

Fortify your position against financial crimes

Preparing Digital Insurers and Takaful Operators for
robust AML/CFT compliance

KPMG in Malaysia

For a long time, the traditional insurance business model has proved to be remarkably resilient. But now, it too has had to adapt to the digital influence. Within the Malaysian context, a case in point to illustrate this shift lies in the expected deployment of digital roadside assistance (DRA) solutions through web and mobile applications by the majority of insurers and takaful operators (ITO) by 2024.¹ This strategic initiative, complemented by the forthcoming release of the Digital Insurers and Takaful Operators (DITO) Framework in H1 2024, underscores the inevitability of change on the horizon.² While this change imperative for the purpose of business efficiency is unequivocal and frequently paves the way for new opportunities, it is not without its inherent set of risks.

The financial crimes landscape in Malaysia

In today's dynamic business environment, financial institutions find themselves exposed to a spectrum of financial crimes, particularly money laundering/terrorism financing (ML/TF). Organized crime syndicates and terrorists are progressively leveraging sophisticated international networks and technologies to move or store funds and assets that are likely to pass through financial systems. The implications of these illicit activities extend beyond monetary ramifications, as they also cause substantial reputational damage to the organization.

The United Nations Office on Drugs and Crime (UNODC) estimates that roughly USD800 billion to USD2 trillion is laundered globally every year.³ To put this into perspective, this is equivalent to up to five times Malaysia's 2022 gross domestic product (GDP), which is the country's highest annual economic output to date.

Meanwhile, Bank Negara Malaysia (BNM) disclosed in its annual report that 242,914 suspicious transaction reports (STR) were received in 2022 – a 27% increase from 2021 – with both STRs on fraud and money

laundering offenses continuing to increase. These resulted in the arrests of 51 individuals, the freezing and seizing of assets of more than RM570 million as well as revenue recovery of RM372 million in relation to crimes such as organized crimes and frauds.⁴

These risks are exacerbated as financial institutions embrace technology. The Malaysia National Risk Assessment 2020 (NRA 2020) reported that technological advancement poses a growing threat to the ML/TF landscape in Malaysia across various financial sectors. The increasing adoption of technology such as online marketplaces and cryptocurrencies has widened the reach of criminals to perpetrate their illicit activities.⁵ The Financial Action Task Force's (FATF) recent publication corroborates this, as it is observed that the use of virtual assets – including anonymity-enhanced coins or cryptocurrencies to disguise terrorist financing – has been increasing.⁶

1. [Driving into the Future – A Digital Motor Claims Journey](#), Bank Negara Malaysia
2. [Outcome of Public Consultation on Exposure Draft on Licensing and Regulatory Framework for Digital Insurers and Takaful Operators](#), Bank Negara Malaysia, 5 October 2023
3. [Money Laundering Overview](#), United Nations Office on Drugs and Crime (UNODC)
4. [Maintaining Financial Integrity, BNM Annual Report 2022](#), Bank Negara Malaysia
5. [Malaysia National Risk Assessment on Money Laundering and Terrorism Financing 2020 \(NRA 2020\)](#), Bank Negara Malaysia
6. [Virtual Assets: Targeted Update on Implementation of the FATF Standards on Virtual Assets and Virtual Asset Service Providers](#), Financial Action Task Force, 27 June 2023

The challenges ahead for DITO

Given the high level of regulation, complex product offerings and extensive distribution networks in the insurance industry, existing insurance players are cautious when it comes to the risks of abandoning legacy systems.⁷ Consequently, the industry as a whole lags behind many other sectors in digital maturity due to its slower pace of digital adoption.



According to a 2022 study conducted by ACORD – a non-profit organization in the insurance industry – it was found that among the 200 largest worldwide insurers, fewer than 25% have truly digitized the value chain, while more than 10% are not appreciably leveraging digital technologies within their current business processes. Further, more than half of the insurers in the study are still exploring how digitization can be applied to their business model.⁸

Malaysia is no exception to the global trend. As the local insurance sector takes its first major stride in embracing digital business models with the advent of DITO, ITOs that are keen to transition will encounter new challenges when it comes to effectively assessing and mitigating risks. The use of digital tools and data analytics plays a crucial role in identifying and managing a wide range of risks, such as fraud detection, underwriting accuracy and claims processing efficiency. A deficiency in digital maturity could result in these tools not being fully leveraged, potentially leading to an underdeveloped risk control framework.

A concomitant rise in cyber threats and the associated risks of ML/TF is to be expected, given today's growing proclivity towards remote transactions buoyed by the convenience of quick, on-the-go and multi-device engagement for consumers. As such, DITOs are compelled to strengthen their anti-money laundering/counter-financing terrorism (AML/CFT) controls and awareness. This is further emphasized as the insurance industry has always placed paramount importance on AML/CFT risk compliance due to its highly regulated nature.

On this basis, in adherence with the Licensing and Regulatory Framework for DITO, applicants are expected to fulfill sound risk management and compliance requirements in AML/CFT measures.⁹ DITOs that provide Life and Family Takaful products are also mandated to comply with the requirements of Electronic Know-Your-Customer (e-KYC).¹⁰

Key challenges



Develop, implement and maintain a risk-based AML strategy that will protect the organization from risks associated with ML/TF and other financial crimes through proactive compliance with relevant laws and regulations.



Growing sophistication of AML/CFT typologies, including complications arising from the use of new technology and cross-border issues.



Manage the scope of various activities including having an adequate number of personnel with the required skill set.



Develop remediation action plans that are cost-effective and do not affect the growth strategy and enterprise goals.



Provide adequate change management and training tools to facilitate the adoption of desired AML/CFT behavior across the organization.

7. [Insurance industry profile](#), Economist Impact, 2022

8. [ACORD's 2022 Insurance Digital Maturity Study of Top Global Insurance Carriers Finds That Fewer Than 25% Have Truly Digitized the Value Chain](#), ACORD, 15 June 2022

9. [Licensing and Regulatory Framework for Digital Insurers and Takaful Operators Exposure Draft](#), Bank Negara Malaysia, 25 November 2022

10. [Electronic Know-Your-Customer \(e-KYC\) Exposure Draft](#), Bank Negara Malaysia, 23 February 2023

Maneuvering through the ML/TF risks landscape



The risk landscape is in a constant state of flux; any advancement in technology is not only beneficial for society and businesses, but also opens up opportunities for cybercriminals to exploit.

The government, in response, has consistently demonstrated the readiness to implement new policies and regulations over the past years. A series of measures were put into action, including the establishment of the National AML/CFT Authority in 2018; the adoption of the FATF's recommendations; and the implementation of the National Anti-Corruption Plan (NACP) 2019-2023. In addition, the National Scam Response Centre (NSRC) allocation was doubled to RM20 million under Budget 2024. This commitment to eradicate financial crimes continues to intensify as the country prepares for the FATF's mutual evaluation in 2024 – 2025.¹¹

Achieving success in this arena demands a unified front, given that we are only as good as our weakest link. Financial institutions are under immense pressure to move away from 'tick-box' compliance by innovating and promoting a culture of compliance to better protect our communities. As the level of regulatory scrutiny increases, financial institutions will need to strategically examine whether their identification and management of ML/TF risks is effective.

1 Develop a holistic AML/CFT compliance framework

To effectively manage this evolving AML/CFT regulatory environment, especially in non-face-to-face (non-FTF) business relationships, DITOs must be vigilant and forward-thinking in combating financial crimes. A holistic approach is needed in developing AML/CFT measures, which must include areas such as onboarding, underwriting, product distribution, policy/takaful certificate servicing, claims processing and payments. These measures encompass:

- ML/TF risk assessment methodologies
- Customer due diligence (CDD), including enhanced due diligence (EDD) and ongoing due diligence (ODD)
- Transaction monitoring (TM)
- Suspicious transaction reporting (STR) processes
- Governance and oversight of ML/TF risks and controls
- AML/CFT policies and procedures
- Monitoring and testing for compliance
- Training and awareness programs

2 Opt for a perpetual Know-Your-Customer (KYC)

Given the profound digital transformation of the financial system, it is vital to ensure that AML/CFT compliance programs remain relevant and effective. This would entail implementing measures that mitigate the emerging ML/TF risks in the detection of fraud for the authentication and verification process. A critical aspect of this initiative is the adoption of perpetual KYC, with integrated technology solutions to maintain relevance and quality of data that is complete, accurate and timely.

3 Leverage advanced technology

While technology advancements present opportunities for exploitation by illicit actors, they also offer DITOs a unique opportunity to enhance their vigilance. By harnessing the capabilities of data analytics and pattern recognition, DITOs can effectively identify high-risk transactions in real-time, enabling them to proactively prevent potential fraud by either rejecting suspicious transactions or flagging them for immediate investigation.

Forward-thinking players can explore the integration of artificial intelligence (AI) and machine learning (ML) – a venture with vast potential – into these existing initiatives. This technology synergy streamlines fast and precise analysis of vast amounts of data, enabling proactive detection of irregularities in transactions and the activation of block or reject mechanisms before any further harm can ensue, which translates to an enhanced efficiency of fraud detection and prevention.

Essentially, the adoption of AI and ML can allow DITOs to maintain a proactive stance and outmaneuver potential fraudsters to safeguard both their clientele and businesses.

4 Build a strong compliance culture

All regulatory policies and procedures must also be supported by clear accountability within the organization. It is imperative for DITOs to not only lay the foundation but also continuously strengthen a strong compliance culture. This entails elevating the standard of staff engagement and proficiency within this domain, and showcasing ethical leadership, so as to ensure a proper and effective implementation of AML/CFT measures.

11. [Stepping up the fight against financial crime](#), The Star, 28 July 2023

How KPMG can help

While BNM continues to enhance efforts in strengthening the resilience of financial institutions in managing ML/TF risks, setting up an AML/CFT compliance program appropriate to the size, nature and complexity of DITOs remains a challenge due to the principle-based nature of current laws and regulations.

At KPMG, we view DITO as game changers where tremendous opportunities await those who are ready to take the digital leap. KPMG's award-winning AML & Sanctions team can help you navigate the complex regulatory environment, design and implement new operating models, remediate past issues, design and test controls and transform organizational culture and capabilities to combat financial crimes effectively.

Together, we can help build a secure and resilient digital financial ecosystem that benefits both businesses and consumers.

This is Part 2 of a series of thought leadership by KPMG in Malaysia. Read the series at www.kpmg.com.my/dito.

Connect with our professionals



Mok Wan Kong
Partner – Head of Insurance
KPMG in Malaysia

T +603 7721 3009
E wmok@kpmg.com.my



Tan Kim Chuan
Partner – Head of Forensic
KPMG in Malaysia

T +603 7721 7052
E ktan@kpmg.com.my



Khurram Pirzada
Partner – Forensic, AML & Sanctions
KPMG in Malaysia

T +603 7721 7119
E khurrampirzada@kpmg.com.my



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