

Examining Compliance Cost Challenges in Suspicious Transaction Reporting among Financial Institutions in Malaysia: A Concept Paper

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ABSTRACT

Non-compliance with anti-money laundering (AML) laws and regulations, specifically in the timely submission of suspicious transaction reports, renders heavy penalties and unfavourable consequences for financial institutions (FIs) in Malaysia. As a result, FIs need to invest in high-cost compliance measures to mitigate the risk of regulatory breach. This paper aims to examine compliance costs challenges faced by FIs in the submission of high-quality suspicious activity reports, with the key area of concern including the demand for workforce expertise and enhancing technology for monitoring purposes. Additionally, this paper also explores the impact of non-adherence, which will cost FIs a hefty monetary penalty amount that adds to the potential compliance cost faced by FIs.

INTRODUCTION

Malaysia's Fifth National Risk Assessment on Money Laundering and Terrorism Financing 2023 (NRA 2023), published by Bank Negara Malaysia in its Annual Report 2024, revealed that fraud, corruption, illicit drug trafficking, organised crime, and smuggling remain the most prevalent crimes that pose a high money laundering risk. Money laundering has increasingly become a major global concern, primarily due to its cross-border nature involving the transfer of illicit funds across multiple countries. This illicit activity has raised growing alarm in Malaysia, as reported cases have shown a consistent upward trend in recent years.

As of September 2024, the Ministry of Finance revealed that the National Scam Response Centre (NSRC) received an estimated 22,000 cases of scams involving losses of over RM147 million (The Star, December 2024). As defined by Bank Negara Malaysia (BNM), money laundering is a process of converting cash, funds, or property derived from criminal activities to give it a legitimate appearance, and the process to launder the illegal source of funds generally consists of three main stages: placement, layering, and integration. Essentially, money laundering is the process through which illegally acquired money is concealed and later converted to appear as clean money.

In line with the international standards established by the Financial Action Task Force (FATF), the enforcement under the First Schedule of the Anti-Money Laundering, Anti-Terrorism Financing and Proceeds of Unlawful Activities Act 2001 (AMLA) in Malaysia imposes mandatory reporting obligations on Reporting Institutions (RIs) across both financial and designated non-financial business and professions (DNFBPs) sectors. The

framework outlines the obligations and requirements for RIs in implementing a comprehensive risk-based approach in managing money laundering, terrorism financing, and proliferation financing (BNM, 2024).

According to a guideline introduced by Basel Committee on Banking Supervision Consultative Document Sound Management of Risks Related to Money Laundering and Financing (2016), the financial crime compliance officer typically functions as part of the second line of defence, serving as a key layer of oversight and control in a financial institution's efforts to combat money laundering. Upon submission, the STRs are reviewed by the Financial Intelligence and Enforcement Department (FIED) of Bank Negara Malaysia, paving the way for possible investigative or enforcement actions, depending on the nature and severity of the reported activity.

Complying with STR requirements is fundamental in the fight against financial crime, but the process is not without challenges. Regulatory expectations can be complex and resource-intensive, often placing significant operational and financial strain on institutions. These challenges can affect how effectively STR obligations are carried out in practice. The cost of compliance should not be underestimated, as it can directly influence the quality, timeliness, and accuracy of STR submissions. When institutions struggle to meet these demands, there is a risk that critical information may be missed or delayed, potentially weakening the overall effectiveness of anti-money laundering (AML) efforts. Understanding and managing these costs is therefore key to ensuring STR compliance that is both efficient and meaningful.

Background of Study

Financial crime, particularly money laundering and terrorism financing, remains a serious global threat, undermining the stability and credibility of financial systems. Experian's (2024) latest report reveals that money laundering costs the United Kingdom's economy at least £100 billion annually, representing around 14% of the country's GDP. The report also indicates that nearly a third, or 23%, of retail banks reported ending customer relationships due to concerns related to financial crime in 2023. The development of strong AML frameworks plays a critical role in identifying and preventing illicit financial activities, with STRs serving as a central mechanism in this process. Mahmud & Ismail (2023) stated that AML legislation aims to curb money laundering using various strategies, policies, and laws.

In Malaysia, these obligations are enforced under the Anti-Money Laundering, Anti-Terrorism Financing and Proceeds of Unlawful Activities Act 2001 (AMLA). The law mandates that financial institutions submit STRs to the FIED of BNM in a swift manner. While STRs are essential for regulatory enforcement, compliance with these obligations can be operationally complex and financially burdensome.

This compliance burden, referred to as compliance cost challenges, is shaped by several interrelated factors. One major cost driver is workforce expertise, particularly the knowledge and training of compliance personnel who must understand regulatory expectations and effectively identify red flags. A previous study by Mahmud & Ismail (2023) identified a significant relationship between suspicious transaction reporting, employee training, and the effectiveness of AML regulations in Malaysian commercial banks.

Another significant factor is the role of emerging technologies, especially artificial intelligence (AI), in enhancing transaction monitoring and streamlining STR processes. Advanced AML/CFT technologies are recognized for their transformative potential in strengthening capabilities, particularly in the identification and tracking of suspicious transactions, rendering traditional investigation methods less effective (Nazri et al., 2019).

While AI has the potential to reduce manual workload and improve detection accuracy, the initial investment in such technologies can be prohibitively expensive for smaller institutions and may require specialized technical expertise to implement and maintain. In addition, the growing threat of regulatory fines and penalties places further pressure on institutions to ensure full compliance. The fear of incurring sanctions for non-compliance or inadequate reporting often compels institutions to over-invest in compliance infrastructure, further escalating operational costs. Despite the relevance of these factors, existing research often overlooks the specific cost implications of STR compliance, particularly in the Malaysian context. Most studies focus on the legal framework or the effectiveness of STRs.

Therefore, this paper aims to examine three key determinants that contribute to identifying the true compliance cost, which are primarily influenced by workforce expertise, emerging technologies, and regulatory penalties. These three core elements, if managed ineffectively, may pose a regulatory risk, particularly in complying with the requirements for submitting STRs.

Problem Statement

According to a report issued by LexisNexis Risk Solutions (2023) titled *The True Cost of Financial Crime Compliance in APAC*, pointed out that 98% of financial institutions in the region reported an apparent increase in compliance costs, which further stressed the growing regulatory pressure on the industry in combating money laundering and terrorism financing. The finding revealed that the total annual cost of financial crime compliance across Australia, China, India, Japan, and Singapore currently stands at an estimated USD 45 billion. China incurs the highest compliance cost in the APAC region, approximately USD 20.4 billion, followed closely by Japan at USD 17.8 billion (LexisNexis, 2023).

The Basel AML Index (2024) ranked Malaysia 67th out of 203 jurisdictions and 10th out of 23 countries within the East Asia and Pacific region, with an overall risk score of 5.50. The index score calls for immediate attention and urgent action to address the region's critical findings on financial transparency and standards.

Financial institutions are expected to maintain high regulatory compliance standards, which are known to be costly to the organisations. Global spending on compliance by financial institutions is estimated to exceed USD 100 billion, while large banks are reported to spend up to USD 1 billion on a yearly basis to uphold the regulatory compliance standards (Financial Crime Academy, 2025).

Thus, sustaining robust compliance efforts in order to meet regulatory standards is definitely complex and demanding task which often underestimated by financial institutions. In recent years, with stricter enforcement of AML/CFT regulations, there are three identified major determinants that contribute directly to the compliance cost in financial institutions, hiring AML/CFT expertise, processes that involve preventing money laundering, and technology adoption for transaction monitoring (Bakertilly,2024).

In a study by Yasaka (2020) found that, there are no universal rules, formulas or guidelines to determine whether transaction conducted is suspicious or not since financial institutions handle a wide range of daily transactions, including wire transfers and cash deposits or withdrawals which resulted the detection and decision-making process to report suspicious transactions relies heavily on the expertise, experience, and sound judgment of frontline staff, usually in close coordination with compliance officers or senior management at the head office.

Therefore, hiring certified technical expertise and personnel with an excellent understanding of regulatory knowledge should be key requirements in the hiring process. However, it becomes a challenge to the financial institutions because it often involves high labour costs, particularly to smaller firms. (Baker Tilly, 2024).

On the other hand, a study conducted by Oztas et al. (2024) found that experts have identified existing issues with the current practice applied in transaction monitoring mechanisms, such as high volumes of false positives, inefficiency, slow processing, and poor responsiveness to emerging risk bring major challenges to the financial institutions. FATF (2021), in its efforts to ensure AML/CFT global standards remain relevant and effective in a rapidly evolving digital landscape, expressed a positive outlook on the adoption of innovative technologies and business models in the financial sector.

However, the cost of implementing a new monitoring system can place a significant financial burden on institutions, especially for smaller institutions that operate with limited budgets and resources (Oztas et al., 2024).

American lawyers Lanier Saperstein, Geoffrey Sant, and Michelle Ng argue that without effective mechanisms to combat money laundering, terrorism financing and the new emerging risk of proliferation financing, specifically in the implementation of screening measures such as Know Your Customer (KYC) procedures and Customer Due Diligence (CDD) procedures which often involved identifying Political-Exposed Persons (PEPs)

and Ultimate Beneficial Owners (UBOs), financial institutions have faced sanctions by regulators and in some cases, banks have received severe penalties even though there are no actual money laundering took place under their supervision (Krecke, 2024).

Hence, in order to avoid non-compliance with money laundering laws and regulations, also to prevent any potential conflicts or penalties from authorities, financial institutions are under pressure to submit STRs promptly and accurately upon detection of unusual transactions (Yasaka,2020). Failure to submit STRs can lead to serious consequences, including monetary penalties imposed by regulators and potential harm to the institution's reputation.

Research Gaps

A series of studies (Gowhor, 2024; Yusoff et al., 2024; Latif & Rahman, 2018) stressed the importance of STRs submission as one of the core components of the AML/CFT. Although prior studies have hinted at the resource strain that adds burden to financial institutions (Rahman, 2013), the discussion on the compliance costs associated with STRs' obligations remains under-researched, particularly in Malaysia.

A prior study by Johari et al. (2023) highlighted that the employees' emotional intelligence, management support, and IT infrastructure significantly impact the decision to submit STRs. Thus, the compliance cost for these factors that contribute to the submission of high-quality STRs, such as personnel knowledge and training, the use of emerging technologies such as machine learning and artificial intelligence, and the impact of non-compliance, should be further explored in Malaysia, as limited research has been done in this context.

These three elements are likely to influence how institutions manage their STRs responsibilities. Any breach of these requirements could have significant negative consequences for these institutions. Hence, these gaps underscore the need for targeted research that investigates how workforce expertise, technological adoption, and regulatory pressures influence STRs compliance costs in Malaysia's landscape.

LITERATURE REVIEW

Workforce Expertise: Knowledge & Training

Tarmizi et al. (2022) emphasised that competency requires substantial experience and exposure, where Money Laundering Reporting Officers (MLROs) hold a key responsibility to be well-versed in the financial operations of money services businesses, which are often exploited by criminals and can become victims of money laundering schemes. Competencies refer to the knowledge, skills, abilities, and behaviours that allow individuals to effectively execute tasks and potentially increase their career opportunities in a competitive market (Azli & Haron, 2024)

Yusoff et al. (2024) also highlighted that with the right training, company staff can become more adept at identifying suspicious transactions and activities that may indicate money laundering and at disclosing such instances appropriately. Training, on the other hand, is a learning process aimed at changing attitudes and improving the knowledge and skills of employees to enhance their performance (Muis et al., 2021).

However, Tarmizi et al. (2022) also identified a significant gap in attitudes toward training between senior and junior management, while senior management generally views training positively, junior staff often struggle with AML responsibilities due to insufficient and unclear training.

According to the Association of Chartered Certified Accountants (ACCA) on its Anti-Money Laundering Training Fact Sheet, effective AML training should cover key topics such as red flags, relevant legislation and regulations, due diligence procedures, and handling suspicious transactions. Without providing such training, companies risk facilitating the flow of illicit funds into the legal financial system, thereby endangering the economy and becoming complicit in serious crimes, including drug trafficking.

Emerging Technologies: Artificial Intelligence

In response to evolving global AML/CFT threats, the FATF (2021) has demonstrated its commitment to adopting new technologies, understanding their capabilities and potential impact in the fight against money laundering. A study conducted by Yusoff et al. (2024) found that the application of new technologies, particularly in Artificial Intelligence (AI), to detect suspicious transactions may potentially reduce the compliance cost.

BNM, in collaboration with Payments Network Malaysia Sdn Bhd (PayNet) and 16 other financial institutions, has launched the National Fraud Portal (NFP) in 2024 (The Edge, 2024), which is designed to leverage AI to enhance the detection of suspicious transactions through predictive analysis with main features of modular design that allows for continuous improvements to be made on the existing basic infrastructure (Nawawi & Noor, 2024).

The implementation of AI in AML mandates the formulation of a robust regulatory framework to guide its deployment. This framework should encompass guidelines, policies, and laws that govern AI's development, application, and ethical deployment within the financial sector. Striking a balance between harnessing AI's potential and safeguarding against its pitfalls is paramount. (Tanuwijaya et al., 2023). The integration of artificial intelligence and machine learning into these systems has enhanced their ability to detect complex patterns and anomalies that would be difficult to identify through traditional methods (Betron, 2012).

AI-driven anomaly detection methods enable real-time identification of irregularities in transactional behaviour, allowing for proactive intervention to prevent illicit activities before they escalate (Zhang & Chen, 2024). Incorporating AI can improve the detection of transactional anomalies within STRs. However, financial institutions regulated by BNM must ensure that their implementation of AI aligns with ongoing advancements in technology integration.

Regulatory Fines & Penalties

As stipulated under Section 14 of AMLA 2001, RIs who suspect or have reasonable grounds to suspect any transactions, including attempted or proposed transactions that appear unusual and may indicate involvement in money laundering and terrorism financing, are legally required to submit STRs to BNM. Any non-compliance with the mandatory reporting obligation under AML/CFT regulations carries significant financial repercussions, which may entail hefty fines and penalties from authorities, thereby heightening the risk of institutions involved in potential reputational damage and regulatory scrutiny.

BNM as a competent authority appointed under AMLA 2001, which empowers the agency to take supervisory and/or enforcement action against any parties who breach the applicable laws and policies and in a series of annual reports from BNM stressed that the supervisory and enforcement actions taken to safeguard economic stability and protect the integrity of the financial system (BNM, 2024).

Based on the BNM Annual Report 2024, a total of 326 supervisory and enforcement actions were taken, and a substantial amount of administrative monetary penalties of RM 18.9 million were imposed against institutions regulated by BNM. According to the statistics released in the annual report, it disclosed that actions taken relating to anti-money laundering, countering terrorism financing, and countering proliferation financing (AML/CFT/CPF) present the highest number of 136 incidents, compared to other offences, prudential with 88 incidents, foreign exchange policies 87 incidents and others contributes to 15 incidents.

As highlighted in a report by The Edge Malaysia on May 30, 2024, AMMB Holdings Berhad (AmBank) has been penalised a staggering amount of RM 53.7 million by BNM, the largest fine ever imposed on a financial institution in Malaysia. The monetary penalty issued was related to the breach of regulatory compliance, including failure to report suspicious transactions linked to the accounts belonging to former Prime Minister, Datuk Seri Najib Razak, in connection with the 1MDB corruption scandal (The Edge, 2024).

In addition, AmBank has reached a global settlement of RM 2.83 billion with the Ministry of Finance (MoF) to resolve all outstanding claims and actions related to its involvement in the 1MDB case (MoF, 2021). The Group,

in its 31st Annual General Meeting (2022), announced that it had completed a four-year programme following BNM requirements in 2016 to improve and enhance the bank's overall operations from the perspective of governance and compliance.

The implication of these regulatory breaches, AmBank has invested a high compliance cost of RM25 million per annum for this specific initiative, which focused on system enhancement, infrastructure, and providing employees training.

Suspicious Transaction Reporting Among Financial Institutions in Malaysia

Suspicious Transaction Reports (STRs) are defined as documents that reporting institutions are required to submit when they suspect that a customer is involved in money laundering (ML), terrorism financing (TF), proliferation financing (PF), or other serious crimes (BNM, 2024). The main purpose of having these STRs is to offer law enforcement agencies valuable intelligence that can be used to help identify and investigate potential criminal activities (BNM, 2024).

BNM emphasizes the importance of submitting Suspicious Transaction Reports (STRs), as they provide critical support to the Financial Intelligence Unit and assist law enforcement agencies by supplying valuable information or intelligence related to potential criminal activities. The quality of Suspicious Activity Reports (SARs) contributes significantly to enhancing the effectiveness of legal enforcement (Loh X.T., 2021).

According to Harvey (2009), the conversion rate from prosecution to conviction may serve as an indicator of the quality of the SARs submitted. According to findings by Deloitte (2020), 62% of banking professionals identified increasing regulatory expectations and the intensified enforcement of existing regulations as the most pressing challenges in achieving AML compliance within the South Asian region. These rising demands have posed significant difficulties for compliance officers, potentially impairing their ability to exercise sound judgment and submit high-quality Suspicious Transaction Reports (STRs) (Deloitte, 2022; as cited in Jamil et al., 2022).

Empirical evidence suggests that regulatory enforcement is instrumental in shaping compliance officers' judgments regarding money laundering risks and their decisions to submit suspicious transaction reports (STRs) (Sanusi et al., 2022). In addition to regulatory pressure, internal organizational factors also influence reporting behaviour.

Chan et al. (2020) found a significant positive influence between a strong organisational climate and regulatory focus on the employees' intention to report suspicious transactions. These findings underscore the importance of external regulatory enforcement and internal institutional culture in fostering effective AML compliance.

A study by Rahman and Mohd Noor (2020) found that employees in financial institutions were more likely to report suspicious behaviour when organizational privacy safeguards were perceived as strong and aligned with regulatory standards.

In 2024, reporting institutions continued strengthening compliance efforts and boosting their mechanisms for detecting suspicious activities. These improvements contributed to a rise in the number of Suspicious Transaction Reports (STRs) filed, with 342,166 STRs submitted during the year, compared to 317,435 in 2023 (BNM Annual Report, 2024).

Conceptual Framework

The conceptual structure depicted in Figure 1.0 illustrates the challenges financial institutions face in meeting Suspicious Transaction Reporting (STR) requirements. The framework highlights workforce expertise, particularly knowledge and training, as a central determinant of effective compliance. At the same time, the increasing adoption of emerging technologies, especially artificial intelligence (AI), together with the growing exposure to regulatory fines and penalties, further intensifies the complexity and cost of STR compliance. These

components collectively shape the operational burden placed on financial institutions, underscoring the need for a deeper examination of how they influence the quality, timeliness, and efficiency of STR processes.

In response to these challenges, financial institutions must establish a strong compliance framework that not only fulfils regulatory expectations but also enhances public confidence in the economic system. A strong compliance framework is necessary because it ensures financial institutions can consistently prevent regulatory breaches while reinforcing trust and credibility among the public and stakeholders. Through prioritising human capital development and leveraging technological innovation, institutions can proactively address future AML challenges, maintain regulatory trust, and strengthen the broader economic environment's integrity and stability. Such an approach helps lower long-term compliance costs while improving the effectiveness and efficiency of AML/CFT controls, positioning financial institutions to navigate an increasingly complex regulatory landscape better.

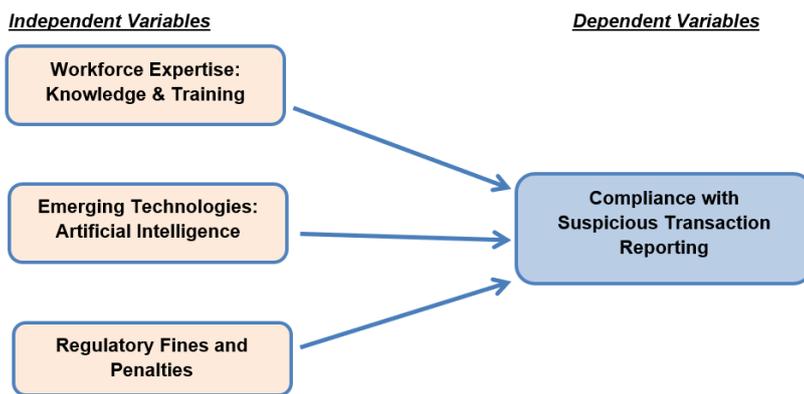


Figure 1.0: Conceptual Framework for Compliance Challenges Faced by Reporting Institutions to Comply with Suspicious Transaction Reports (STRs) Requirement

RECOMMENDATION

A skilled and knowledgeable workforce forms the backbone of effective anti-money laundering (AML) systems. As noted by Azli and Haron (2024), a compliance officer requires strong risk assessment evaluation skills to efficiently detect any suspicious transactions. Strengthening the AML/CFT training and awareness program, fostering a strong compliance culture among employees, and allocating sufficient resources for compliance functions to take place are essential to prevent non-compliance and act as preventive measures in the institutions. Employees who are well-trained in identifying suspicious transactions, understanding complex regulatory requirements, and applying critical judgment are far more likely to submit high-quality STRs that truly support law enforcement efforts.

Equally important is the strategic integration of advanced technology. FATF (2021) acknowledged that new technologies, including Artificial Intelligence (AI), Machine Learning (ML), and Natural Language Processing (NLP), are among the innovative tools that have transformed how financial institutions execute their AML/CFT obligations in today's digitalised environment. These technologies will assist financial institutions by improving real-time data analysis in large volumes, identifying hidden patterns, and flagging anomalies that might be overlooked during manual processes. As a result, compliance teams can focus their attention and resources on genuinely high-risk transactions, rather than being overwhelmed by low-priority or irrelevant alerts, ultimately improving both the efficiency and effectiveness of investigations (Lucinity, 2025).

Taken together, these recommendations should build a robust compliance framework that not only meets regulatory expectations but also reinforces public confidence in the financial system. Prioritising human capital and technological innovation, financial institutions can position themselves to adapt proactively to the future AML challenges, maintain regulatory trust, and contribute meaningfully to the integrity and stability of the wider financial ecosystem, which can reduce compliance costs while increasing effectiveness and efficiency.

The combination of people, process, and technology forms a powerful foundation for addressing the complex decision-making required in effective AML/CFT compliance. Skilled personnel, a well-designed process through leveraging technology in financial institutions, can build a robust and adaptable compliance culture. Effective and efficient preventive measures reduce the risk of regulatory breaches and the associated penalties.

CONCLUSION

Addressing compliance costs is vital to ensure the long-term sustainability of financial institutions. High-profile cases involving breaches of money laundering regulations, such as the Danske Bank Estonian branch scandal (2007–2015) and the 1MDB case, which was exposed in 2015, have demonstrated how major local and international banks, including AmBank and Goldman Sachs, can become entangled in such violations. These incidents not only resulted in hefty monetary penalties and reputational damage to the institutions but also inflicted other damages on stakeholders, including undermining public trust and shareholder confidence.

Employees' aptitude and understanding of submitting quality STRs requires continuous training and consistent enhancement of their AML/CFT knowledge and skills. Management should, at all times, prioritise the capacity by strengthening their compliance culture as a continuous effort to minimise the risk of errors or non-compliance, and reduce the likelihood of costly regulatory fines. Ultimately, investing in hiring competent personnel and professional expertise, as well as embracing technological advancements, will significantly help financial institutions to remain resilient and sustainable in their fight against money laundering.

This integrated approach not only mitigates the risk of breaches but also demonstrates a proactive commitment to upholding the integrity of the financial system in an increasingly complex and regulated environment. Financial institutions should remain vigilant about the key factors that can contribute to regulatory breaches. Vulnerabilities, including inadequate training, weak internal controls, outdated monitoring systems, and poor data security, may pose a significant risk of non-compliance, which can expose institutions to substantial regulatory penalties, reputational harm, and loss of public trust.

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