WHITE PAPER

Solving Financial Services Compliance Challenges with Lean Six Sigma

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Solving Financial Services Compliance Challenges with Lean Six Sigma

Highlights

Lean Six Sigma tools can be successfully used to help financial services organizations combat the challenges of increased regulatory requirements.

EXECUTIVE SUMMARY

Most financial services organizations agree that the current risk and compliance environment has become increasingly complex and a navigational challenge. New mandates pose cost challenges, task employee skill levels, challenge system and process integration and require ongoing enhancement of overall performance management practices. The costs of non-compliance are high; fines, adverse impact to reputational capital, citations and restrictions on non-organic growth opportunities are some obvious ones.

Six Sigma is a methodology that helps any business reduce costs and inefficiencies by identifying and eliminating whatever wasteful steps exist within a process. Although it was originally developed for use within manufacturing, Six Sigma tools can be effective within financial services organizations to help solve compliance problems, even though the problems typically have many intricate and legacy processes.

Given the cost of non-compliance fines, there is real motivation within financial services to adhere to regulations and to more effectively manage the compliance processes and cost. In this paper, we:

- briefly indicate the challenges faced in this regulatory and risk management landscape
- highlight the approaches that can be adopted to help the company manage these challenges
- review how one financial institution used Lean Six Sigma tools to meet compliance challenges

CONTEXT

The Royal Bank of Scotland recently estimated that the cost of its risk and compliance has risen 30 percent in the last two years. A survey by Veris Consulting, conducted in early 2013, showed that banks must plan to devote more resources to Anti-Money Laundering (AML) and Office of Foreign Assets Control (OFAC) complaints, but a third of the respondents had insufficient budget to meet those demands.

For many financial institutions, the answer is simply to hire more staff. But the Federal Reserve Bank of Minneapolis estimated in 2013 that hiring just one additional employee would reduce the return on assets by 23 basis points for banks with total assets of $50 million or less. This decline could cause about 13 percent of them to go from profitable to unprofitable.

"…failure to deal with triggered alerts within the allowable regulatory time allotments resulted in OCC citations and adverse findings."

But there is an alternative that requires an inward focus rather than an outside view of bringing in additional staff. Lean Six Sigma tools could be deployed that would streamline processes, eliminate waste and cancel the need for more personnel.

The Alacer Group recently worked with a U.S.-based financial institution that had rapidly grown through acquisitions. It had not adequately anticipated the resources, process and system challenges inherent in integrating the compliance functions across multiple entities with differing regulatory needs. The parent organization's risk monitoring systems were being applied indiscriminately to acquired entities, leading to volume spikes in suspicious activities. The organization's resulting failure to deal with the triggered alerts within the allowable regulatory time allotments resulted in OCC citations and adverse findings.

In addition to volume spikes and unprocessed alert backlogs, the compliance officers and investigative teams faced the following challenges:

- each alert's increasing processing cost
- declining productivity per investigator
- 95% of alerts were not processed within the allowable timeframe
- non-existent performance management processes
- limited transparency

The immediate management directive was clear: find a way to deal with the backlog of alerts to achieve regulatory compliance. Other desired initiatives:

- calibrate the monitoring system
- optimize the review process
- reduce processing costs
- improve investigator productivity
- deploy end-to-end performance management practices

“…a real opportunity to financial institutions to combat financial and reputational damage without incurring sustained additional cost.”

APPROACH

The Alacer team believed that, by using basic Lean Six Sigma techniques, the financial organization could optimize its review processes and improve its ability to comply with regulatory mandates and guidelines, yet reduce time and resource costs.

Initially, we focused on establishing a fact and data-derived baseline that could provide an accurate view of the institution’s current performance across several dimensions: incoming alert volumes, processing costs, productivity, mean and dispersion of review cycle times and levels of adherence to performance management practices. Once established, the baseline could then be analyzed using a combination of Lean Six Sigma tools. This identified root causes of problems and suggested the best improvement options.

RESULTS

For this organization, using Lean Six Sigma tools to streamline its risk and compliance processes has resulted in:

- 57% decrease in alert volume
- 63% increase in productivity
- 21% decrease in processing costs
- 100% of alerts now fully compliant within regulatory review periods

In comparison, there were 23,160 alerts out of compliance on January 1, 2011; by March 2011, there were zero alerts out of compliance.

CONCLUSIONS

Lean Six Sigma tools can be successfully applied to the financial services industry, particularly in the areas of risk management and compliance; after all, these are simply business processes. The monitoring, reviewing and reporting functions can all be streamlined through the skillful use of lean principles. Given the current regulatory environment, Lean Six Sigma presents a real opportunity to financial institutions to combat financial and reputational damage without incurring sustained additional cost. Through Lean Six Sigma, tangible, successful outcomes can include a reduction in processing costs, enhanced productivity and, ultimately, full compliance with regulatory guidelines.