

THE NATURE OF AML/CFT RISK ASSESSMENTS

(Business & Customer)



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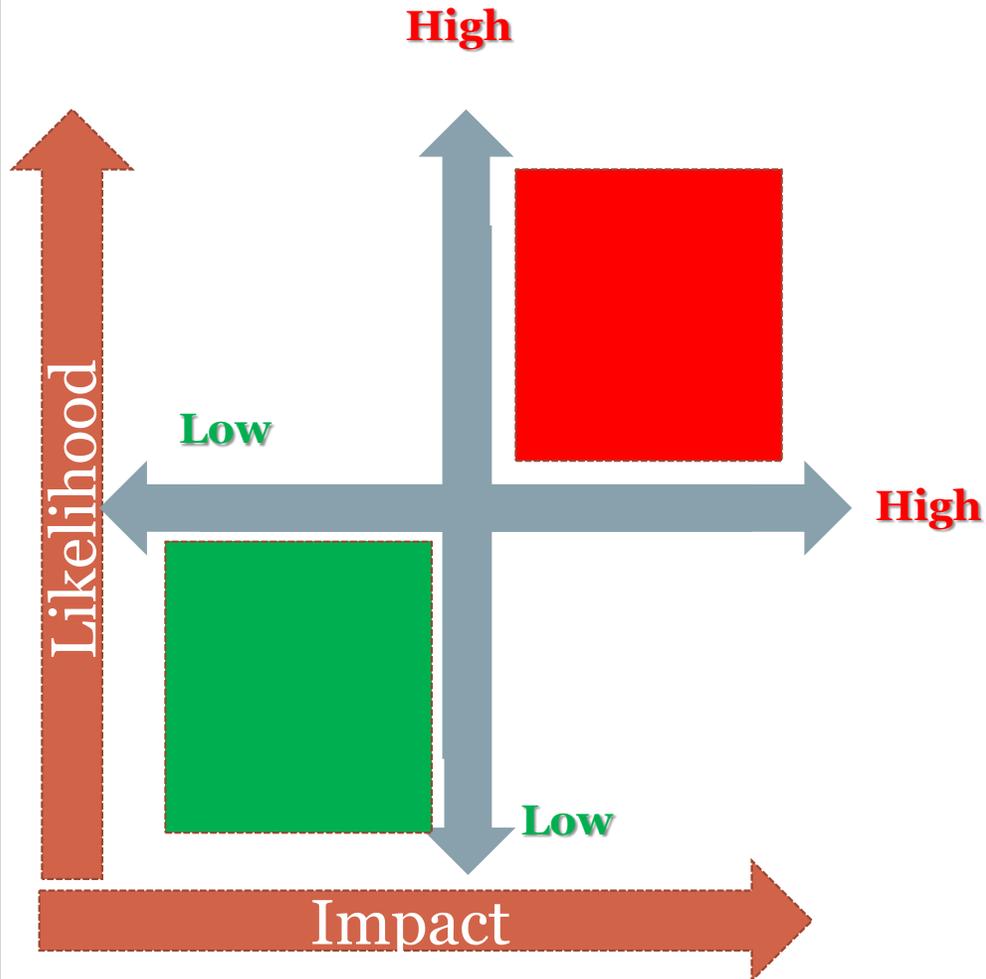
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Private Sector Risk Assessments



- 1. Developing a AML/CFT risk methodology**
- 2. Applying Risk Findings**
- 3. Customer Due Diligence (Perspective Of The Financial Institutions)**

Private Sector Risk Assessments



Basis for and Advantages of RBA

Types of risk assessments

Business line risk assessment

Components of a risk methodology

How to conduct a risk assessment

What types of customers pose a risk?

Types of behaviours suggesting risk

Possible risk factors

Risk scoring process

Basis for Risk Assessment/Advantages for RBA



Rules-based Approached

- **One size fits all**
- **Potentially expensive**
- **Regulatory compliance *Rec. 5**

Risk-based approach

- **AML measures commensurate with identified risk**
- **Reduce cost of AML**
- **Reflects national risks**
- **More focused**
- **Regulatory compliance *Rec. 10**



What is risk?

Threats

Vulnerabilities

Consequences



Private Sector Risk Assessments

VULNERABILITIES

Lack of awareness

Failure to identify money laundering transactions

Focus on fraud

Savings and investments features

Cash deposits/transactions

Use of intermediaries

The Risk Assessment



The risk of exposure of a financial institution affect and expose the entire business. Therefore a global risk assessment is conducted in order to understand the businesses' entire risk exposure.

Risk will vary from time to time **(Inherent vs residual)**

The Risk Assessment



Enterprise-wide

- All business lines
- All subsidiaries
- All affiliates
- All holdings

Business line

- Specific business lines
- Products/services
- Customer base
- Geography
- Controls

Customer

- Customer base

What?

IS A RISK ASSESSMENT

The Risk Assessment



Measures:

3

- The inherent risk in a business and/or of process
- The strength of current controls
- The residual risk of a business and/or processes



The Risk Assessment



Types

2

- **Business Line Risk Assessment**
- **Customer Risk Assessment**

Business Line Risk Assessment



Identifies Vulnerabilities

By evaluating

- **Inherent risks of products/services**
- **Customer base**
- **Geography**

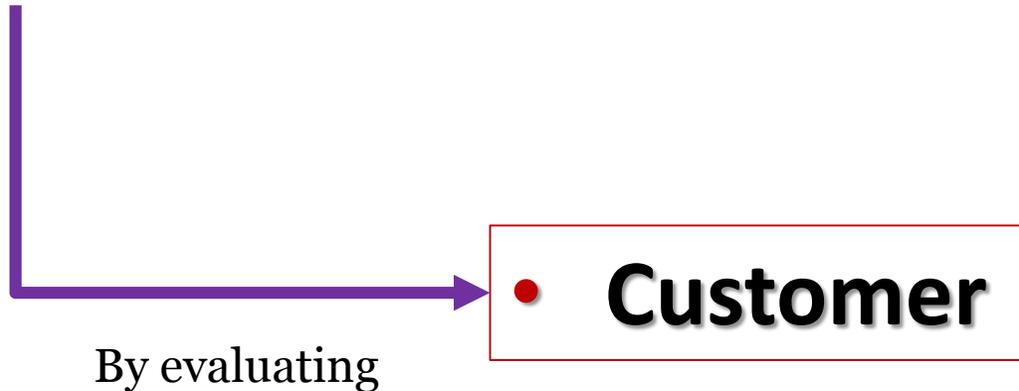
**&
Controls**

...at macro level

Customer Risk Assessment



Identifies Vulnerabilities



Typically at the inception of each client relationship based on information provided during account opening process

The Risk Assessment



How to conduct a risk assessment

Consider

- Types of customer
- Where you and your customers are based
- Customers' behaviour
- How customers come to you
- The products or the services offered
- Delivery channels and payment processes, (cash over the counter, cheques, electronic transfers or wire transfers)
- Where customers' funds come from or go to

The Risk Assessment



Types of behaviours suggesting risk

- **Not wanting provide documentation, or providing documentation that isn't satisfactory**
- **Not wanting to reveal the name of a person they represent**
- **Agreeing to bear very high or uncommercial penalties or charges**
- **Entering into transactions that don't make commercial sense**
- **Transactions where you can't easily check where funds have come from**

The Risk Assessment



What types of customers pose a risk?

- **New customers carrying out large, one-off transactions**
- **Introduced customers** – (because the introducer may not have carried out due diligence thoroughly)
- **Customers who aren't local to you**
- **Customers involved in a business that handles large amounts of cash**
- **Businesses with a complicated ownership structure that could conceal underlying beneficiaries**
- **Customer - or group of customers - who makes regular transactions with the same individual or group of individuals**

The Risk Assessment



- Existing customers
- Existing products

- Penetrates the past, present and future of activities
- Must be continuous
- As risk changes internal controls must be adjusted to meet compliance objectives

**Informs changes to AML/CFT
Compliance Programme**

The Risk Assessment



Evaluation is dependent on two phases

i. IDENTIFICATION

Identifies specific variables of business within the following categories:

- **Clients**
- **Financial Products and Services**
- **Distribution Channels**
- **Jurisdictions or Geographic Areas**

The Risk Assessment



Evaluation is dependent on two phases

i. IDENTIFICATION

- 1. What factors affect a client's risk rating for ML/TF?**
- 2. What factors affect a financial product/service risk rating for ML/TF?**
- 3. What factors affect makes a distribution channel susceptible to ML?**
- 4. What factors affect a jurisdiction or geographic area's risk rating for ML/TF?**

The Risk Assessment



Evaluation is dependent on two phases

ii. **ANALYSIS**

Analyses specific variable within the risk factors including :

- Number/quantity and volume of transaction
- Nature of customer relationship
- Purpose of the account

The Risk Assessment



Analysis has two
specific objective

Determined by

BoD

Feeds into

**AML/CFT
Policy & Procedures**

1. Determine risk tolerance/appetite; and

2. Identify residual risk

The Risk Assessment



Analyses must also include:

Evaluation of the quality and effectiveness of AML/CFT Policies and Procedures

- Training
- Staffing
- Resources

The Risk Assessment



Risks are fluid and the assessment must be updated in order to identify changes in the financial institution's profile.

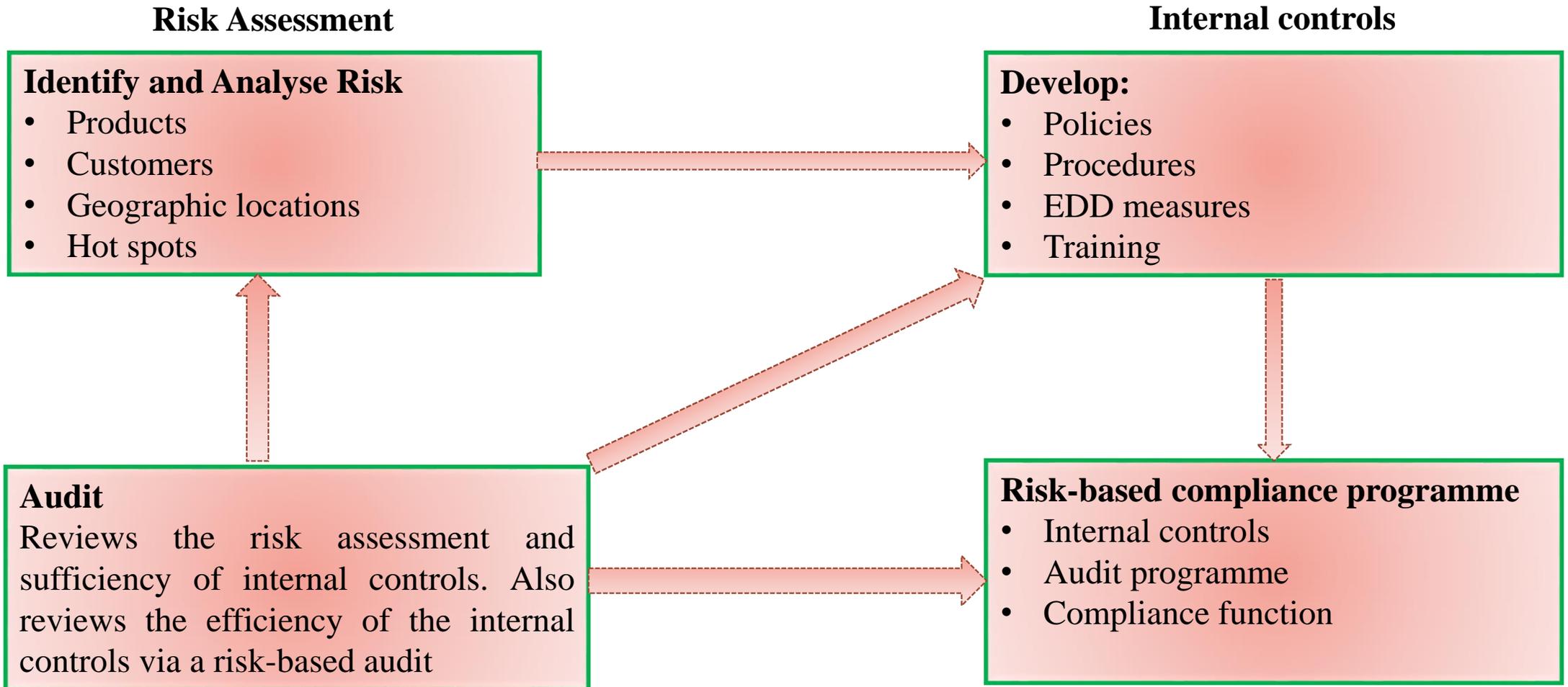
Triggers for a risk update include:

- Changes in line of business
- Introduction of new products/services
- Growth through mergers & acquisitions
- Entry into new markets
- Results of NRA

Then What?

1. Applying risk findings

Link to CDD



The Risk Assessment



Factors to consider



1. **Customer tenure**
2. **Product type**
3. **Geographic Locations – Country of Residence**
4. **Geographic Locations – Funds transfers**
5. **Geographic Locations – Crime or STR Hotspot**
6. **Economic Activity/High risk business**
7. **Transaction volume**
8. **Transaction volume (number of services requested)**
9. **Source of funds**
10. **Politically Exposed Person**
11. **Means of Payment**
12. **Private Investment Companies (PICs) /Asset Holding Vehicle**
13. **Suspicion of Money Laundering or Terrorist Financing**

The Risk Assessment

→ **Factors to consider**



1. **Customer tenure**
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10. **Politically Exposed Person**
11. **Means of Payment**
12. **Whether or not Payment will be made to a Third Party**
13. **Private Investment Companies (PICs) / Asset Holding Vehicle**
14. **Suspicion of Money Laundering or Terrorist Financing**

The Risk Assessment → Factors to consider



Risk Quantification Matrix

Source: *Basel Committee on Banking
Supervision – Working Group on Cross
Border Banking – Risk Matrix*

The Risk Assessment → Quantification



Customer Tenure

Risk Factor	Rating	Score
New Client	H	3
Less than 2 years	M	2
More than 2 years	L	1

The Risk Assessment → Quantification



Account Type		
Risk Factor	Rating	Score
DDA	H	3
Savings	L	1
Trust	H	3
Investment Account	H	3
Loan	L	1
Credit Card	M	2
Any combination with a DDA	H	3

The Risk Assessment → Quantification



Geographic Location (Country of Residence)

Risk Factor	Rating	Score
The residence is in a country considered high risk	H	3
The residence is in a country considered <u>NOT</u> high risk	L	0

The Risk Assessment → Quantification



Geographic Location (Funds transfer)

Risk Factor	Rating	Score
The country where customer sends/receives funds is considered high risk	H	3
The country where customer sends/receives funds is <u>NOT</u> considered high risk	L	0

The Risk Assessment → Quantification



Geographic Location (Residence of high crime area)

Risk Factor	Rating	Score
The area where the customer resides is considered high risk	H	3
The area where the customer resides is <u>NOT</u> considered high risk	L	0

The Risk Assessment → Quantification



Economic Activity

Risk Factor	Rating	Score
Economic activity or business of the customer is considered high risk	H	3
Economic activity or business of the customer is <u>NOT</u> considered high risk	L	0

The Risk Assessment → Quantification



Transaction Volume (Size of transaction)

Risk Factor	Rating	Score
Customer's transaction profile for dollar amount is greater than < Legislative SOFD trigger >	H	3
Customer's transaction profile for dollar amount is greater than < FI's SOFD trigger >but less than < Legislative SOFD trigger >	M	2
Customer's transaction profile for dollar amount is less than < FI's SOFD trigger >	L	0

The Risk Assessment → Quantification



Transaction Volume (number of services requested)

Risk Factor	Rating	Score
Customer exceeds 5 transactions per month in cash/manager's cheques/wire transfers	H	3
Customer does <u>NOT</u> exceed 5 transactions per month in cash/manager's cheques/international funds transfers	L	0

The Risk Assessment → Quantification



* Source of Funds

Risk Factor	Rating	Score
Customer funds transfer activity does not include high risk international jurisdictions, HIDTAs, HIFCAs or other areas classified by the bank as high risk	L	0
Customer funds transfer activity includes high risk international jurisdictions, HIDTAs, HIFCAs or other areas classified by the bank as high risk	H	3
Customer activity does <u>Not</u> include funds transfer	L	0

*Activity which generate the funds

The Risk Assessment → Quantification



Foreign Politically Exposed Person

Risk Factor	Rating	Score
Customer is a Foreign PEP	H	3

The Risk Assessment → Quantification



Domestic Politically Exposed Person

Risk Factor	Rating	Score
Customer is <u>NOT</u> considered a PEP	L	0
Customer is considered a PEP but has not been actively engaged or in office in over 10 years	M	2
Customer is considered a PEP and is actively engaged in office within less than 10 years	H	3

The Risk Assessment → Quantification



Means of Payment

Risk Factor	Rating	Score
Wire transfer	H	3
Cash	H	3
Bank draft/Credit Card/Personal Cheque	L	0

The Risk Assessment → Quantification



Suspicion of Money Laundering

Risk Factor	Rating	Score
Money laundering or terrorist financing suspected	H	3
Money laundering or terrorist financing not suspected	L	0



Risk Scoring Process

Exposure	Range	Identifier
Low (L)	1 to 15	
Medium (M)	16 to 31	
High (H)	Above 31	

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