



AML Risk Assessments & Suspicious Activity Transaction Monitoring (July 28, 2009)

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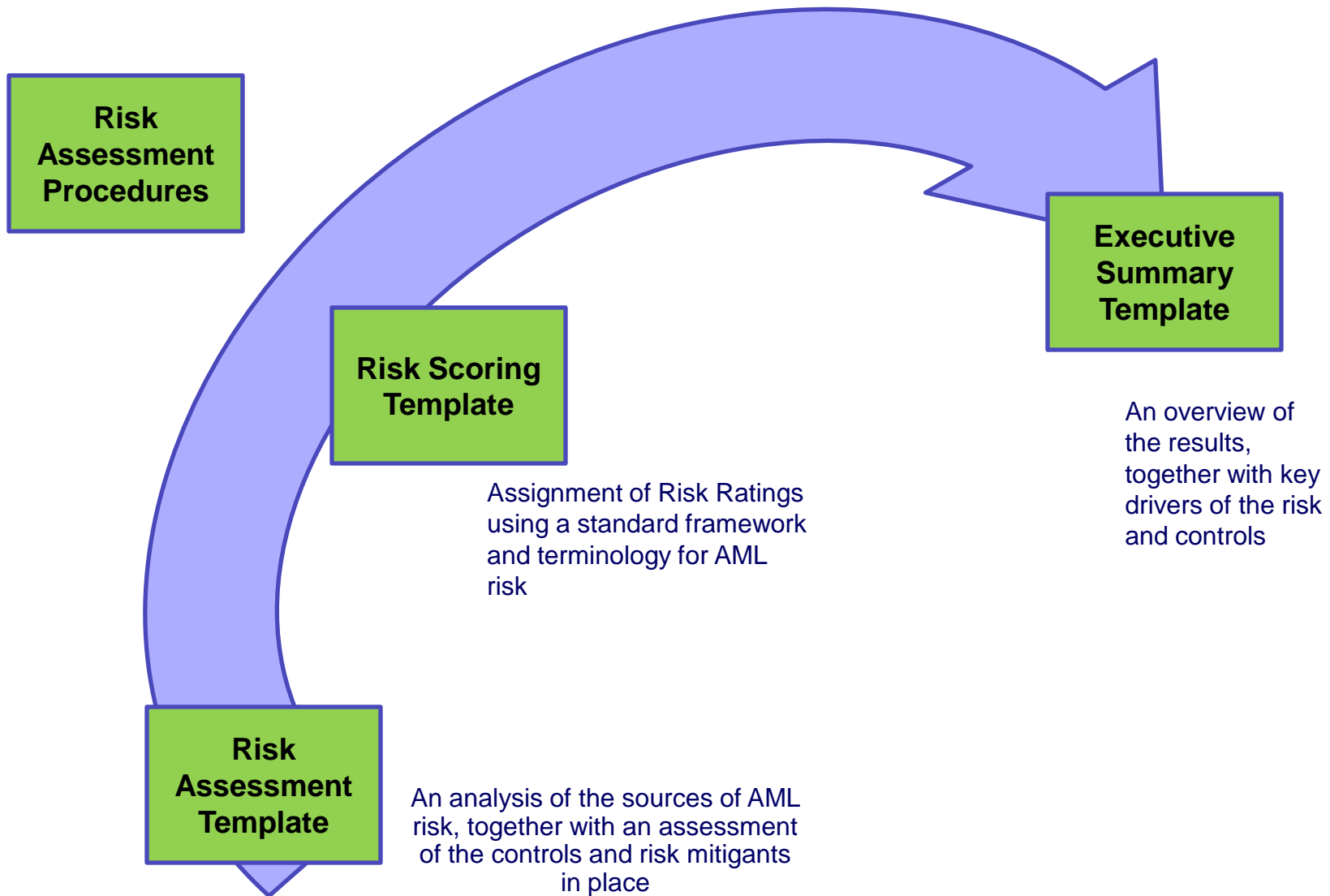
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AML Risk Assessments - Introduction

- Fundamental component of a risk-based AML compliance program.
- Documents source and quantity of AML risk arising in each Line of Business (LOB).
- Captures details on scope and effectiveness of risk mitigants and control processes used to manage AML risk.
- Provides Board, Senior Management, LOB, and Compliance Officers with an analytical assessment of:
 - inherent AML risk levels arising from customers, transactions and geographies;
 - risk mitigants and control processes in place to manage this risk, as well as their effectiveness.
- Beneficial in meeting the needs/expectations of regulators and Internal Audit.

Risk Assessment Program – Procedures, Templates and Bottom-Up Process



Risk Assessment Program

Inherent AML Risk Factors

Risk Assessment documents each LOB's exposure to inherent AML risk factors arising from three primary areas:

- 1) Products and services known to have been, or which can potentially be, abused by money launderers and terrorists;
- 2) Customers and entities who move large amounts of cash or other funds to disguise 'dirty money'; and
- 3) Countries and territories with weak AML controls, with a documented history of corruption problems, or associated with the production and distribution of narcotics or associated with terrorism.

AML Risk Assessment Program

Typical Criteria for Assigning Risk Ratings for Inherent Risks

- **Low** - Indicates truly minimal activity related to high-AML risk customers or products and services.
- **Medium** - Risk is characterized by larger numbers of high-risk customers and volumes of transactions in high-risk products.
- **High** - Is appropriate when high-risk customers or products and services are actively pursued as a business strategy and as a result comprise a material portion of the customer base, transactions and financial performance.

Note: Many institutions use High and Neutral as an alternative

AML Risk Assessment Program

Risk Mitigants and Controls

- Risk may be managed, mitigated or, perhaps in some instances, eliminated. “Mitigation Factors” are those controls that, if properly implemented and maintained on an on-going basis, could lessen or mitigate some or all of the inherent risk.
- Controls can be preventive (such as checklists, training, written procedures) or detective (such as monitoring/quality assurance, LOB compliance team testing). Preventive controls are generally considered to be stronger than detective controls in managing risk. With appropriate controls in place, even a high inherent risk may be reasonably managed.

AML Risk Assessment Program

Assigning Risk Ratings for Risk Mitigants and Controls - Example

- **Strong** - indicates that the control is in place, well established, extremely effective in preventing the occurrence of risk events, and performed with an appropriate frequency that is relevant to the process. A strong control is also performed effectively by the control group and is periodically tested to ensure it is still in place. For a strong assessment, there must have been no significant risk events that occurred as a result of a breakdown of the control.
- **Adequate/Medium** - rating characterizes a control that is in place, established and generally effective in preventing the occurrence of risk events. It is performed periodically and on an acceptable frequency. For a satisfactory rating, such controls must remain in place and be effectively performed. There must have been no significant risk events that occurred as a result of a breakdown of the control.
- **Weak** - describes a control that is not in place although it needs to be, is not particularly effective in prevent risk events, may not be performed with any particular frequency or on any scheduled timetable (if one can be ascertained) or there were significant risk events that occurred and may have been prevented if the control was in place or a stronger control.

PHASE 1: Assessment of the Inherent AML Risk

Example of inherent AML risk assessed across 5 main risk areas. Multiple risk factors are evaluated within each main risk area to determine the overall inherent AML risk for each country/business.

Legend: For each country / risk area / risk factor the inherent AML risk can be rated on a scale of:

	Level	Score
Risk	Very High	4
	High	3
	Medium	2
	Low	1

Inherent AML Risk

Summary Dashboard

Country Business	Customer Base Inherent Risk	Product/Account Type Inherent Risk	Transactional Inherent Risk	Business Strategy Inherent Risk	Geography Inherent Risk	Overall Inherent Risk
Country A	Medium	Medium	Low	Medium	Low	Medium
Country B	Medium	Medium	Medium	Low	Low	Medium
Country C	Low	Low	Low	Medium	Low	Low
Country D	Medium	Medium	Medium	Medium	Low	Medium
Country E	Medium	High	High	Low	Medium	Medium
Country F	Low	Low	Low	Low	Medium	Low
Country G	Medium	Low	Low	Low	Low	Medium
Country H	Low	Low	High	Medium	Medium	Medium
Country I	Low	Low	Low	Low	High	Low
Country J	Medium	Medium	Medium	Medium	Medium	Medium

Summary Dashboard provides an overview of the overall risk for each country by 5 main risk areas

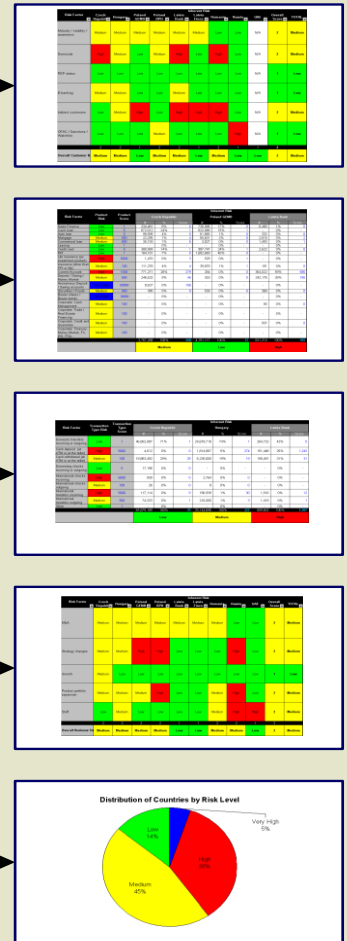
5 Main Risk Areas

- Customer Base Inherent Risk**
- Product / Account Type Inherent Risk**
- Transactional Inherent Risk**
- Business Strategy Inherent Risk**
- Geography Inherent Risk**

Examples of Risk Factors

- Maturity/stability
 - Domicile/residency
 - PEP status
 - E-banking
 - Indirect customers
- Portfolio of product offerings:
 - Sales finance
 - Mortgage
 - Life insurance
 - Anonymous savings accts
 - Portfolio of transaction types:
 - Domestic transfers
 - Cash deposits
 - International checks
 - International transfers
 - M&A activity
 - Business strategy changes
 - Expected growth
 - Product portfolio expansion
 - Staff turnover
- Country risk rating model:
 - Positive factors (FATF, EU, BIS)
 - Negative factors (OFAC, NCCT, 311, offshore, etc.)

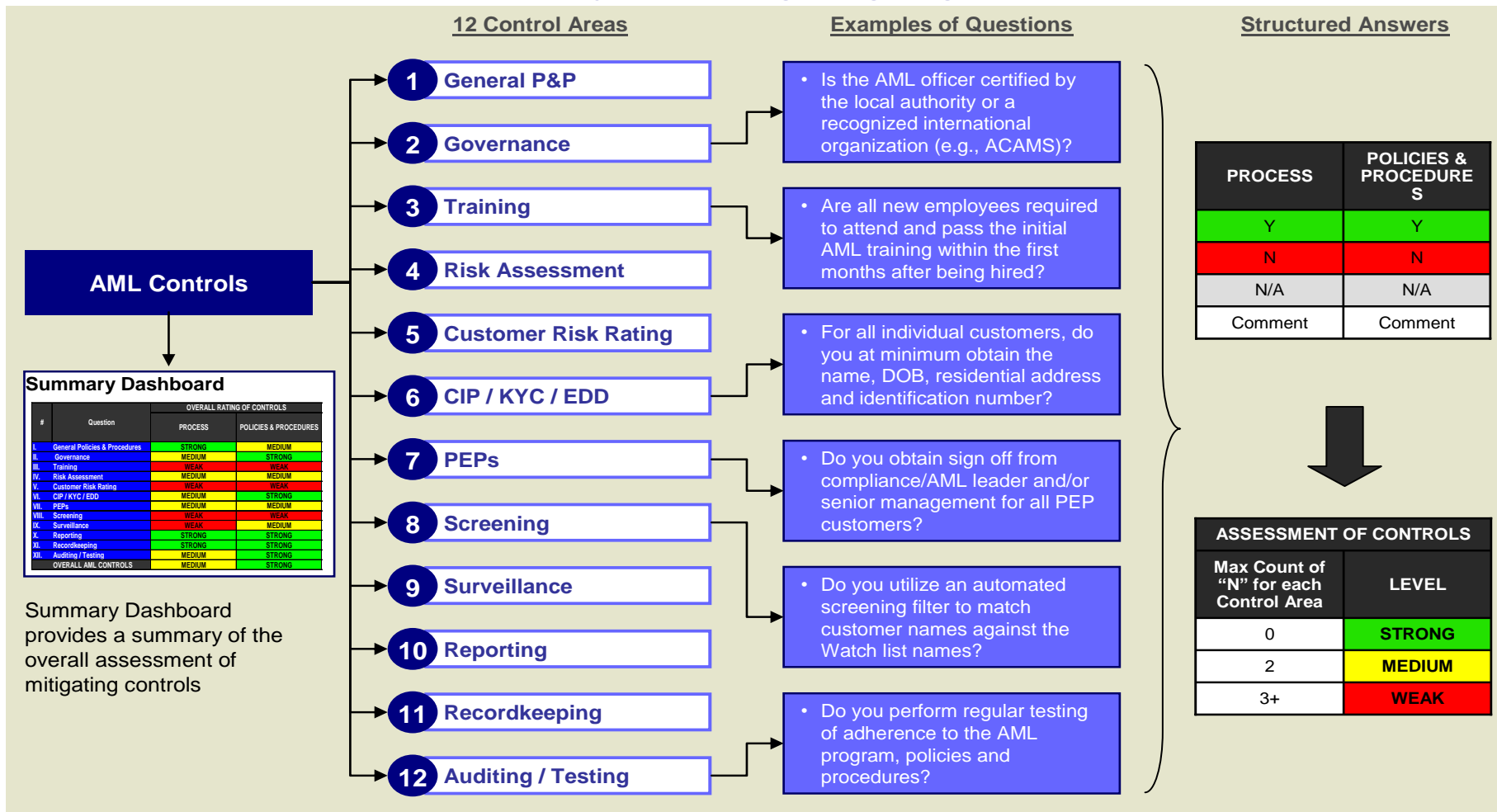
Risk Model Snapshot



PHASE 2: Assessment of the Residual AML Risk

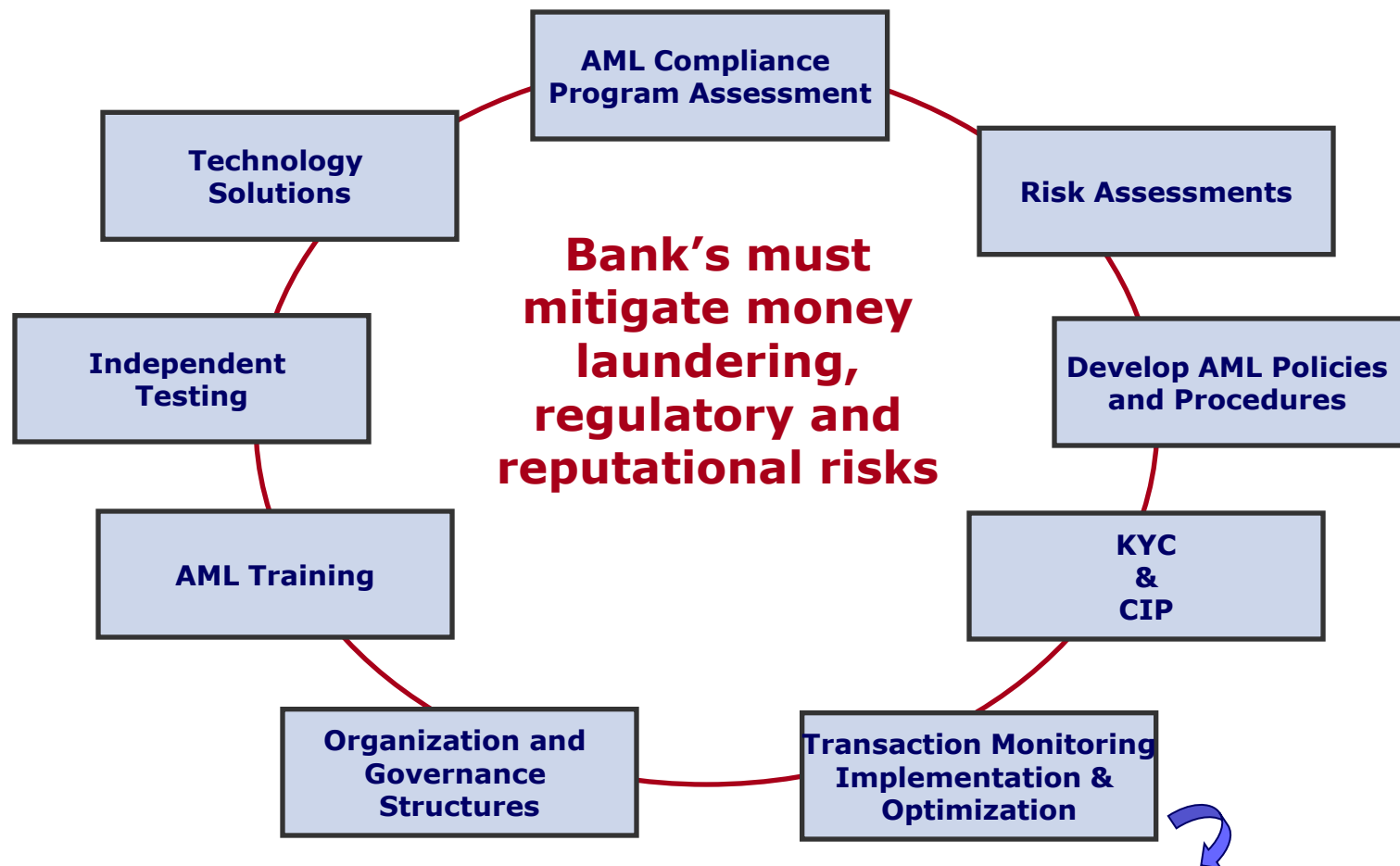
Step 1: Mitigating controls in form of AML policies, procedures and processes are assessed for each country/business

Step 2: Residual AML risk is derived by 'subtracting' mitigating controls from the inherent AML risk



Suspicious Activity Transaction Monitoring

A bank's AML program typically consists of multiple core competencies working together to mitigate risk



Let's Explore....

Suspicious Activity Transaction Monitoring

Many banks employ a sophisticated approach to customer account opening, monitoring, and analysis using a combination of technologies.

- Customers are on-boarded and their information is typically entered into a bank's KYC/CIP database. The data is matched against public and private information to search for risk factors including, but not limited to, PEP status.
- After the new customer completes the KYC/CIP process, accounts are opened and the risk scores are populated within the customer database.
- All account activity is periodically monitored through the bank's Transaction Monitoring application where risk factors are analyzed in connection with transactional patterns in search of anomalous activity at both customer and account levels.

Suspicious Activity Transaction Monitoring

- Comprehensive enterprise-wide account monitoring systems enable the bank to detect unusual & potentially suspicious activity that may indicate the need for additional internal money laundering investigations.
- Monitors account activity for unusual transaction patterns or events that exceed statistical thresholds within pre-defined scenarios. The systems typically utilize temporal analysis to evaluate transactions over multiple dimensions of time.
- Alerts generated are typically clustered with other intelligence data and reviewed by a bank's Financial Intelligence Unit ("FIU"). The FIU's mission is to bring a focused and proactive approach to the operational aspects of financial crimes deterrence, detection, and reporting. The result can be an enterprise view of risk from across the organization.
- Many banks use some sort of manual transaction monitoring, particularly for very high risk areas
- Determine if SAR filing is necessary

Sample Retail Transaction Monitoring Scenarios

- Structured Cash
 - Frequent cash deposits under the reporting threshold (e.g., patterns between \$8 to \$10k) or instances of periodic round dollar transactions
- High Velocity Wires
 - Instances of frequent wire activity within an account that exceeds a behavioral threshold
- High Risk ATM
 - Instances of unusual ATM withdrawal activity in high risk locations or geographies
- Dormant Accounts
 - Instances of sudden spikes in an account's activity which was previously dormant
- Large Incoming/Outgoing Wire
 - Instances where an account receives or sends a large wire that is outside the predefined threshold for that customer segment

Sample Investment Banking Transaction Monitoring Scenarios

- Significant changes in trading patterns
 - Instances of transactions within an account (commodities, securities or foreign exchange account) that are unusual in total dollar volume, trade size, frequency, or type of product, given the customer's typical trading history
- Stated business of customer not commensurate with type or level of activity
 - Instances of transactions within an account (commodities, securities or foreign exchange account) that are unusual in size, frequency, or product, given the information known about the customer's business
- Transactions in an amount beyond the known financial resources of the customer
 - Instances of transactions, or inflows of funds or assets, in an amount that appears unusually large given the known financial resources (such as income, revenue or total assets) of the customer

Sample Investment Banking Transaction Monitoring Scenarios (Con't)

- Transactions at an off-market rate or price
 - Instances of transactions within an account (commodities, securities or foreign exchange account) that are at a rate or price substantially unrelated to the market rate or price for the product purchased or sold
- Series of transactions (buys and sells) that do not result in change of ownership
 - Instances of a series of buys and sells of a product within an account on the same day (commodities, securities or foreign exchange account) that do not result in any change of ownership of the product, and there does not appear to be any reason for the transactions

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