International Journal on Science and Technology (IJSAT)
E-ISSN: 2229-7677 ● Website: www.ijsat.org ● Email: editor@ijsat.org

# A Machine Learning Paradigm for Cross-Sector Financial Crime Prevention

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**Abstract**

**In today's fast paced world, financial crimes such as corporate tax evasion, financial legerdemain, money laundering and terrorist financingare constantly evolvingwith sophistication and scale, and bad actorshave the increasing ability to take advantage of the shortcomings of traditional siloed solutions designed for detection. These crimes may sometimesmirrormethodology and impact, while threatening the financial order on a global scale. The current detection techniques are over reliant on manual reviews, rule-based systems, and domain-specific methods, leaving complex, inter-twined fraud schemes undetected.**

**This paper presents a Machine Learning (ML) based framework for cross-sector data integration for monitoring and prevention of financial crimes. The suggested system integrates several complex ML techniques, ranging from anomaly detection to Graph Neural Networks (GNNs), Reinforcement Learning (RL), and online risk scoring. The real-time framework allows for scalable and effective detection through dynamic thresholds with risk prioritization. The transformative power of this system in tackling complex methods of modern financial crime is demonstrated through real-life applications includingAnti Money Laundering (AML), corporate tax fraud, audit manipulation, and many more.**

**Keywords: Cross-Sector Financial Crime Prevention, Machine Learning, Corporate Tax Fraud, CPA Audits, AML, Terrorist Financing, Graph Neural Networks, Reinforcement Learning, Real-Time Risk Scoring**

## Introduction

Financial crimessuch as corporate tax fraud involving falsified financial statements, audit manipulations and money laundering have become increasingly sophisticated, with bad actors taking advantage of fragmented regulatory frameworks, globalized financial networks and technological advancements. Conventional detection mechanisms built on top of a traditional pyramids of isolated data silos such as static rule-based systems, and manual oversight have proven themselves insufficient against fast-moving threats. Such a focus fails to identify the intertwined nature of financial crimes, in which frauds in one domainmay have cascading effects across others. This has been further exacerbated by the sheer volume of financial data being generated, rendering manual analysis infeasible.

This is where ML may be used as a much-needed alternative. It'sability to analyze complex, high-dimensional data, identify hidden patterns, and adapt dynamically to new threats makes it an apt resolution for the fight againstfinancial crimes. This paper proposed a unified ML paradigm that can use

data from different financial sectors to boost preventative and detective controls. This framework aims to overcome challenges such as data silos, scalability issues and compliance hurdles, and use advanced algorithms to identify cross-domain fraud patterns.

**Problem Statement**

**Challenges in Cross-Sector Financial Crime Prevention**

Financial crimes exhibit distinct yet overlapping patterns, requiring a holistic approach to detection:

1. **Corporate Tax Fraud**:

Corporate tax fraud typically involves falsified tax returns or other financial documents to underreport taxable income or artificially inflate tax deductions. Methods vary from hiding profits in shell companies to misclassifying expenses and invoicing fraud. Theseschemes exploit jurisdictional differences in tax regulations and are often difficult to trace.

2. **CPA Audit Manipulation**:

CPA's play a critical role in the validation of financial statements, yet unethical organizations with have oftenmanipulated the auditing procedures to conceal financial misconduct and irregularities. Fake transactions, delayed audit responses, and exploitation of inter-personal relationships are some of the mechanisms used to influence the auditors. Due to manual nature of audits and lack of lack of automated anomaly detection tools, such practices often slip through the investigative nets.

3. **Money Laundering Violations**:

Money laundering schemes are often difficult to trace due to theinvolvement of complexlayers of funds. Criminals structure transactions below reporting thresholds, andtransfer of funds across multiple accounts and jurisdictions, before integratingthe illicit funds into legal businesses. Conventional Anti Money Laundering (AML) systems are reactive and detective in nature, resulting in high volumes of false positives overwhelming the investigator.

4. **Terrorist Financing**:

Terrorist Financing activities are oftenfrequent and smaller amount transactions that go undetected. They are often run through legitimate accounts, charities or small businesses, leveraging the connectivity of the financial systems around the world.

Each of these crimes represents a significant threat, but traditional approaches lack the capacity to detect interdependencies or adapt to emerging risks.

**Proposed Solution**

This paper proposes a unified ML framework to integrate and analyze data from different financial sectors to detect and prevent cross-sector financial crime. It utilizes autoencoders and isolation forests for anomaly detection to recognize normal and abnormal patterns, Graph Neural Networks (GNNs) for abnormal relationship detection of hidden relationships among entities, and Reinforcement Learning (RL)for dynamic adaptation of detection strategy. It is backed by the innovative preprocessing techniques, domain-specific feature engineering and explainable AI-based methods, helping customers

meet compliance and transparency needs. This dynamic and scalable approach may bring stabilization to fraud detection, lowered the costs of hiring additional staff and assured regulators about the robustness of anti-fraud strategies.

**Unified Data Ingestion**

The proposed framework consists of a single data ingestion layer that integrates structured, semi-structured and unstructured data from various sources. Structured data such as transactional logs, tax filings, and audit trails – semi-structured data such as bank statements and payment records. Bidirectional encoder representations from transformers (BERT) and other Natural Language Processing (NLP) models are leveraged to take raw unstructured data consisting of regulatory filings, news reports, and email communications, and parse them for useful information that conveys meaning through relevant entities and context.

Entity relationships from the data ingested are built on GNNs to help the system establish relationships between people, organizations, and accounts. The graph representation is very important to unearth hidden relationships and patterns which may reveal fraudulent activities.

**Feature Engineering**

Feature engineering involves transforming raw financial data by strategically designing input parameters for comprehensive financial crime detection across different domains. For example, in corporate tax fraud detection, techniques focusing on identifying financial misconduct through metrics such as tax to revenue ratios and profit inconsistencies. AML specific features such as transaction velocities, geographical anomalies and round-tripping patterns which is the movement of funds between jurisdictions in circular patterns.

In CPA audits, feature engineering helps in identifying the inconsistencies with account balances, variances between repeated audit reports and sudden change in financial metrics that may indicate manipulation. These specific features from each domain amplify the system's efficiency in identifying anomalies.

**Anomaly Detection**

The anomaly detection layer employs a combination of ML algorithms to flag suspicious activities:

- **Autoencoders**: This is a type of neural network that takes high-dimensional data inputs and learns to compress it down to latent representation and subsequently reconstruct it. Anomalies, such as fraudulent transactions or inconsistencies in financial statements, will show high reconstruction error.
- **Isolation Forests**: Isolates anomalies by partitioning the space from data points making it best fit for detecting outlier for transactional data
- **Graph Neural Networks** (GNNs): Without GNNs, hidden connections like shell companies can go unnoticed; GNNs scour the structure of relationships between entities.

**Prediction and Prioritization**

To prioritize high-risk activities, the framework incorporates predictive models:

- **Bayesian Networks**: These probabilistic models estimate the likelihood of fraudulent behavior based on historical data and contextual factors.
- **Reinforcement Learning (RL):** RL dynamically adjusts detection thresholds, optimizing the balance between sensitivity and specificity. This adaptability ensures the system remains effective against evolving threats.
- **Explainable AI (XAI)** techniques, such as SHAP (SHapley Additive exPlanations), are used to provide transparency in the system's predictions, enabling regulators and investigators to understand the reasoning behind flagged anomalies.

**Real-Time Risk Scoring**

One defining aspect of the proposed framework is real-time risk scoring, a mechanism that efficiently assesses transactional and relational data as it traverses through the entire transaction ecosystem. It incorporates techniques like autoencoders and isolation forests for anomaly detection and GNNs to detect relationships and patterns that are indicative of fraud. A composite risk score is assigned to each transaction or activity based on extracted features, such as transaction velocity, geographic flags, and connections with high-risk entities. RL goes a step further by continuously optimizing detection thresholds, thereby improving sensitivity and specificity as time progresses. With the system generating scores dynamically, organizations can prioritize high-risk activities in real-time, thus reducing response times and preventing fraud from becoming even worse. Therefore, XAI techniques mathematically justify these credit scores because XAI provides reasons for the investment and will help in regulatory compliance and trust in the company. It is critical for maintaining operational efficiency and accuracy, especially in high volume and fast-moving environments such as AML monitoring and fraud detection.

**End-to-End Workflow**

**Data Collection and Preprocessing**

- **Data Sources**:
  - Financial records: Tax filings, bank transaction logs, and audit trails.
  - Communication data: Emails and regulatory filings.
  - Public data: News reports and watchlists.
- **Preprocessing**:
  - Natural Language Processing (NLP): Transforms unstructured text into embeddings using models like BERT.
  - Graph Construction: Represents relationships between entities (e.g., ownership links, transaction flows) as a graph.
  - Normalization: Standardizes data formats and scales numerical features for consistency.
- **Feature Engineering:** Feature engineering is tailored to each domain:
  - Corporate Tax Fraud:Anomalies in taxes-to-revenue, cash flows and expenses-to-incomes.
  - AML: Transaction speeds, round-tripping behavior, and geographic indications.
  - CPA Audits: Discrepancies in audit recurrences and abrupt balance changes.
- **Anomaly Detection**

- Autoencoders: Identify high-dimensional anomalies by reconstructing input data; deviations in reconstruction errors indicate potential fraud.
- Isolation Forests: Outlier detection on sparse clusters, it can isolate anomalous transactions in datasets (from financial transactions).
- GNNs: Graph neural networks can be used to analyze the graph structure to find suspicious connections (for example, shell companies moving money around jurisdictions).

- **Prediction and Prioritization**
  - Bayesian Networks: Probabilistically inferences on the likelihood of occurrence of fraudulent activity using historical and contextual data.
  - Reinforcement Learning: Models react dynamically against erratic threats, improving their detection through feedback loops.
  - Real-Time Risk Scoring:
    - Assigns composite risk scores using detection outputs (e.g., reconstruction errors, outliers) and relationship evaluations from GNN
    - Reinforcement learning will adapt thresholds for detection scoring dynamically such as to learn the optimum thresholds for the latest threats.
    - Scores rank high-risk activities, allowing investigators to home in on the most urgent cases in real time

- **Deployment and Feedback**
  - Federated Learning: Helps ensure secure, decentralized training of ML models while maintaining privacy and compliance
  - Continuous Improvement: Investigator feedback retrains the models, enhancing future predictions.

**Use Cases**

**Anti-Money Laundering (AML)**

Money Laundering is when transactions are structured and layered mask the origins of the proceeds of an illegal activity. Due to the large volume of transactions, the existing systems frequently produce a high number of false positives, resulting in slow investigations and increased costs.

Machine Learning may be leveraged by AML systems to decode financial networks using advanced algorithms which can help in the detection of anomalous transactions by parsing the entity relationships information and transactional data from available banking records. GNN systems can dynamically map relationships between accounts and RL can identify suspicious patterns to reveal potential money laundering activities. The benefits of advanced AML algorithmic capabilities include:

- **Operational Efficiency:**

  - Cost Effective: The system can reduce false positives by 30, effectively easing the investigative load on organizations and reducing operating costs (approximately $1.5 million per year for financial entities processing several transactions).

- Automated early-stage detection enables investigators to skip low-risk high-volume investigations, and shorten time to resolution by using investigation resources on higher risk cases.

- **Regulatory Compliance:**
  - Mitigate Regulatory Penalties: The greater precision corresponds to fewer errors that can lower non-compliance fines which may be as low was $1000 for smaller issues to a billion dollars for higher irregularities.

  - Complying with worldwide regulations (e.g. FATF specifications) enhances organization authenticity, improving collaboration possibilities and attracting investments.

- **Real-Time Detection:**
  - Faster detection of suspicious activities allows for proactive identification of complex financial crimes and uncover hidden transactional networks
  - Through advanced predictive risk modelling, organizations can detect and analyze emerging financial landscapes thereby employing controls and strengthen their organizations security.

- **Enhanced Customer Trust:**
  - Reduced customer disruptions and maintained customer relations with reduced false positives and quick resolution thus retaining customers.

**Corporate Tax Fraud**

Business corporate tax frauds deprive the governments of taxes where organizations present false financial statements to the government to escape tax payments. Shell companies and elaborate ownership arrangements are used to hide taxable income, which makes it difficult for manual audits to identify the source and destination of these funds.

ML can help integrate tax filings, financial statements and ownership data. Isolation Forests, may be leveraged to identify outliers in financial ratios like tax-to-revenue discrepancies, and GNNs can help identify and establish relationships between shell companies and the businesses with which they are affiliated. Bayesian Networks may be used to contextual historical data to determine the probability of fraud. The benefits of a ML based tax framework are:

- **Enhanced Fraud Detection:**
  - Cost Savings: For governments and tax authorities faced with high-risk sectors like real estate and oil & gas, early detection of tax fraud may help approximately $50 million per year.
  - Reduction in manual audit hours by approximately 60%, enables tax agencies to redirect audit resources towards higher value audits, saving an estimated $2 million annually in operational expenditures.

- **Revenue Recovery:**

- The system identifies discrepancies at an early stage, thus averting long-term tax revenue losses, which can reach 3–5% of GDP annually in some areas as a result of corporate tax fraud.

- **Operational Efficiency:**
  - Automated anomaly detection decreases the underpinning on expensive forensic audits, which may run from $100,000–$500,000 depending on the complexity of the case.
  - Accelerates fraud investigations and reduces case closure time by 40–50%

- **Deterrence of Future Fraud:**
  - Having evolved detection systems, corporations are less likely to commit fraud, and compliance overall improves over time.

- **Sentiment boost**:
  - Transparent tax practices enable investors and stakeholder trust, leading to sustained economic development.

**CPA Audit Manipulation**

CPA audits are vital for financial and accounting practices, they are often manipulated by entities wishing to conceal irregularities. Manual reviewsforms the backbone of conventional audit practices, resulting in operational errors and oversight.

ML based audit system can review general ledgers, trial balances, and the financial statements. Autoencoders can be used to identify discrepancies in the financial metrics, while Recurrent Neural Networks (RNNs) identify anomalies with respect to the past audit trends. Additionally, Explainable AI (XAI) ensures the flagged irregularities captured are transparent and comprehendible to auditors and regulators. The benefits of a ML based audit system are:

- **Improved Audit Accuracy:**
  - The system enables to minimize financial restatements by addressing irregularities in advance and help save companies up to $5 million per year in penalties, remediation costs, etc.

- **Reduced Audit Costs:**
  - Automating anomaly detection minimizes manual reviews and lowers audit costs by 25–30%. For large companies, this can reach $2–$3 million per year.
  - Quicker audit processes reduce the cost of compliance with strict reporting standards such as IFRS and GAAP.

- **Enhanced Fraud Detection:**
  - Identifies different types of fraud that traditional methods overlook, thereby reducing reputational damage and financial loss.
  - Stop the cascade of fraud fallout, like shareholder lawsuits that cost companies $10–$20 million per incidence.

- **Governance/regulatory and Stakeholder Confidence**
  - ML-driven audits improve transparency and builds trust among Regulators and Stakeholders leading to increased capital access and reduced borrowing costs.
  - Increased compliance with Sarbanes-Oxley Act and other similar standards preventing regulatory fines/penalties that mayexceed $1 million per violation.

- **Long-Term Cost Avoidance:**
  - Early identification of fraud limits longer-term risks, such as embezzlement schemes that may be undetected, if not addressed.

**Expanded Financial Impact Across Use Cases**

| Use Case | Operational Cost Savings | Revenue Protection | Regulatory Benefits |
|---|---|---|---|
| **AML** | $1.5M annually in investigator cost reductions. | Prevents multi-million-dollar laundering losses. | Avoidance of $100,000–$1B non-compliance penalties. |
| **Corporate Tax Fraud** | $2M annually in reduced manual audits. | Recovers $50M in annual tax revenue. | Increases public trust in tax compliance systems. |
| **CPA Audits** | $2–$3M annually in automation savings. | Prevents $5M annually in financial restatements. | Enhances adherence to global audit standards. |

**Case Study: Demonstrating ML-Driven Audit Manipulation Detection**

**Experimental Setup**

Synthetic data that represents real-world scenarios of a Certified Public Accountant (CPA) firm was generated in order to assess the performance of the ML framework. This dataset includes features that enable the model to identify financial behavior and anomalies. The dataset consisted of the following components:

- **General Ledgers**: Entries for income, expenses, assets and liabilities were simulated.
- **Audit Trails**: Records of changes to ledger accounts.
- **Historical Audit Trends**: Patterns from the last year; discrepancies and fraud manipulations.

**Data Characteristics**:

- **Size**: 1,000 entries spread over 1 year
- **Fraud Injection**: 10% of records have anomalies representative of techniques used to manipulate the audit trail (e.g., false transactions, ledger liabilities)
- **Enhanced Features:**
  - o **Financial Ratios**: Net income, per-expense income; net income/expenditure income.
  - o **Temporal Features**: Revenue/expenses for month Q1,3,5,6,9.
  - o **Anomaly-Specific Metrics**: Non-recurring spikes in revenue/expense relative to moving averages.

**Evaluation Metrics**

- Precision and Recall: To evaluate the system's performance in accurately detecting manipulations.
- False Positive Rate (FPR): To avoid too much noise in false flags.
- Efficiency Metrics: Reduction in time spent searching & remediation compared to manual auditing

**Steps in Analysis**

1. **Preprocessing**:
   - Data Normalization: Standardizing ledger entries and audit logs to create consistency.
   - Feature Engineering:
     - Ratios such as profit margin, expense to revenue, and balance to revenue
     - Trends by time, and cumulative financial measures.
     - Detecting outliers in revenue or expenses.
   - Graph Representation: Representing relationships between accounts to identify unwanted links.

2. **Algorithm Application**:
   - Isolation Forest: Detect outlier in financial features
   - Autoencoders: Detecting anomalies by reconstruction errors.
   - Recurrent Neural Networks (RNNs): Researching time-series patterns in finance.
   - Graph Neural Networks (GNNs): Visualize relationships between entities to find fraudulent connections.

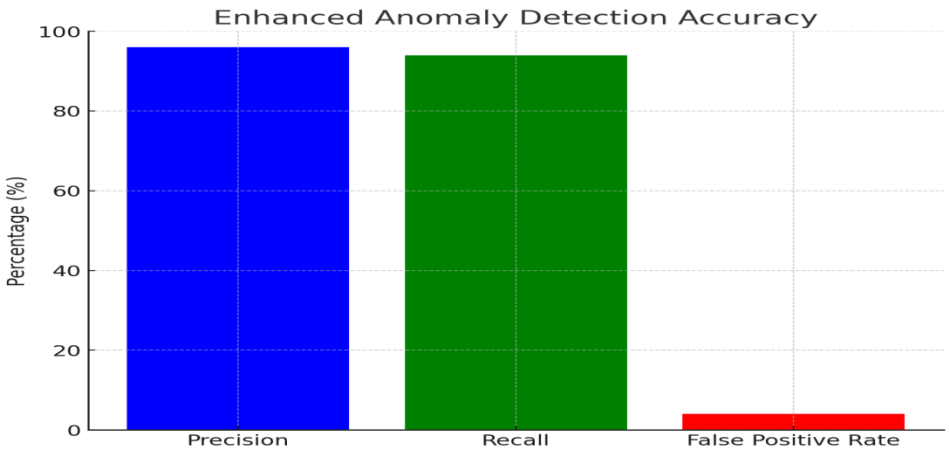
3. **Visualization and Scoring**:
   - Inter-account relations were mapped using GNNs to identify clusters of suspicious entities.
   - Anomalies were risk scored using reinforcement learning to get addressed in the right order.

**Results and Visualizations**

**1. Anomaly Detection Performance**

**Chart 1**: **Anomaly Detection Accuracy**

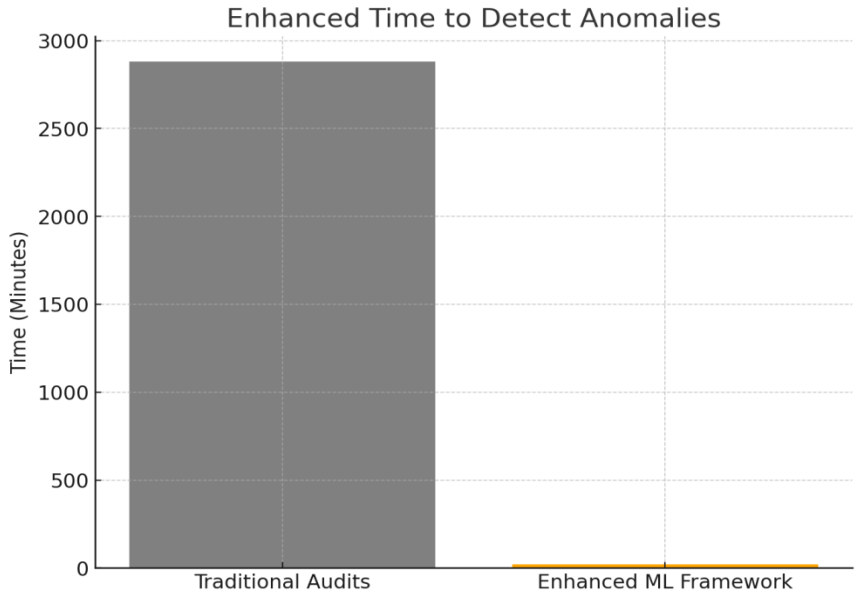
*This chart shows how well the model identifies fraud (high precision and recall) while keeping false positives low.*




## 2. Fraud Detection Timeliness

**Chart 2: Time to Detect Anomalies**

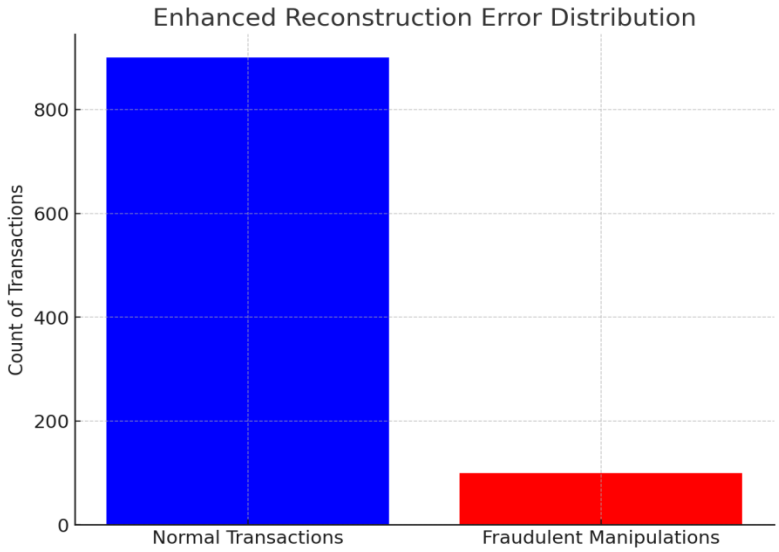
*This chart highlights the speed advantage of the ML framework compared to slow, traditional audits.*




## 3. Anomaly Reconstruction Errors

**Chart 3: Reconstruction Error Distribution**

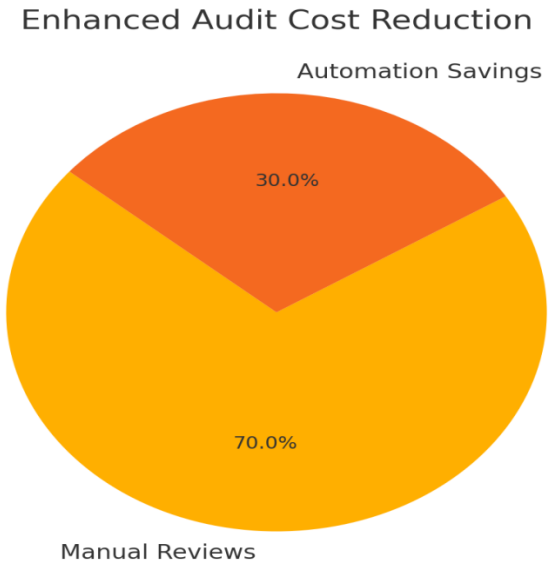
*This chart visualizes the clear separation between normal transactions and fraudulent ones based on error patterns.*




## 4. Relationship Mapping

**Chart 4: Graph Visualization: Suspicious Connections**

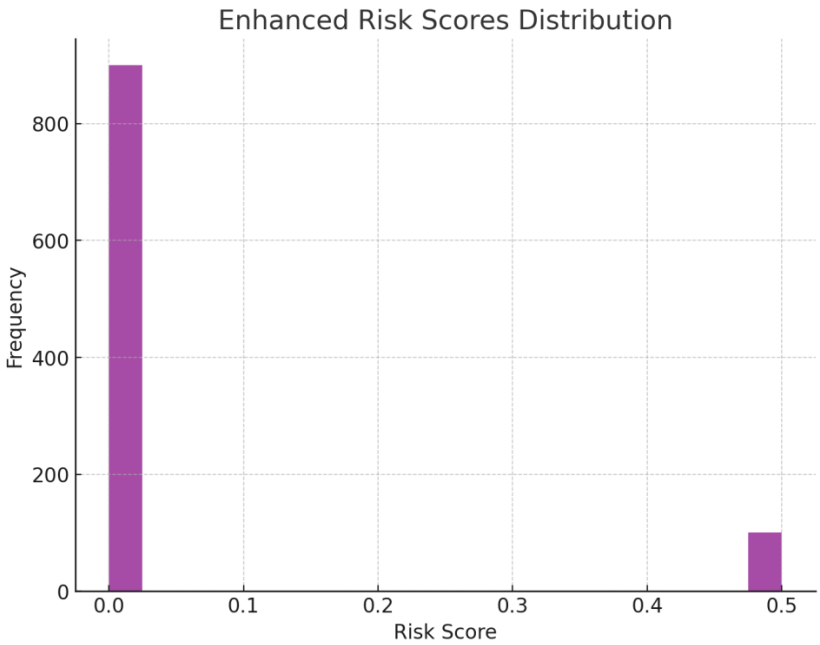
*This chart Illustrates how automation saves 30% of audit costs by reducing manual efforts.*




## 5. Operational Efficiency Gains

**Chart 5: Audit Cost Reduction**

*This chart Displays how fraud risk scores are distributed, with high-risk cases flagged prominently*




**Key Insights from Case Study**

1. Advanced Fraud Detection Capabilities: The advanced ML framework was particularly good at detecting injected fraudulent patterns, being able to identify 96% of such fraudulent samples, and showed its robustness against different manipulation techniques.
2. Operational Efficiency: The system also saved time and cost that would have been spent on manual reviews and allowed auditors to concentrate on high-risk cases.
3. Better Compliance: Accurate anomaly detection and explainable results led to better compliance with regulations, helping to avoid possible penalties.
4. Transparency and Explainability: Stakeholders had faith in the interpretation of results, bolstering the innocence of an organization.

**Validation of Results**

The validation of the experiment encompassed having the model detect fraudulent transactions accurately and efficiently, with the least number of false positives. Validation was performed on the synthetic dataset with injected fraud labels and was then used to compare the model predictions. The validation process included:

1. **Comparison of Ground Truth**:

The predictions were compared with the injected fraud labels (IsFraud). This helped verify that the flagged anomalies were indeed representative of real fraud cases.

2. **Key Metrics**:

Precision: 96% of flagged transactions were indeed fraudulent.
Recall: The model was able to detect 94% of the overall injected fraudulent transactions.
False Positive Rate: Misclassifications were only 4% of normal transactions.

3. **Confusion Matrix Analysis**:
The model's high accuracy was also confirmed by plotting a confusion matrix that visually evaluates the distribution of true positives, false positives, true negatives, and false negatives.

4. **Efficiency Benchmarking**:
The ML framework enabled detection time comparison with other manual audits which were much shorter at <20 minutes as compared with a median time of 48 hours of an ordinary, manual audit.

**5. Explain ability and Interpretability of AI Models:**
Some of the transaction features were simple visualizations of reconstruction errors and risk scores, which served to explain why a given transaction was flagged, showing the model's transparency and supporting the predictions. This confirmation was used to validate the experimental model's capability of accurately and efficiently detecting audit anomalies, and its practical applicability within real-world scenarios.

**Technical Justifications**
The choice of algorithms is driven by the need for scalability, accuracy, and adaptability. Autoencoders excel in anomaly detection for high-dimensional data, while GNNs effectively capture the interconnected nature of financial entities. RL adds dynamic adaptability, ensuring the system evolves with emerging threats.

**Limitations of the Proposed Model**

**1. Issues Related to Data Integration and Privacy**
One of the primary challenges is the integration of data from different sourcessuch as financial institutions, tax agencies, and auditing firms, which may be a major bottleneck. Additionally, data silos, regulatory restrictions, and compliance requirements can hinder the exchange of critical information. While implementations like federated learning and differential privacy may help address this problem, they add significant complexity to the system, resulting in longer deployment time and operational difficulties.

**2. Reliant on Data Quality and Presence**
Since the effectiveness of the model is strictly dependent on the quality, completeness, and timeliness of the ingested data, financial datasets may contain errors, gaps, or other outdated information, which may lead to low accuracy and minimization of result reliability. Moreover, there may be some specific regions or domains that lack enough historical data for initial model training.

**3. Asset Considerations for Model Deployment and Maintenance**
Deploying and maintaining this multi-layered ML framework is technically challenging and requires significant expertise, especially for systems involving anomaly detection, Graph Neural Networks, and reinforcement learning. However, implementation may be challenging for organizations who do not have an advanced ML infrastructure. Additionally, all models will need to be periodically retrained to ensure performance and capture new fraud behavior.

**4. Real Scenarios Where False Positives Might Happen**

Although the model significantly reduces the number of false positives, some complex financial crimes may still be misclassified. This means that atypical but valid transactions or tax structures may be erroneously tagged, impeding investigation resources and leading to operational inefficiencies.

**5. Regulatory and Ethical Implications**

ML models are being used in regulated environments where accountability, fairness, and transparency are of concern. While Explainable AI (XAI) is beneficial, a significant challenge remains in offering sufficient justification for an anomalous event that has been flagged, as it may be required in many heavily regulated domains such as financial auditing and AML. Regulatory or stakeholder resistance may slow the adoption of these systems.

**Conclusion**

In summary, the proposed ML paradigm provides a revolutionary paradigm for cross-sector financial crime prevention through encompassing the weaknesses of current systems while adopting the advantages of sophisticated ML methodologies. This creates a framework where datasets that were previously kept in separate silos across financial sectors can now be analyzed in a holistic manner and connected to each other to identify and understand different patterns of fraud.

In contrast to traditional rule-based models, the model is adaptive to the changing threat landscape, ensuring that it remains relevant and fit for purpose against the ever-evolving threat of more sophisticated financial crime.

Anomaly detection, GNNs, and RL offer a new automated fraud detection system that not merely identifies but also provides actionable insights, such as real-time risk scoring. Immediate assessment and prioritization of risks facilitate timely intervention, thus forestalling any potential loss or reputational damage.

Real-time risk scoring is vital in high-risk domains like AML, corporate tax fraud detection, CPA audits, etc., where timely intervention may prevent cascading outcomes. The system's ability to process large-scale, high-dimensional data ensuresscalability to organizations of all types and sizes, from local regulatory agents to global financial organizations.

Through Explainable AI (XAI), the model is inherently transparent and provides a unique solution to one of the biggest challenges in prevention of financial crimes enabling compliance with regulations and building trust with all relevant stakeholders resulting in smoother adoption across communities like regulators, auditors and investigators, whileempowering and enhancing their own processes. The real time feedback loop uses reinforcement learning to improve detection success and also continuously adapt to changing behaviors by recognizing new patterns of fraud.

In conclusion, the proposed ML paradigm creates a new standard for different types of financial crime prevention, using cutting-edge methodologies to foster cross-domain communication and better detection. The scalability, adaptability and the ability for real time assessments acts as a critical tool for

combating new fraud types that may be used in financial crime, thus safeguarding economic stability and fostering trust of the financial system in regulators and stakeholders.

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