



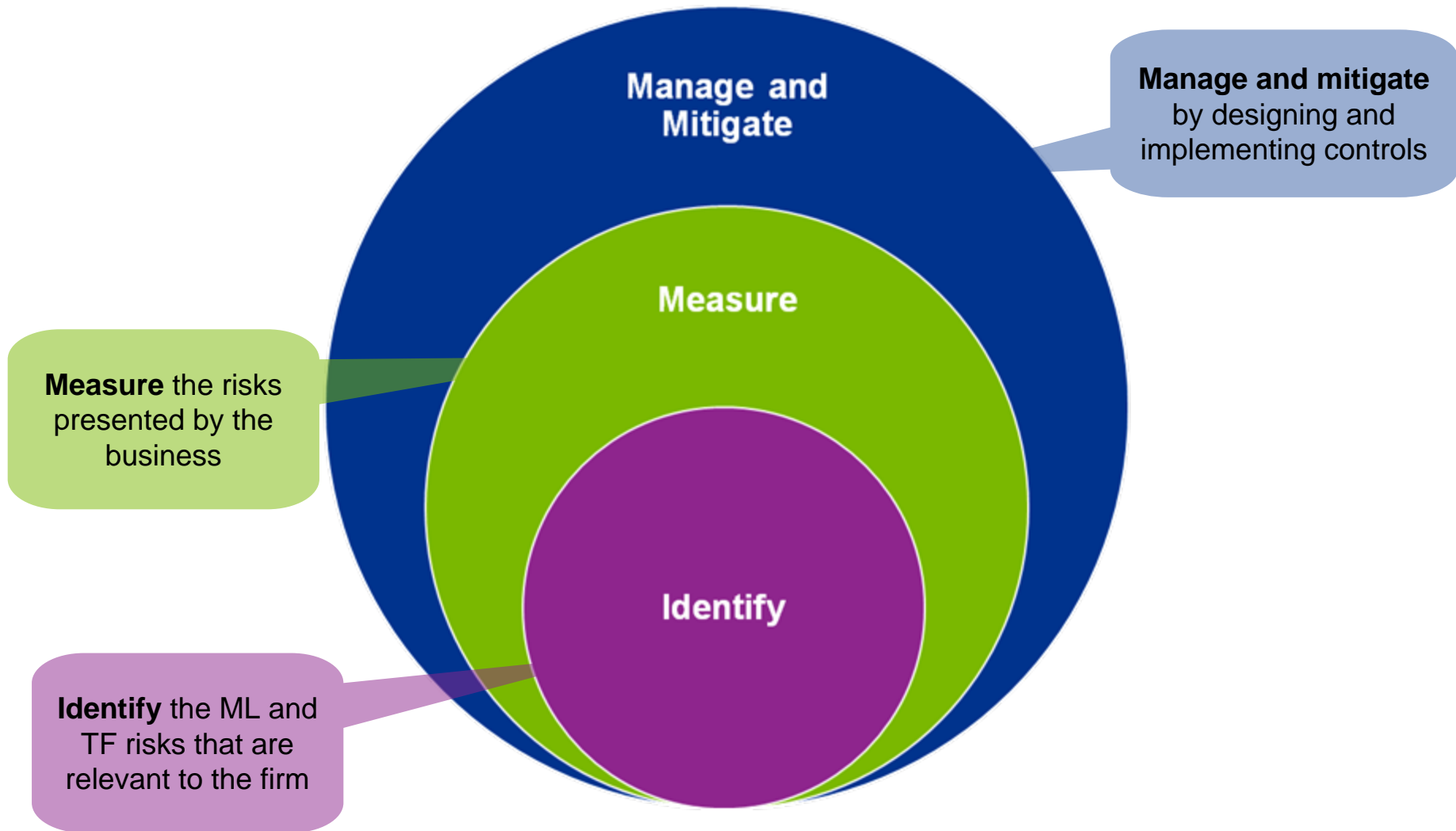
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**Putting the FIAU's
Implementing
Procedures into
practice
*The Risk-Based
Approach***

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Basic view of risk



Mandatory or optional?



Mandatory risk procedures

Subject persons are required to have in place procedures to manage the ML/FT risks posed by their customers, products and services ... Subject persons are to establish procedures on, inter alia, risk assessment and risk management that are adequate and appropriate to prevent the carrying out of operations that may be related to ML/FT

FIAU Implementing Procedures 4.1

What this means is that we all have to carry out a business risk assessment!

Why a business risk assessment?

- **An assessment of how vulnerable the business is to the risk of money laundering and terrorist financing**
- **Identify 'risk hot spots' through the consideration of certain risk areas**
- **Where a customer touches a risk hot spot, enhanced due diligence may be required**

Mandatory risk procedures

Subject persons are required to develop and establish effective customer acceptance policies to determine whether an applicant for business or a beneficial owner is a PEP or is likely to pose a higher risk of ML/FT

FIAU Implementing Procedures 4.1.1.1

A customer acceptance policy should, as a minimum, include:

- a) A description of the type of customer likely to pose higher than average risk;**
- b) The identification of risk indicators, such as the customer background, country of origin, business activities, products, linked accounts or activities and public or other high profile positions; and**
- c) The requirement for the application of EDD measures for higher risk customers and PEPs**

Mandatory risk procedures

Risk assessment procedures should at least include identification and assessment of customer risk, product/service risk, interface risk and geographical risk, in relation to every business relationship or occasional transaction

FIAU Implementing Procedures 4.1.1

Customer risk	<ul style="list-style-type: none">• Natural persons: risk assessment generally based on the person's economic activity and/or source of wealth• Legal entities: corporate structures, trusts, foundations, associations and commercial partnerships may be used to obscure links• Awareness of customer behaviour is required – commercial rationale; complex/unusual transactions; levels of secrecy; audit trails; layering; willingness to disclose details of real owners and controllers• Automatically classify as high risk customers subject to sanctions or other economic measures
Product / Service risk	<ul style="list-style-type: none">• Riskier products/services are inherently more risky and thus more attractive to criminals• FATF RBA guidance on determining the risks of products/services
Interface risk	<ul style="list-style-type: none">• Use of internet for provision of services may exacerbate ML/FT risks due to rapidity and anonymity
Geographical risk	<ul style="list-style-type: none">• Notion of 'reputable jurisdiction'• FATF RBA guidance on determining when a country poses a higher risk

What is the output of a business risk assessment?

Documenting the BRA

What risks has [company name] considered?

Where is [company name] vulnerable to the risk of money laundering and terrorist financing?

How does [company name] determine whether new customers bring a higher level of risk?

How does [company name] determine whether existing customers bring a higher level of risk?

How have we communicated the risk-assessment to our staff?

When will we review the business risk assessment?

How will we demonstrate Board approval and senior management buy-in?

The background features a series of overlapping, semi-transparent geometric shapes in various shades of blue, from light to dark, set against a white background. The shapes are primarily parallelograms and trapezoids, creating a dynamic, layered effect.

The Risk Based Approach

Mandatory or optional?



The Risk-Based Approach

While the risk-assessment and risk-management procedures are mandatory, the application of a RBA is optional ... Subject persons may determine the extent of the application of CDD requirements on a risk-sensitive basis, depending on the type of customer, business relationship, product or transaction

FIAU Implementing Procedures 4.2

- **Subject persons may apply an RBA provided they are able to demonstrate that the extent of the application on a risk-sensitive basis is appropriate in view of the risks of ML/FT**
- **Involves moving away from a rules-based ‘tick-box’ approach – shifting the focus on adopting measures commensurate with identified risks and allocating resources efficiently**
- **An ongoing procedure with strategies developed to manage and mitigate identified risks**
- **Should assist in managing ML/FT risks effectively; not prohibit the undertaking of certain transactions or the establishment of certain business relationships**
- **Should not be applied rigidly without allowing past experience and available information to be taken into consideration in reaching a determination**

The Risk-Based Approach

The RBA does not necessarily require a complex set of procedures as long as the procedures are based on a set of objective criteria

FIAU Implementing Procedures 4.2.1

- **A model to implement the RBA framework is required which may be simple or sophisticated**
- **This should depend on the size and nature of the business and services offered, the customer base and the geographical area of operation**
- **Subject persons to show that reasonable business judgement has been exercised with respect to customers and the determinations reached in the application of the RBA are justified in the light of the ML/FT risks identified**

A practical approach to Chapter 4

Structured risk assessment process leads to well-informed and consistent decisions about whether a potential or existing customer relationship was within risk appetite

Effective transaction monitoring depends on having completed good initial CDD work

A risk-scoring system is commonly used:

HIGH



MEDIUM



LOW



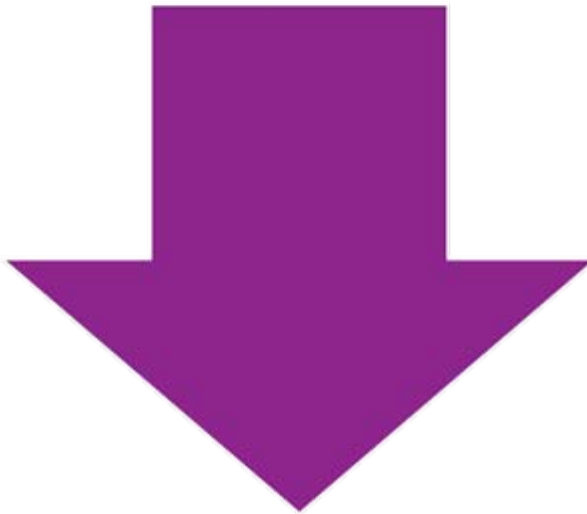
Risk assessment to be reviewed regularly and to take account of significant developments, for the purposes of ongoing monitoring

Formal procedure for escalating prospective customers to committees and senior management on a risk based approach

Pros and cons of a fully fledged RBA



- Better management of risks and cost-benefits;
- Focus on real and identified threats;
- Flexibility to adapt to risks that change over time.



- Identifying appropriate information to conduct a sound risk analysis;
- Addressing short term transitional costs;
- Greater need for more expert staff capable of making sound judgments;
- Greater need for appropriate training;
- Regulatory response to potential diversity of practice.

An integrated Risk-Based Approach





**The RBA in
action**

Risk assessment in action – the Deloitte/EC Report on the application of the Third Directive

“... the introduction of the risk-based approach has not caused a diminishment of the national CDD requirements. The approach has only rationalized the requirements allowing more efficient and effective use of resources proportionate to the risks faced while maintaining minimum requirements that have to be complied with in all situations”

EC, Final Study on the Application of the Anti-Money Laundering Directive, 2011

- **The adoption of the RBA is perceived as a step forward in the AML framework**
- **3 main issues are being seen to hinder the application of the RBA in practice:**
 1. The compliance costs attached to IT systems required or the manual work required to implement
 2. A lack of guidance from the FIU or competent authority on the RBA. This is more acute for non-financial professions e.g. lawyers and notaries. The FATF guidance was considered important but most respondents said they prefer guidance adapted to their own national situation
 3. The danger that the RBA chosen by entities is questioned by the competent authorities if a suspicion is not aroused.

Risk assessment in action – the FSA’s 2011 assessment

- FSA 2011: **Banks’ management of high money laundering risk situations**

[http://www.fsa.gov.uk/pubs/other/aml_final_report.pdf]

- The report describes how banks operating in the UK are managing ML risk in higher risk situations. It focuses on correspondent banking relationships, wire transfer payments and high-risk customers including PEPs

Instances of good practice

Risk assessment systems and controls appropriate to nature, scale and complexities of the business

ML/FT risk assessment to at least include consideration of company structure, political connections, country risk, reputation, source of wealth/funds, expected account activity, sector risk, involvement in public contracts

Risk assessment policies reflecting risk assessment procedures and risk appetite

Understanding & awareness of risk assessment policies, procedures, systems and controls

Quality assurance of risk assessment policies, procedures, systems and controls

Appropriately-weighted scores for risk factors

Clear audit trail supporting ratings

Instances of poor practice

Allocating higher risks countries with low risk scores to avoid EDD

Inappropriate customer classification systems which make it almost impossible for a customer to be classified as high risk

Failing to assess customers until shortly before an on-site visit

Allowing the business to override customer risk scores without sufficient evidence to support decision

MLROs being too stretched or under-resourced

Low risk weightings due to incorrect reasons – frequent dealings, “regulated” industries (such as extractive industries and pharmaceuticals) not regulated for AML purposes

Three things to take away

1. We all need to carry out some form of risk assessments to at least determine PEPs and high AML risk situations

2. We don't need to adopt a full RBA and if we do, it need not be overly complex

3. Ensure you can justify your approach with the regulator - a "no surprises" attitude!

Thank you

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