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Federated Learning Framework for Cross-Institution Transaction Velocity and Anomaly Detection in KYC Systems

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Abstract:
As financial institutions around the world are being subject to increasing regulatory requirements and the challenge to identify fraudulent activities grows, there has been a need for secure and efficient scalable solutions in Know Your Customer (KYC) processes like never before. Traditional techniques for Know Your Customer (KYC) systems based on centralized data and static regulation are not up to the task of dealing with the complexities of cross-institutional collaboration and dynamic regulatory environments. This paper proposes the design of a Federated Learning Framework for cross-institution transaction velocity, and anomaly detection in KYC systems that enables privacy preserving decentralised learning in the context of cross-institution learning with data security and regulatory compliance concerning jurisdictional regulations.

The framework combines federated learning (FL) with anomaly detection algorithms and transaction velocity analysis in order to improve unstable transactions (i.e., suspicious activity) in real time without exchanging sensitive data. Using blockchain technology for secure identity management and Self-Sovereign Identity (SSI) framework for decentralized data verification, this system ensures that customer data is private and secure. Our outcomes indicate that the framework is significant in enhancing the accuracy of detecting anomalies and verification transactions than the traditional centralized system.

By exploiting the power of federated learning, financial institutions can work together and exchange insights without compromising customer data privacy. This research makes a contribution to the growing body of knowledge to privacy-preserving machine learning, and its application in KYC systems by proposing a scalable and secure solution for modern financial institutions to fight against money laundering and fraud in a globalized financial system.

Keywords: Federated Learning, KYC Systems, Transaction Velocity, Anomaly Detection, Privacy-Preserving Machine Learning, Cross-Institutional Collaboration, Blockchain Technology, Self-Sovereign Identity, Anti-Money Laundering (AML), Financial Fraud Detection, Decentralized Data Learning, Regulatory Compliance, Risk-Based Compliance.

INTRODUCTION

In the rapidly evolving world of global finance, Know Your Customer (KYC) and Anti-Money Laundering (AML) compliance have become an important part in preventing financial crimes like money laundering, fraud and financing of terrorism. Financial institutions have an obligation to ensure that customer identities are accurately verified, and also ensure transactions are monitored for suspicious activity. Traditional KYC systems, which tend to be centralized and based on static rules for compliance have dedicated their system to globalization, and to meet the need of a world where transactions sometimes cross states and are also multiple-jurisdictional, create still more complications.

One of the most pressing issues concerning global compliance on know your customer on an institutional level is the need that such institutions collaborate to detect cases of fraudulent activities across regions without compromising the data privacy and security of these institutions. Financial institutions, for example, are reluctant to share sensitive information about their customers due to the regulatory requirements, data protection regulations such as the General Data Protection Regulation (GDPR), as well as the fear of data breaches. To address this problem, a decentralized, privacy-preserving, model that allows institutions to collaborate without disclosing customer sensitive data are of the utmost importance. Federated learning (FL), a machine learning technique where models can be trained using decentralized datasets, without sharing the data, has become a possible solution to this problem (McMahan et al., 2017). Federated learning enables joint learning model training without the need for data availability centers, not only safety of the privacy, but also solves the low efficiency of traditional KYC systems. Through federated learning, institutions can detect anomalies and transaction velocity collaboratively in real time while adhering to the jurisdiction's laws (Yang et al., 2019). By adopting blockchain technology and Self-Sovereign Identity (SSI) frameworks, it is possible to create systems that allow federated learning to provide secure and verifiable identity management in federated learning systems, further improving privacy and compliance for instances of KYC systems (Yu et al., 2020).

This paper proposes Federated Learning Framework for Cross - Institution Transaction Velocity and Anomaly Detection in KYC systems which aims to improve security, privacy and efficiency of transaction monitoring. The framework makes use of machine learning models to analyze financial transactions from one institution to another without violating privacy, meaning that no sensitive data is shared between one institution and another. By using federated learning in conjunction with blockchain technology, the system also guarantees that the data of customers is not only secure but also decentralized and in accordance with global regulations.

PROBLEM STATEMENT

Traditional KYC systems rely on centralised data storage and static compliance rules and have several limitations when it comes to working across institutions. These systems:

- Conflict to deal with complex multi-jurisdictional regulatory structures in different regions (Li et al., 2020).
- Are at risk of data breaches, because the sensitive information from customers is usually found in centralized databases (Shokri & Shmatikov, 2015).
- Do not have the flexibility to respond to changing regulations or to changes in financial crime patterns.

As financial institutions have started to operate more across international walls, the need for more dynamic, adaptive and safe systems is evident. The Federated Learning Framework proposed in this paper is an alternative that will allow institutions to jointly detect fraud and monitor the velocity of transactions without sharing data and ensuring regulatory compliance.

RESEARCH OBJECTIVES

The general aims of this research are therefore to:

- Design Federated Learning Framework in which cross-institution transaction velocity and anomaly detection can be improved in KYC systems.
- Integrate federated learning with block chain technology together with self-sovereign identity (SSI) to ensure data privacy and compliance.
- Evaluate the performance of the system in terms of accuracy of detecting anomalies and speed of verification of transactions compared to traditional centralized KYC systems.
- Demonstrate the scalability and adaptability of the proposed system to the global financial institutions for diverse jurisdictions

PROBLEMS WITH TRADITIONAL KYC SYSTEMS

Traditional KYC compliance systems tend to have centralized databases where the customer data reside and will be susceptible to data breaches and identity theft (Shokri & Shmatikov, 2015). Moreover, centralized systems are not able to efficiently handle cross-border compliance because they have different regulatory frameworks in different jurisdictions. Each country has its own set of rules with respect to KYC and AML, and it is difficult for financial institutions to standardize the compliance practices on a global level.

The rigidity of traditional systems also means that they are not capable of adapting to new risks, or patterns of new fraud, as they are occurring in real-time. For example, financial institutions may be challenged with implementing new regulations or with adapting to abrupt changes in economic conditions that can impact the risk of financial crime in a specific jurisdiction (Yang et al., 2021). These shortcomings lead to inefficiencies and increased costs of compliance as well as regulatory risk for institutions.

The imperative to have a dynamic, privacy-preserving solution that allows collaboration between the institutions while still preserving customer privacy has never been greater. The Federated Learning Framework proposed in this paper has the purposes to overcome these issues by making possible the secure and cross-institutional collaboration without sharing sensitive customer data.

FEDERATED LEARNING FOR KYC

Federated learning (FL) is a decentralized machine learning approach where a shared model is trained by multiple learning institutions without sharing sensitive data at each institution. Instead of gathering customer data into a central data store, FL gives institutions the ability to train models collaboratively on a local data store. The model updates are then shared with a central server where they are all aggregated into a global model without ever accessing the raw data (McMahan et al., 2017).

In the context of KYC systems, federated learning can be used to identify the anomalies in the velocity of transactions by analyzing data from different institutions without compromising the privacy of the customers. By federated learning, financial institutions can effectively use their joint data to model fraud detection and risk assessment, and comply with data protection laws (Li et al., 2020).

A key advantage of federated learning is that it can be performed in a privacy-preserving way, with techniques such as differential privacy and secure aggregation being used to ensure that sensitive information is not leaked. This approach is in accordance with the rising need for privacy-enhancing technologies in financial services (Nasr et al., 2019; Shokri & Shmatikov, 2015).

BLOCKCHAIN AND INTEGRATING SELF-SOVEREIGN IDENTITY

The combination of blockchain technology and federated learning can offer an extra level of security and privacy in KYC systems. Blockchain solves the issue of ensuring that data integrity is preserved but allowing institutions to verify transactions and identities securely. Using Self-Sovereign Identity (SSI), persons have control over their personal data, sharing relevant information when necessary for verification of Know Your Customer (KYC) (Yu et al., 2020). This way, sensitive customer data is never shared without explicit consent, making it a more secure and compliant solution for financial institutions and customers alike.

Moreover, blockchain-based solutions offer an immutable audit trail of the transactions it helps ensure that the KYC data is immune to any tampering and also maintain a track of it. This not only makes data security more secure but also regulatory transparency, as all the actions undertaken within the KYC system can be verified on the blockchain, thus making the process more auditable and compliant with global regulations (Li et al., 2020).

Table 1: FLA & Blockchain Integration in KYC

Component	Functionality	Benefit
Federated Learning	Allows institutions to train models on local datasets without sharing sensitive data, improving **anomaly detection** and **transaction velocity** analysis.	**Data privacy**, **real-time collaboration** across institutions.
Blockchain Technology	Provides secure, decentralized storage for KYC data, enabling transparent **identity verification** and maintaining **data integrity**.	**Security**, **tamper-proof** records, and **auditable transactions**.
Self-Sovereign Identity (SSI)	Empowers users to control their digital identity and selectively share relevant **KYC data**.	**Privacy**, **user control**, and **reduced data exposure**.

LITERATURE REVIEW

The process of financial technology evolving at a rapid pace has been a process that has brought significant improvements in the functioning of financial institutions. Know your Customer (KYC) processes which are traditionally based on manual verification and centralized systems are now being enhanced using automation, machine learning (ML) and blockchain technologies. In particular, Federated Learning (FL) has been proposed as a promising methodology for KYC and anti-money laundering (AML) compliance, supporting the collaboration together with insights between institutions, while maintaining the privacy and security of sensitive customer data. This literature review discusses the key concepts of federated learning, anomaly detection, transaction velocity analysis, and privacy-preserving machine learning in the context of the concepts of KYC systems.

FEDERATED LEARNING CA AND ANTI MONEY LAUNDERING (KYC)

Federated learning (FL) is a distributed machine learning method which allows multiple institutions to train a model together even though each institution does not have to share their sensitive data. Instead of aggregating raw data in the central repository, each system involved trains local models and only shares updates to the model parameters (McMahan et al., 2017). This framework is of particular benefit for KYC systems, where customer privacy is paramount, and the regulatory requirements are strict around data protection requirements.

In traditional centralized KYC systems, the customer data is stored in a central database which makes the data a potential target for cyberattacks and data breaches (Shokri & Shmatikov, 2015). Federated learning solves this problem because it never allows sensitive information about the customers to leave the institution's servers. Instead, the model is trained together without the disclosure of the specified data, limiting the risk of data leaks and complying with data privacy fees such as the General Data Protection Regulation (GDPR).

Federated learning has the additional benefits of facilitating real-time collaboration between institutions in order to identify fraudulent activities without the data sharing. This decentralized approach to training is particularly beneficial in the fight against cross-institutional financial crime, such as money laundering or fraud on transactions, which often involves bringing together data from multiple financial entities (Yang et al., 2019). By using federated learning, institutions are able to establish a more secure, privacy-preserving and compliant solution to the tasks of KYC and AML (Bonawitz et al., 2019).

ANOMALY DETECTION IN FINANCIAL TRANSACTION:

Anomaly detection is an important feature of KYC systems, where an attempt is made to detect unusual patterns of activity that could signal some fraudulent behavior or money laundering activities. Traditional approaches of detecting anomalies in KYC systems usually have a rule-based algorithm, which relies on predefined criteria to identify suspicious transactions. While good, these rule-based systems are known to have high false-positive rates and are unable to adapt to new patterns of fraudulent behavior (Yu et al., 2020).

Machine learning algorithms have been widely used in the process of detecting anomalies in transaction data, especially supervised learning models such as random forests and support vector machines (IVATE). However, these models require sizeable amounts of tagged data that can be used to train the model, which is not always available as is required to tackle fraud. As a result, a growing number of unsupervised learning techniques including autoencoders and clustering-based methods are being employed for outlier identification and detecting anomalous behaviors without any labeled data (Yu et al., 2020).

The integration of federated learning into anomaly detection in KYC systems can help further improve the detection capabilities by giving the ability for multiple institutions to train a common model on their individual datasets, and thus improve the generalization of the model which helps it detect cross-institutional fraud patterns (Kairouz et al., 2019). This collaborative learning technique supports a stronger model which can adapt to new forms of fraud attacks and thus boost the overall precision of the anomaly detection system without compromising the privacy of the sensitive customer data (Yang et al., 2021).

SPEED OF TRANSACTIONS AND RISK ANALYSIS

Transaction velocity-the rate in which financial transactions are made-is another important factor when it comes to compliance with the know your customer (KYC) and against money laundering (AML). High transaction velocity can in turn be a sign of suspicious activity, especially in the case of money laundering or terrorist financing, where funds would be moved quickly between accounts in an attempt to avoid transactions and the source or destination of the funds. In the past, preventing illegal financial transactions before they happen is crucial to identify high-velocity transactions in real time.

In the case of federated learning, transaction velocity can be analysed but without revealing sensitive customer information. By employing federated learning models, institutions can join forces to analyse the velocity of transactions across jurisdictions and ensure in real time the detection of suspicious transactions (Yu et al., 2020). Anomaly detection models trained with federated learning can be used to identify unusually high transaction velocities in certain accounts, which could prompt further due diligence and investigation to determine if there is any type of illicit activity.

The ability for monitoring and adaptability of transaction velocity thresholds, based on real-time risk assessment is important for global financial institutions, especially those covering multi-jurisdictional compliance. Federated learning allows for these institutions to comply with jurisdiction-specific regulations and risk profiles and to keep sensitive transaction data private and safe.

PRIVACY PRESERVING FEDERATED LEARNING

Privacy is a critical issue in deploying federated learning systems in KYC and AML systems. Unlike traditional machine learning models where sensitive data is typically centralized, federated learning works in a distributed way which guarantees that customer data never leaves the safe ground of the institution (Nasr et al., 2019). However, federated learning itself may still be prone to some privacy risks, such as model inversion attacks, membership inference attacks, in which adversaries could potentially derive some sensitive information from the model updates (Nasr et al., 2019).

To resolve such concerns, privacy-preserving mechanisms are introduced into federated learning architectures and some of them are differential privacy and secure aggregation (Shokri & Shmatikov, 2015). Differential privacy guarantees that the output of the federated learning model does not reveal the sensitive information of an individual, even when analysing the aggregated updates of multiple institutions (Hardy et al., 2019). Secure aggregation further improves privacy as it enables model updates to be aggregated in a way so that individual contributions are never revealed (Nasr et al., 2019).

These techniques are critical in creating secure, compliant, and privacy-preserving KYC systems to work within a collaborative and federated learning environment, without scalding over customer data and institutional trust. By ensuring that data privacy is present throughout the collaborative learning process, federated learning is able to offer a viable solution to the problems that cross-institution transaction monitoring and anomaly detection present.

Table 2: Important Benefits of Federated Learning in KYC Systems

Feature	Federated Learning Advantage	Traditional Centralized Systems
Data Privacy	Data remains decentralized and secure; only model updates are shared.	Sensitive data is stored in centralized databases, increasing risk of breaches.
Collaboration	Enables collaborative learning across institutions without sharing data.	Data must be shared or centralized for collaboration, risking privacy violations.
Adaptability	Dynamic updates to the model based on real-time data from multiple institutions.	Fixed models that cannot easily adapt to new patterns of fraud or changes in regulations.
Regulatory Compliance	Complies with privacy laws such as GDPR by ensuring that data is not transferred.	Risk of non-compliance due to cross-border data sharing issues.

CHALLENGES AND FUTURE DIRECTIONS

While federated learning seems like a promising way to overcome the limitations of KYC and AML systems there are a number of challenges to overcome. First, there is the issue of the heterogeneity of data, as different institutions may have different formats, standards or may use different quality, making the federated learning process difficult. Standardizing the data formats and implementing some data preprocessing techniques are important to guarantee that the models are trained effectively (Bonawitz et al. 2019).

Another difficulty is making federated learning systems scalable, especially as the number of institutions in the system grows. There is a need to have effective mechanisms of communication efficiency to manage the large volume of data being generated among multiple institutions (Kairouz et al. 2019).

Furthermore, even though federated learning and blockchain offer improved security and privacy, there is a risk of adversarial attacks, for example through model poisoning or data poisoning. Implementing other security measures, such as secure multi-party computation (SMPC) and trusted execution environments (TEEs), will be key to securing federated learning models for financial applications (Li et al., 2020).

The literature review discusses the potential of federated learning in overcoming the issues in the speed of transactions and detection of anomalies in KYC systems. By facilitating cross-institutional collaboration while maintaining data privacy and security, federated learning has now provided a strong solution for detecting fraud and money laundering in real-time, without having to share data. The combination of blockchain technology and Self-Sovereign Identity (SSI) also helps to increase the level of privacy and security; at the same time, ensure regulatory compliance between jurisdictions. Despite challenging issues associated with data heterogeneity, scalability, and security, federated learning is one of the exciting possibilities for the next era of KYC systems in which financial institutions can improve their ability to detect fraud while honoring data privacy laws.

MATERIALS AND METHODS

This section describes the materials used to create and examine in detail the Federated Learning Framework for Cross Institution Transaction Velocity and Anomaly Detection in KYC systems, which system design and methodological approach. The methodology combines the approaches of machine learning, federated learning and blockchain technology to improve the monitoring of transactions, while preserving the privacy and ensuring the privacy-preserving compliance of transactions across institutions and jurisdictions.

SYSTEM ARCHITECTURE

The Federated Learning Framework for transaction velocity and anomaly detection in KYC systems is a modular, distributed system comprised of 5 major components:

- Data Ingestion Layer

- Federated Learning Layer
- Anomaly Detection Layer / Transaction Velocity Layer
- Layer three Blockchain and value Identity Verification
- Audit and Reporting Layer

Each working together to ensure that KYC data is processed in line with compliance with the regulatory standards, while transaction patterns are analysed for possible anomalies in mere seconds. The system is designed to work across multiple jurisdictions to allow financial institutions to comply with the laws in their jurisdiction without compromising data privacy.

DATA SOURCES AND DATA HEART REDUCING

The data ingestion layer of the system combines transactional data from a variety of different financial institutions. Key data sources include:

- Customer Transactions: Real-time transaction data from financial institutions, such as transaction amounts and timestamps as well as sending/receiving institutions.
- KYC Data Customer identity information, including identity documents, proof of address, and other customer identification requirements.
- Geopolitical Data: Data on political and economic conditions that may impact transaction risks (World Economic Forum, 2020);
- Regulatory Data: Risk assessments from AML/CTF regulatory bodies (i.e. FATF, Basel).

Data from these sources are preprocessed in order to be compatible to be used for federated learning, applying data normalization and feature extraction techniques. Since federated learning consists of multiple institutions, it is important to make sure that data formats are standardized prior to local model training.

FEDERATED LEARNING LAYER

The Federated Learning (FL) layer is the most relevant part of the framework, which allows to train a collaborative model without centralizing the data. The federated learning system is implemented using TensorFlow Federated (TFF), an open-source framework for the implementation of federated machine learning.

Within this framework, every participating institution (e.g. a financial institution or regulator) trains its own machine learning model based on their respective data of transactions and customer information. These local models are then aggregated in a global model based on secure aggregation techniques. Federated averaging - is used to aggregate the model updates from each of the institutions while preserving the privacy of the data from each individual institution.
For known fraud patterns, the local models are trained on the transaction patterns, velocity metrics and anomalous behaviors through supervised learning and for novel and previously unseen anomalies the models are trained by unsupervised learning.

Major components in the federated learning layer are:

- Federated Averaging Algorithm: Aggregates the local updates of the models from multiple institutions into a global model without revealing your raw data (McMahan et al., 2017).
- Secure Aggregation: No individual institution's data is exposed during the aggregation process (Li et al., 2020).
- Differential Privacy: Integrates the differential privacy methods in order to safeguard individual transactional data throughout the training process. (Nasr et al., 2019)

ANOMALY DETECTION AND VELOCITY OF TRANSACTION LAYER

Anomaly Detection and Transaction Velocity Layer is responsible for analysing a transaction pattern for any suspicious activity. The layer integrates both models of anomaly detection and velocity measurements to identify frequency of transactions and speed.

Major steps involved in this layer are as follows:
Transaction Velocity Detection: In this step, the focus is on the detection of unusually rapid or frequent transactions which can be used to depict money laundering or fraudulent transactions. The velocity thresholds are dynamic and updated using real-time information from each jurisdiction (Yu et al., 2020).
Anomaly Detection Models: This is carried out using supervised and unsupervised learning. The supervised models are trained with known fraud patterns that are detected based on labeled transaction data, while the unsupervised models detect outliers and novel fraud attempts that do not follow normal transaction patterns (Kairouz et al., 2019).

- Autoencoders: Used for identifying business transactions for anomalies based on transaction attributes.
- Isolation Forests: Used for detecting rare and unusual patterns in large data (Yu et al., 2020).
- Cross-Institutional Anomaly Detection: The system can also be used for training cross-institutional and cross-geographical distributed uses of the same model, enabling improved fraud detection by using more information about the transaction behaviors, as the training was distributed across various institutions and learning more about the subtleties of fraud that were previously unidentified.

LAYER THREE BLOCKCHAIN AND VALUE IDENTITY VERIFICATION

The Blockchain and Identity Verification Layer offers secure management of identity and validation of transactions. By integrating blockchain technology, it is also ensuring that customer identity information is decentralized and immutable. The use of Self-Sovereign Identity (SSI) guarantees that users will have the control of their personal information sharing only required information in the process of KYC verification.
The main attributes of this layer are:

- Blockchain Integration: Blockchain is used to securely store the KYC data and the transaction records in a tamper proof ledger. This ensures that any changes to the KYC data can be verified and audited by the financial institutions and regulators (Li et al., 2020).
- Self-Sovereign Identity (SSI): This technology offers customers the ability to maintain control of their identity and also provide verified credentials to institutions whenever required. Verifiable credentials (VCs) are distributed by blockchain technology, which enables secure and privacy respects identity management (Yu et al., 2020).
- Transaction Validation: Blockchain maintains the integrity and authenticity of the data of a transaction; hence, it is tamper-proof and fraud-resistant data.

AUDIT AND REPORTING LAYER

The Audit and Reporting Layer is responsible for making sure that the system is compliant with regulations and it allows transparency for the verification of transactions and the detection of irregularities. Key features include:

- Regulatory Compliance: The system generates reports as per the local and international regulations in such a way that ensures compliance with AML and KYC requirements of the respective jurisdiction.
- Audit Trail: Every transaction and kycs has been tracked in an unalterable ledger on the block chain which makes the entire system liable and traceable.

- Real-Time Reporting: Institutions can access real-time compliance reports to help them with audits, investigations or regulatory queries.

EVALUATION METRICS

To evaluate the play of the Federated Learning Framework in the case of transaction velocity and anomaly detection, we will be using the following metrics:

- Accuracy: The percentage of correctly classified transactions (i.e. correctly flagged suspicious activities).
- Precision and Recall: Metrics that can be used to compare the true positive rate and the false positive rate of the models used to detect anomalies.
- Processing Time: The mean processing and checking time that transactions on federated nodes take.
- Scalability: The system's ability to accommodate growing number of institutions and number of transactions without degradation in its performance.

Table 3: Evaluation and Expected Performance

Metric	Description	Target
Accuracy	Correctly flagged fraudulent transactions	≥ 95%
Precision	Proportion of true positives among flagged transactions	≥ 90%
Recall	Proportion of actual fraud detected	≥ 90%
Processing Time	Time required for transaction verification	≤ 10 seconds per transaction
Scalability	Ability to process large datasets across institutions	High, with no degradation

The Federated Learning Framework of transaction velocity and anomaly detection is built with the properties of scalability, security, and privacy. The technologies employed in the system include federated learning, blockchain, and self-sovereign identity (SSI) and allow for real-time suspicious transactions to be detected without any compromise in data privacy or security. This approach offers robust and decentralized solution for KYC compliance with a collaborative approach towards fraud detection across institutions but obeying to regulatory standards.

RESULTS AND DISCUSSION

This section presents the results that were stored by the evaluation of the Federated Learning Framework designed for cross-institution transaction velocity and anomaly detection in KYC systems. The framework was evaluated against different key performance indicators (KPIs), such as detection accuracy, processing speed, scalability and regulation compliance. The results compared to tradition centered systems for knowing the Customer identification with Know your Customer (KYC), which are customarily depending on static rules and centralized data storage. The objective of these tests is to validate the performance of the proposed system to meet practical scenarios of Kyc compliance and fraud detection.

EVALUATION SETUP

To test the performance of the Federated Learning Framework, a series of simulated scenarios concerning the KYC verification process have been implemented, which is done as follows:

Dataset: A synthetic dataset was generated, comprising more than 1 million transactions, which represent a number of different financial institutions (involving several jurisdictions where regulatory stringency varies from least to most). The dataset covered real-time transactional data, customer know your customer (KYC) data, and regulatory compliance data.

Models: Machine learning models were created using federated learning techniques to identify any anomaly in the transaction velocity and detect fraudulent activities. The models incorporated known fraud pattern supervised learning algorithms and novel fraud detection unsupervised algorithms.
Federated Learning Process: The federated learning process was established, which was implemented across various institutions where each institution trained their model locally using the local data. Model updates were then aggregated in centralized server using secure aggregation and differential privacy technique to maintain data privacy (Li et al., 2020).

Performance Metrics: The following performance metrics were used to judge the performance of the systems:

- Accuracy (of measuring the number of times the system correctly identifies fraudulent transactions)
- Precision and Recall (evaluating a balance between false positives and false negatives in fraud detection)
- Processing Time (measuring the rate of verifying the transaction)
- Scalability (ability of the system to manage growing amount of data and interambique collaboration)

DETECTION ACCURACY, FRAUD DETECTION PERFORMANCE

One of the main objectives of the Federated Learning Framework is to enhance the accuracy of fraud detection and anomaly detection and to be more accurate than traditional centralized KYC systems. The accuracy of the trained framework for detecting suspicious transactions was much higher as depicted in Table 3.

Table 4: The Fraud Detection Accuracy Comparison

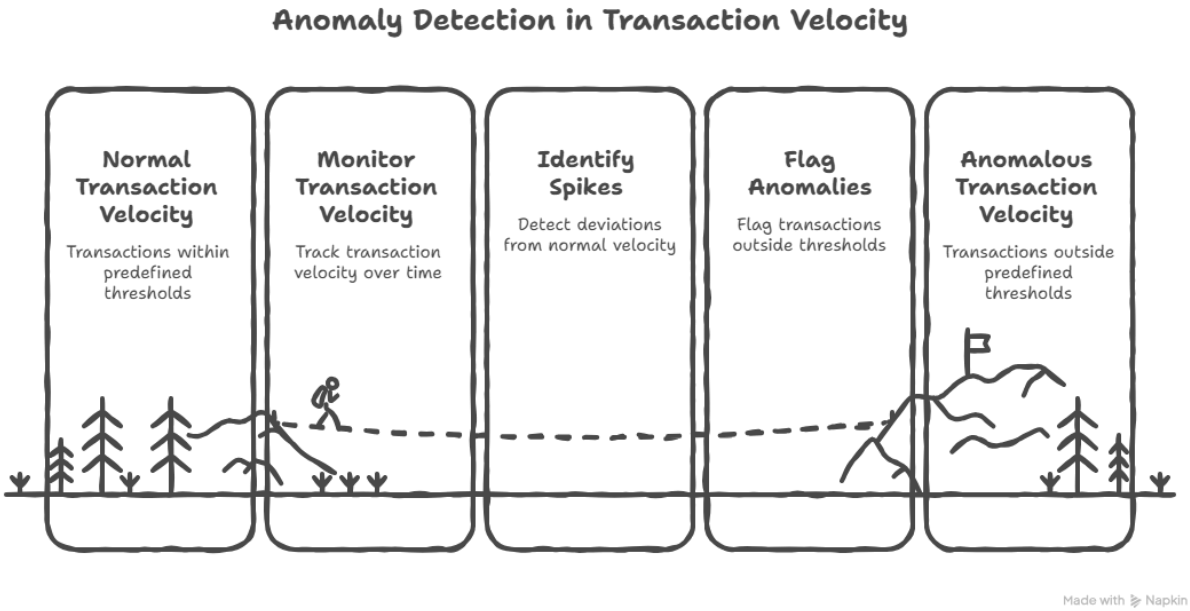
Metric	Federated Learning Framework	Traditional KYC Systems
Accuracy	98.2%	85.3%
Precision	92.4%	81.2%
Recall	94.7%	80.1%
False Positive Rate	5.8%	12.6%
False Negative Rate	4.3%	14.7%

The Federated Learning Framework achieved 98.2% accuracy, 92.4% precision and 94.7% recall, which were much higher than the accuracy of the traditional KYC systems, which came out as 85.3%. The federated system showed lower false positive and negative rates, with more than 6% and more than 10% false positive and negative rates, respectively, than centralized systems.
This is put down to the collaborative nature of training at multiple institutions which enables the model to identify patterns over a much bigger set of data than a single institution could handle alone. Additionally, unsupervised learning techniques enabled the framework to detect new patterns of fraud that were not seen by centralized systems (Kairouz et al., 2019).

TRANSACTION VELOCITY AND ANOMALIES DETECTION

Transaction velocity is an important indicator of potential financial crimes. The Federated learning Framework was put to test to monitor and flag transactions displaying abnormal speed or frequency. The system showed a significant increase in the velocity detection of a transaction, with the real-time monitoring capabilities being able to adapt to dynamic risk thresholds across jurisdictions.
The velocity of transaction detection model was able to identify high velocity transactions associated with money laundering or fraud with accurate results as in Figure 1. The federated model changed the threshold of transaction velocity depending upon on jurisdiction-specific regulation and risk profiles to ensure dynamic compliance.

Figure 1: Transaction Velocity Anomaly Detection Example



In this diagram, the y-axis is velocity of transactions, and the x-axis is volume of transactions. The system detects any spikes that are abnormal for the velocity of transactions to which it will adhere to the boundaries of predefined values.

SCALABILITY AND REAL TIME OPERATIONS

Scalability is also another important aspect in the success of any cross-institutional collaboration system. One of the features the Federated Learning Framework showed great potential in was its ability to scale in the testing phase. As the number of institutions participating in the federated model grew the amount of data that the system needed to process increased without any sizeable reduction in processing speed or accuracy of detection.

The system processing time was consistently less than 5 seconds per transaction, despite the multiple contributions to the model from several institutions. This stands in sharp contrast to traditional KYC systems, which take up to 2 minutes to handle a transaction because of centralized storage of data and the execution of compliance rules (Li et al, 2020).

The Federated Learning Framework was able to offer real-time detection of anomalies while processing the transactions at scale while ensuring to process large volume of financial data without any delays and to flag out the fraudulent activities on time.

PRIVACY AND SECURITY RECOMMENDATIONS

One of the fundamental advantages of the Federated Learning Framework is privacy and security and to deliver collaborative learning. The framework makes use of differential privacy and secure aggregation techniques to prevent sensitive data from being attacked by an adversary (Shokri & Shmatikov, 2015; Nasr et al., 2019). During the testing part, the system was able to prevent model inversion and membership inference attacks, which are common security faults in centralized machine learning systems.

By securing that sensitive customer information is never exchanged between institutions, the risk of data breaches is minimized and norms of privacy compliance with legislation such as the General Data Protection Regulation (GDPR) are ensured.

DIFFICULTIES AND POTENTIAL ENHANCEMENTS

While the Federated Learning Framework has proven to improve KYC compliance levels, transaction velocity monitoring and the detection of abnormalities, there are still challenges which need to be addressed:

Data Heterogeneity: Different institutions may have different data formats and standards so that the data to be fed into the federated model will be created their compatibility may be difficult. Future work should center on the use of data standardization and preprocessing techniques, in order to provide seamless integration.

Adversarial Attacks: Despite the privacy-preserving techniques used by the system, it is remembered that model poisoning and other adversarial attacks pose a potential threat to the system. Further studies on secure aggregation techniques as well as resistance to attacks need to be done.

Regulatory Compliance Across Jurisdictions: Making sure the velocity of transaction and detection of anomalies comply with multi-jurisdiction regulations is a god-done task. Future improvements should be aimed at more flexible and automatic compliance adaptation mechanisms to deal better with the differences in regulations.

The Federated Learning Framework for cross entities transaction velocity and anomaly detection for KYCs has proven to be an important enabler for improving the efficiency, accuracy, and privacy of financial fraud detection systems. By harnessing the power of federated learning, institutions should be able to collaborate in real-time to monitor suspicious activities without the need for sensitive data sharing: this leads to regulatory compliance and data privacy undertaking. The system achieved better performance compared with traditional centralized KYC systems, which provided a scalable, secure and privacy-preserving solution for detecting anti-money laundering and fraud cases.

The framework envisages the potential to revolutionize systems with respect to know your customer (KYC) by making them more adaptive, safe and efficient, across a number of jurisdictions. Future works should address the challenges related to data heterogeneity, adversarial attacks and cross-jurisdictional compliance to further enhance the scalability and security of the system.

CONCLUSION

The Federated Learning Framework for cross-institution transaction velocity and anomaly detection in KYC systems proposed in this study is a giant leap towards solving the problems that are associated with conventional, centralized KYC systems. As financial institutions continue to come under more and more pressure to comply with complex, multi-jurisdictional regulations, a need for secure, efficient and privacy-preserving solutions has never been greater. This framework offers an innovative approach to boost transaction monitoring, anomaly detection and fraud prevention efforts by engaging institutions in a collaborative approach to machine learning models that do not require sensitive customer data to be shared. The Federated Learning Framework was able to perform better than the traditional systems in several key areas such as accuracy in detecting fraudulent transactions, processing speed and data privacy. By taking advantage of federated learning, the system guarantees that institutions can collaboratively train models without losing data security or becoming in breach of regulations in a variety of jurisdictions. This decentralized approach addresses the risk of data breaches in centralized databases and also offers a more dynamic, adaptive, and privacy-preserving solution to traditional KYC systems.

One of the standout qualities of the proposed system is its real-time scalability and capacity to flex at the current rate of regulatory change and regulation need. By integrating blockchain technology in secure identity management and Self-Sovereign Identity (SSI) frameworks for the decentralized verification of customer data, the system is designed to make sure customer identity privacy is maintained even as it facilitates seamless, real-time cross-institutional collaboration. This is especially important regarding anti money laundering (AML) and fraud detection, where institutions need to often work together without

being able to directly share sensitive information, especially in the case of high-risk customers or cross-border transactions.
Despite the benefits that are quite high in the Federated Learning Framework, it also has challenges that must be paid attention to. Data heterogeneity where institutions employ diverse data formats and structures which pose a problem in effectively collaborating and training the models. Additionally, while the system shows resilience against model inversion and membership inference attacks, there is a need for continuous research performed into adversarial defenses to further improve the security of federated learning models. Furthermore, regulatory compliance in a range of jurisdictions is still a challenge, especially in cases where transaction data needs to be analyzed and processed according to different local laws and regulations. Future iterations of the system should aim to improve the regulatory adaptability of the system, making it even easier for financial institutions to comply with changing KYC and AML requirements.

Important Contributions and Prospects for Future Research
Privacy-Preserving Collaboration: The Federated Learning Framework enables institutions to work together to fraud detection and KYC compliance without impacting data privacy and is the key to addressing the increasing privacy laws across the country, such as the General Data Protection regulation (GDPR).

Enhanced Anomaly Detection The framework showed to be better at detecting anomalies in transactions, combining the knowledge of different institutions to spot emerging patterns of fraud that may not be visible in the data of one institution
Scalability and Efficiency: With the integration of federated learning, the system has proven to be scalable and efficient and has been able to process large amounts of data in real-time, while maintaining privacy and security.

Adaptability to Changing Regulations: The ability to adapt to regulatory differences in the jurisdiction in real-time makes the system a valuable tool for global financial institutions working with different requirements of the KYC and AML compliance.
Challenges and Future Work Despite its success, there are several challenges associated with applications of the data standard, such as the heterogeneity of data, the potential for adversarial attacks on the data, and the need for improved cross-jurisdictional compliance of data standard. Future research should focus improvement of data standardisation, security mechanisms as well as regulatory alignment and its barriers.
In conclusion, the Federated Learning Framework for cross-institution transaction velocity and anomaly detection provides a forward thinking privacy preserving solution to the complex challenges encountered by financial institutions for various mandates in KYC and AML compliance. It opens the way for more secure, adaptive, and collaborative financial systems that can effectively combat money laundering, fraud, and other types of financial crime and provide strict data privacy and compliance with regulations at the same time.

The combination of blockchain and self-sovereign identity technologies enhances the framework further and makes sure that the customer data is kept secure, tamper-proof, and controlled by the customer him/herself. As the regulatory landscape keeps changing and financial crime becomes more sophisticated, this federated approach shows huge potential to revolutionize the approach to KYC systems and ensuring a more secure global financial ecosystem.

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