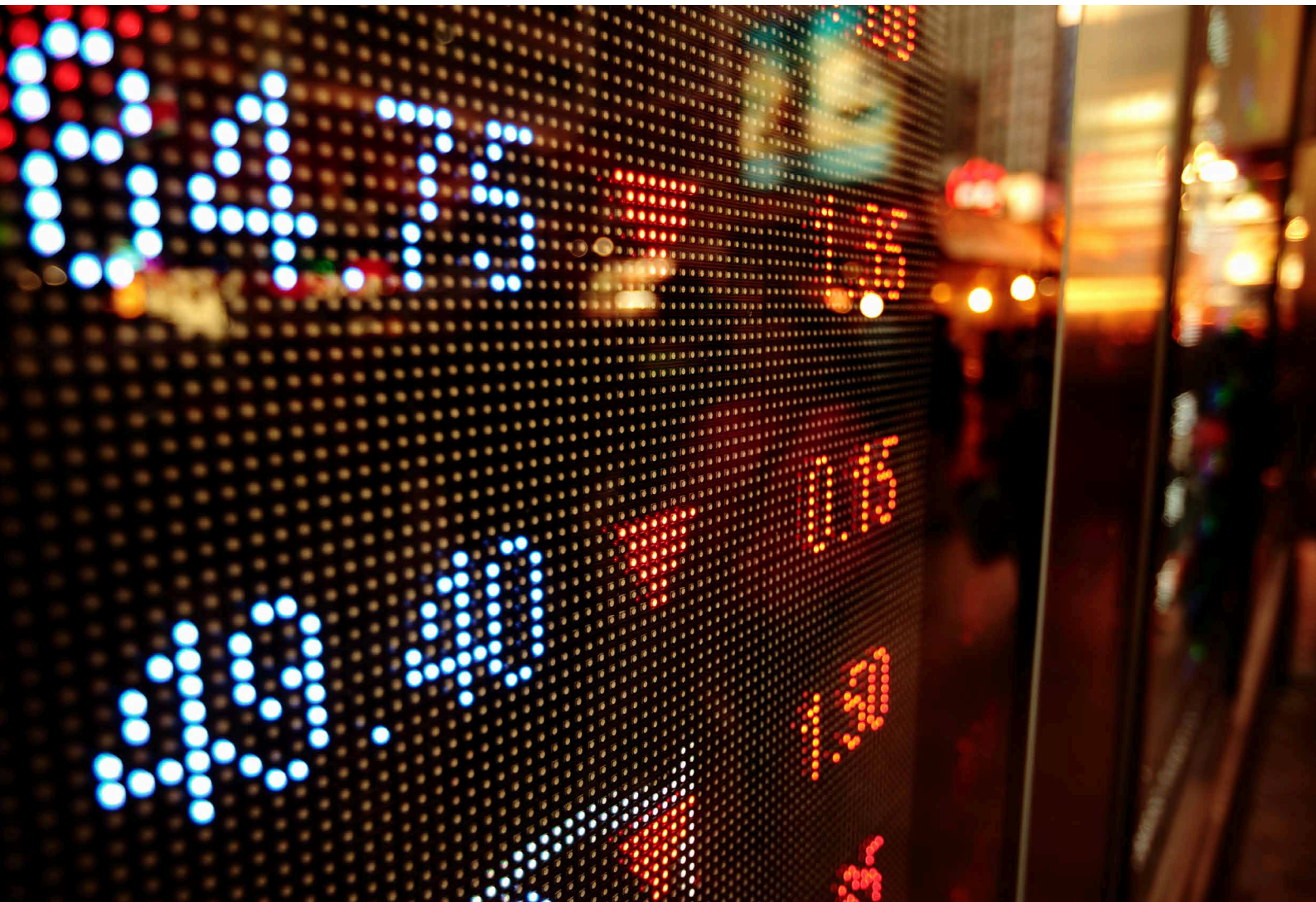
4 Intergenerational wealth and assets transfer: This transition is increasing demand for improved real-time digital interaction with investors and adding pressure on FinCrime Ops to take part in and support the digitization of a broader range of customer journeys. Offline and paper-based processes do not match the expectations of digital natives, operating online through technology or applications. Additionally, cryptocurrencies and decentralized finance might have been a step too far for the boomer generation, but are becoming commonplace for Gen X and millennials who are inheriting or managing increasing volumes of assets personally and professionally.

5 Tokenization and democratization of private markets: The momentum around DeFi and the usage of blockchain networks for registering and transferring the ownership of investment units is expected to drive significant changes in how FinCrime controls operate in the sector today. It will not take long for traditional investment units registered off-chain to start coexisting with on-chain investments registered in blockchain networks. Right now, some deals have long lockups, and it can be expensive to buy and

sell a private asset. With more assets set up on-chain, the industry can increasingly overcome the liquidity problem, making investing by smaller increments easier, frictionless and more fractionalized. FinCrime Ops will have to adapt to this new reality. With more flexible technology, FinCrime Ops can ease the reconfiguration of FinCrime controls to conduct financial crime checks on smart contracts. The lack of speed in adapting to these changes may result in irreversible technical debt, negatively impacting the business's ability to stay relevant for its customers in future.

6 Inorganic growth strategies: The EY WAM Outlook 2023 report indicates that dealmaking will continue as firms seek to build economies of scale; however, large-scale M&A activities will be a lesser strategic tool than in the past.⁵ Instead, firms will focus on delivering planned synergies from past deals. The modernization of FinCrime legacy technology and simplification of the system's architectures and processes are key priorities for firms aiming to realize the benefits from previous, and to a lesser extent new, M&A deals.

⁵ "Six ways asset managers can prepare for an uncertain future", *EY website*, [ey.com/en_gl/wealth-asset-management/six-ways-asset-managers-can-prepare-for-an-uncertain-future](https://www.ey.com/en_gl/wealth-asset-management/six-ways-asset-managers-can-prepare-for-an-uncertain-future).



Rapid reaction is crucial to responding to the current market outlook and to harnessing long-term opportunities

In the face of this market outlook, which is aggravated by years of underinvestment in FinCrime technology, heads of FinCrime Ops in WAM firms cannot take a backseat. We are seeing firms take strategic transformation steps to enhance operations by renovating their technology application and architecture blueprints.

Rapid reaction is becoming crucial for firms to keep costs under control, maintain profitability and make a successful start to stand out in future. WAM firms need to establish appropriate plans to respond to the current market conditions by:

- 1 Improving efficiency and reducing cost to offset fee compression and declining AUM:** With legacy technology, firms will continue to rely on error-prone processes and repetitive tasks that increase operational costs and impact competitiveness. These are detrimental factors in a market with an increased demand for lower costs and interest rates at the highest level since 2008. There also exists an opportunity to release resources from low-value activities to focus on higher-risk analysis. This is possible by leveraging automation and proven solutions that can improve KYC productivity and anti-money laundering (AML) operations.
- 2 Modernize technology to enable rapid response to regulatory changes:** Following years of active regulatory focus on the banking sector, regulators have started to scrutinize other sectors, especially wealth and asset management. Changes are expected to happen more frequently in the coming years, following the recent consultation raised by the FCA on updating and improving the UK regime for asset management. Modernizing legacy technology and adopting flexible solutions that allow rapid implementation of changes for FinCrime processes will be critical for compliance.
- 3 Improving transparency over underlying investor's KYC data:** Several debates, following data leaks, have showed that firms, did not apply proper due diligence over their clients. These leaks revealed that firms held accounts for high-profile, sometimes convicted individuals,

and suffered significant reputational impact because of that. Making better use of third-party data to enrich client information and allowing transparency over the ownership of investments across distribution layers is critical. This can help prevent blind spots from impacting the Operations teams' ability to perform proper due diligence on investors.

- 4 Improving data quality and supporting wider digital transformation:** Supporting the digitization of multi-channel customer journeys is critical in improving customer experience and meeting expectations of digital-native generations who are inheriting and managing increasing volumes of assets and wealth. However, this is not possible without data quality, which is essential for successful automation and digitization. Without accurate data, WAM firms cannot identify, mitigate or manage financial crime risks effectively, let alone innovate financial crime processes. Moreover, we have seen poor management information (MI) causing significant impact on WAM firms' operational governance, risk management and decision-making processes.
- 5 Preparing for assets' tokenization:** Without change, processes will move into the status quo and miss preparing to apply financial crime controls on tokenized assets, which are expected to co-exist with traditional investment units in the following years. This modernization will be driven mainly by the tokenization of funds based on blockchain networks. Developing flexible future-proof technology that allows FinCrime processes to operate under this new ecosystem is critical for long-term sustainability of the industry.
- 6 Integrating technology to simplify M&A transactions:** Modern technology can simplify integration with different platforms and help realize the benefits expected from transactions. Historically, complex and fragmented technology architectures added complexity to M&A transactions and resulted in significant remediation programs.



Incremental changes are not enough to keep pace with the forces reshaping the sector

We see WAM firms still largely focused on delivering enhancement through incremental change. This approach is unlikely to deliver the transformation required to keep pace with forces reshaping the industry and to harness long-term opportunities.

The EY Transformation Realized™ methodology is a powerful tool that allows firms to kick-start strategic transformation to maintain the firm's relevance in the long term. It helps firms identify and move into a better transformational S-curve.

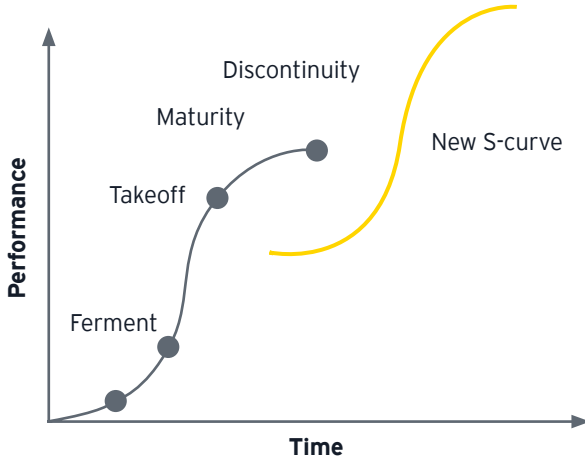
S-curves are a way to visualize how innovations develop over time, at the beginning, the rate of adoption of new innovations is slow – just a few people take notice, then it becomes mainstream, and the rate of adoption speeds up.

Finally, once that innovation has been adopted widely, the rate of adoption and growth slows or stalls completely. The challenge for organizations today is to not only ascend that S-curve, but to take the leap to the next innovation – the next S-curve.

Heads of FinCrime Ops in WAM firms should consider a shift of approach to change. By moving away from the typical short-term, business-as-usual, incident-driven approach to change towards a strategic mindset, they can realize a truly

transformational leap over to a new, better S-curve. In doing so, FinCrime leaders can face into the dynamic forces shaping the sector and articulate the benefits of transformation by linking their business case into the wider strategy and needs of the firm.

S-curve of innovation





To embark on a better transformational curve, heads of FinCrime Ops need to step outside their comfort zones, collaborate with wider stakeholders across the business and ask themselves: what does the business really need from us now? Will current processes be fit-for-purpose in the next 2, 5 or 10 years from now?

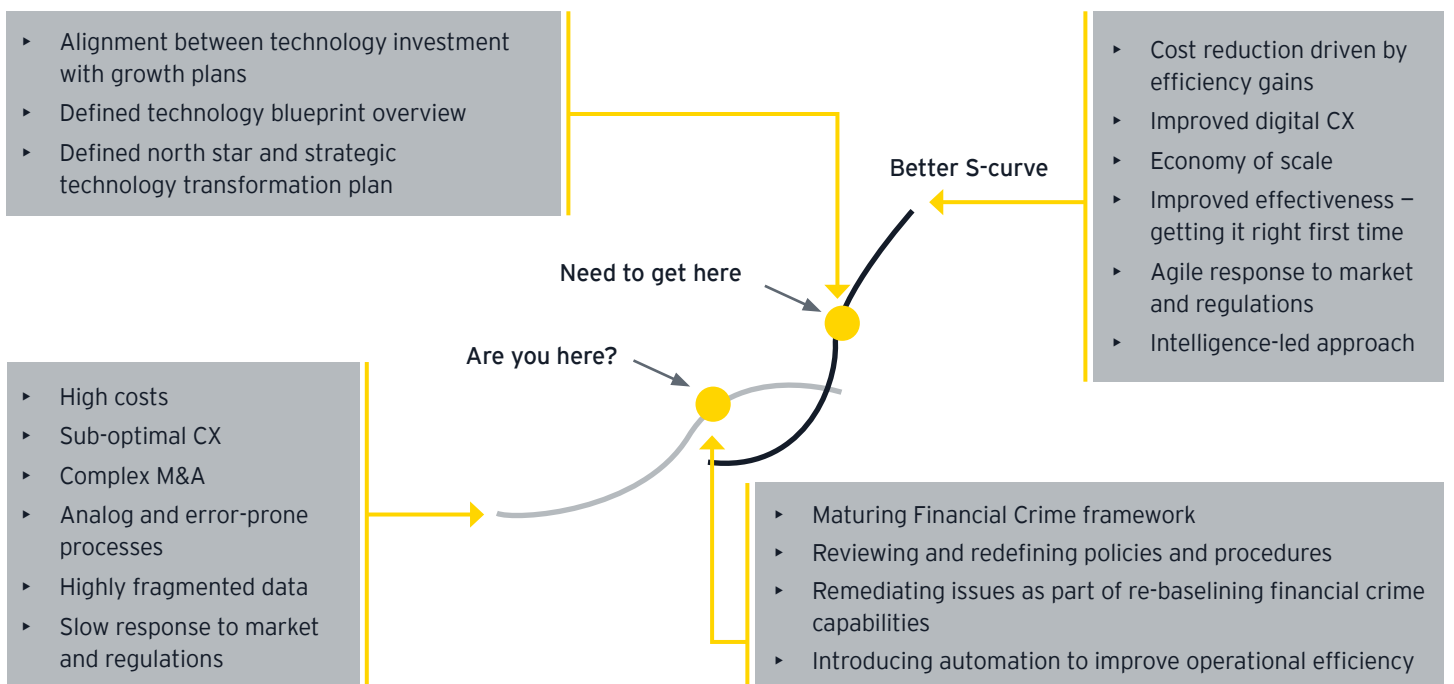


Figure 1 – The Better Transformational Curve



The five steps wealth and asset managers financial crime leaders must take to harness innovation and growth opportunities

The EY Transformation Realized™ methodology helps firms to step into the future, work backwards and develop insights about the changes needed today for a better tomorrow. It has three main components (define, design and deliver) and comprises five key steps.

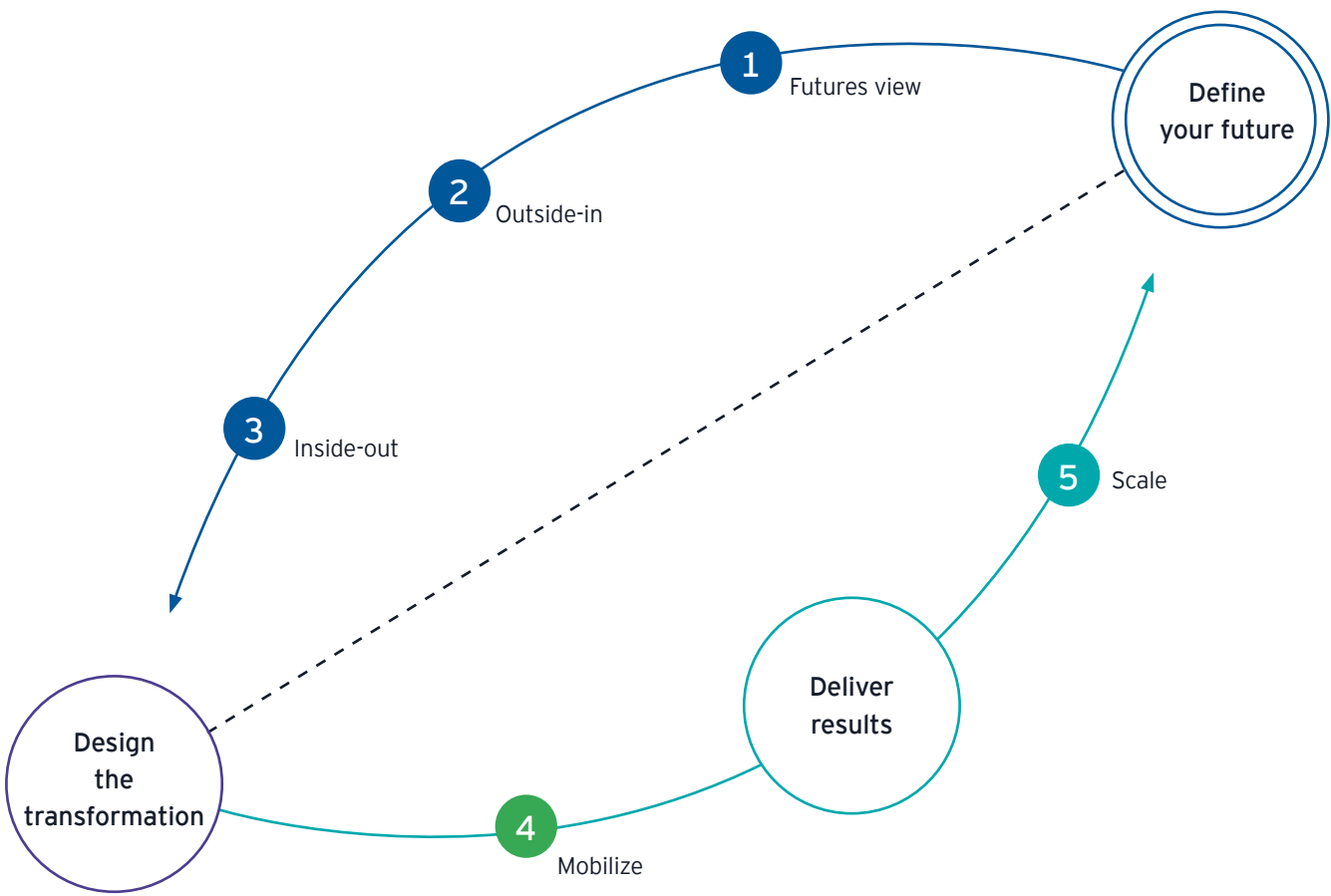


Figure 2 – EY's Transformation Realised Methodology



1 Future view:

To start their FinCrime transformation journey, WAM firms need to define principles and future-state vision statements that align with the institutional values and purpose and consider the market outlook and forces reshaping the industry. At this stage, firms should identify the building blocks underpinning FinCrime processes and define the high-level blueprint for FinCrime Ops. This includes the functional and operational components required to support the future vision. We can support firms in defining this view through an EY wavespace™ session. EY wavespace brings together business, design and technology, enabling firms to accelerate transformation, drive innovation and create measurable outcomes through our design thinking lab. In these sessions, we deliver basic data, insights and background to illuminate and provide context for the work ahead, uncovering critical assumptions and issues. These sessions also help in exploring creative and fresh perspectives in the work we do.

2 Outside-in:

When a clear future view and a high-level blueprint is defined, firms are in the right position to compare the current state with the future art-of-the-possible and benchmark their technology with their industry peers. We have recently supported WAM firms to review and improve their FinCrime technology landscape by leveraging top-graded customer lifecycle management (CLM), analytics and workflows solutions. By combining the outside view with internal reflections, firms can translate the unified purpose, vision and future state into transformation priorities, new business models and working methods that align with the organizational strategic goals.

3 Inside-out:

Go deeper and define how to make transformation a tangible reality by identifying the capabilities required to achieve the future state, including the existing ones and the ones that need to be developed. At this stage, firms are able to bring in internal data and specific business knowledge to refine the technology blueprint and define the essential prerequisites to develop the target state. We have seen firms developing FinCrime technology requirements as part of wider unrelated initiatives and missing the opportunity to focus on leading technology and best practices, especially in areas such as KYC, screening and third-party risk

management. The financial crime technology landscape is complex and constantly evolving. Therefore, leveraging specific FinCrime knowledge and sector experience to develop clear-cut prerequisites is critical in making the right long-term decisions.

4 Mobilize:

Plan the end-to-end transformation journey by developing short-term and longer-term initiatives. At this stage, we break down prerequisites into smaller components, for example, Electronic Identification and Verification (eID&V), risk rating, adverse media screening (AMS), and organize the transformation program into workstreams that make execution possible. Research shows that major changes are twice as likely to result in incidents than standard (smaller) changes.⁶ The roadmap and ways of working required to deliver the transformation program should also be defined and agreed upon at this stage with stakeholders.

5 Scale:

Move from the kick-off, vision and strategy development part to execution in the direction of the desired state – transforming the functions and platforms, and adjusting the direction of travel, when required, to deliver the highest-quality outcome. As execution progresses, it is essential to take into account the principle of proportionality. WAM firms' transformation projects can run into issues where they have replicated solutions developed for other types of financial institutions, especially retail and commercial banks, without reasoning whether these solutions were proportionate to their needs.

Being transformative requires planning for the now, next and beyond, and refocusing from the historical value drivers of scale, scope and efficiency to a new core of value creation. By applying the correct values and leveraging industry experience to define transformation strategies, firms can avoid pitfalls and leapfrog over challenges already faced by other financial institutions.

While speed and change are imperative, businesses can't afford their transformation to fail. Those who succeed do more than prosper – they create lasting exponential value. What we have seen from successful firms that create exponential value is that they place humans at the centre of their organization, leverage technology at speed and innovate at scale.



In summary

- WAM firms have typically underinvested in FinCrime technology compared to peers and rely on legacy systems, manual processes and poor data quality to support financial crime processes. This undermines their capacity to identify, mitigate and manage financial crime risks and comply with regulations.
- WAM firms need to align their FinCrime technology development strategies with the institutional landscape, strategy and respond to forces reshaping the industry today, such as fee compression, evolving regulation and digitization.
- WAM firms have been focused on customer experience and growth opportunities but have not developed financial crime controls proportionately. Implementing efficient and digital due diligence processes can create frictionless customer experience without jeopardizing the FinCrime Ops responsibilities as risk owners.
- Incremental actions are unlikely to deliver the transformation required to keep pace with the changes expected in the upcoming years; therefore, a more transformational approach is required for WAM firms to stay relevant in the future and harness long-term opportunities.
- Significant change is expected from the adoption of blockchain to store ownership of investment units, and the democratization of private assets through tokenization. Regulatory support has built momentum recently, and WAM firms need to prepare for these changes.
- To align with other financial sectors and avoid becoming the weakest link in the chain, WAM firms need to build stronger digital foundations in financial crime. They should also ensure that the right investment levels and leadership support to develop FinCrime controls are in place alongside other business priorities.



How EY teams can help

EY professionals have extensive experience in supporting WAM clients to define their future views and in designing and implementing transformational strategies for FinCrime Ops. This includes developing operating models, policies, procedures, technology and data solutions to improve efficiency, effectiveness and customer experience. We have supported WAM firms to innovate their processes by driving the right decisions on technology and leading the cultural changes required to deliver strategic transformations and allow institutional growth.

The EY FinCrime team has launched a wealth and asset management roundtable group, and we are accepting nominations for membership to participate in thematic sessions focused on the key trends reshaping the sector. If you are a senior leader focusing on FinCrime Operations and transformation, please get in touch with the key contacts below.

Key contacts

For further information, please contact the Financial Crime and Forensics team.



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