NOV 08
Lauren Ashcraft

Banks must make de-risking processes more human to avoid reputational damage

Article

The trend: A recent New York Times article sheds light on **a rising trend of unexpected bank account closures,** emphasizing the challenges customers face in navigating their necessary day-to-day financial activities.

- FIs aren't required to report how often they're wrong about their account closure decisions, but consistent errors can place financial institutions (FIs) under a negative spotlight.

The legal requirement: FIs must report suspected illegal activity by submitting "suspicious activity reports" (SARs) to the US Department of the Treasury's Financial Crimes Enforcement Network.

- Although they don't disclose to a customer when this has happened, banks reported over 1.8 million SARs in 2022, marking a 50% increase within two years.
- FIs are on track to submit over 2 million SARs in 2023.

What type of activity raises a red flag? The New York Times highlighted a handful of the 500 complaints it has received from consumers—painting a picture of ordinary, lawful circumstances that allegedly led to the account closures, such as:

- A bar manager who makes regular cash deposits slightly below reporting thresholds for legitimate reasons
- A woman whose husband receives direct deposits from a cannabis company that acquired his employer
- A customer relying on regular overseas wire transfers to cover expenses like rent and family support
- An individual whose financial behavior, though atypical, comprises unexpected large transfers or occasional inconsistencies
- A person with a prior criminal record unrelated to financial services
- Community members engaged in regular and repetitive transactions within a susu—their trusted financial community, a popular collective savings practice in African, Caribbean, and some Asian cultures

Aaron Ansari, who used to program the algorithms that help FIs identify suspicious activity, told the New York Times: "There is no humanization to any of this, and it's all just numbers on a screen. It's not, 'No, that is a single mom running a babysitting business.' It's 'Hey, you've checked these boxes for a red flag—you're out.'"

How'd we get here? Banking expert J.D. Koontz says FIs act out of an abundance of caution—erring on the side of compliance rather than facing hefty penalties for letting suspicious activity slide.

- In a statement to KCAL, **Bank of America** noted it discloses to customers that accounts can be closed if it suspects fraudulent activity.
- **JPMorgan** spokesperson Jerry Dubrowksi says, "Accounts are closed only after appropriate review and consideration of the facts," and that the bank "acts in accordance with our compliance program, consistent with our regulatory obligations."
- However, **the Bank Policy Institute found that only 5% of SARs warranted followup from law enforcement.**

The bigger picture: The trend of sudden unexplained account closures isn't limited to the US, and has prompted UK lawmakers to propose rules that would require banks to clearly explain any closure—and give customers 90 days to challenge a decision through the Financial Ombudsman Service or find a replacement bank.

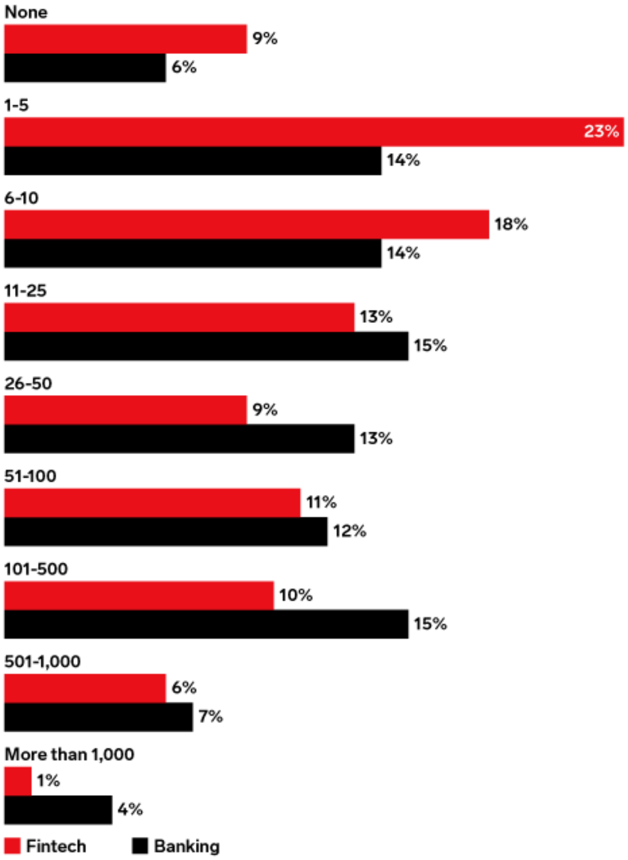
- However, US laws prevent FIs from informing individuals when they are the subject of a submitted SAR—meaning change will be driven by a FI's internal customer service protocol.

Key Takeaways: While algorithms can raise valid red flags and highlight abnormalities in banking activity, the customer testimonials in the New York Times revealed a breakdown in the process. Namely, it needs to incorporate relevant facts customers provide about their banking activities.

- **FIs should check their de-risking practices to ensure they incorporate human feedback and insight.**
- Failure to do so can result in traumatic ends to long-term banking relationships, a significant loss of business, and reputational damage.

Number of Identity Fraud Incidents Experienced at Their Company According to Fraud Prevention Professionals Worldwide, Banking vs. Fintech, Jan 2023

% of respondents



Note: in the past year
Source: Regula, "Cost of Identity Fraud to Financial Organizations" conducted by Sapio Research as cited in press release, March 29, 2023

281315 InsiderIntelligence.com