

AML Risk Assessment – Challenges and Best Practices

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YOU CANNOT RUN AWAY, YOU HAVE TO MANAGE RISK !!!

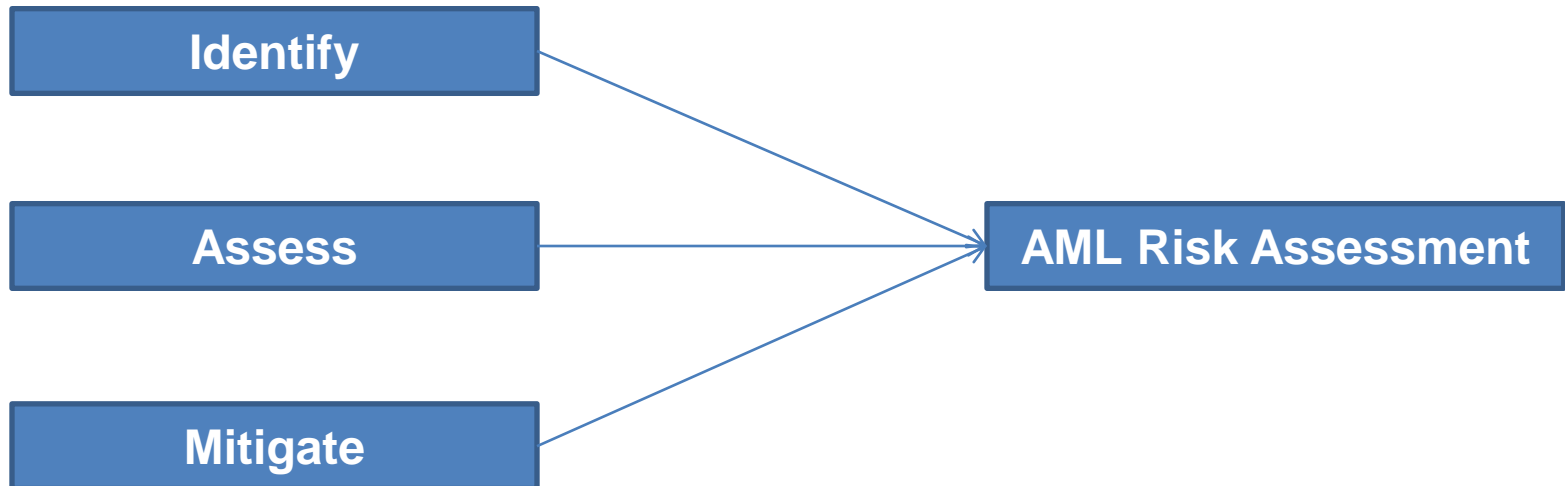
What is Risk?



What is an AML Risk Assessment?

An AML Risk Assessment identifies:

- an institutions inherent risks across a range of categories
- gaps and level of risk that is acceptable and in line with it's risk appetite
- the required internal controls to mitigate it



Need for AML Risk Assessment

- An entity should identify and mitigate risks in line with its risk appetite
- Integral component of a strong AML compliance program
- Enhances compliance & risk management programs
- It is a part of accountability towards stake holders and regulators
- Detects and helps prevent potential violations of laws and regulations.
- Thorough and continuous appraisal of entity's critical risks
- Severe penal actions from Regulators/LEAs
- Risk assessment is integrally linked to reputation and financial risk
- Board and Senior Management should be aware of inherent / residual risks

Rules v/s Risk Based Approach

Rules-based Approach

- One size fits all
- Bureaucratic
- Cumbersome
- Costly
- Hostile to customers
- Scarce resources not applied in the most effective way

Risk-based Approach

- More focussed
- Lesser bureaucracy
- Less paper work
- Reduced cost of AML
- Better customer experience
- Critical resources applied to high risk clients

In October 2008, the FATF adopted Guidance on the Risk-Based Approach (RBA) to combating Money Laundering and Terrorist Financing. This is now embodied not only in the FATF 40 Recommendations but also in other standards/ rules and regulations

Enterprise / Business Line Risk Assessment

Identifies Vulnerabilities

...at a macro level

By evaluating

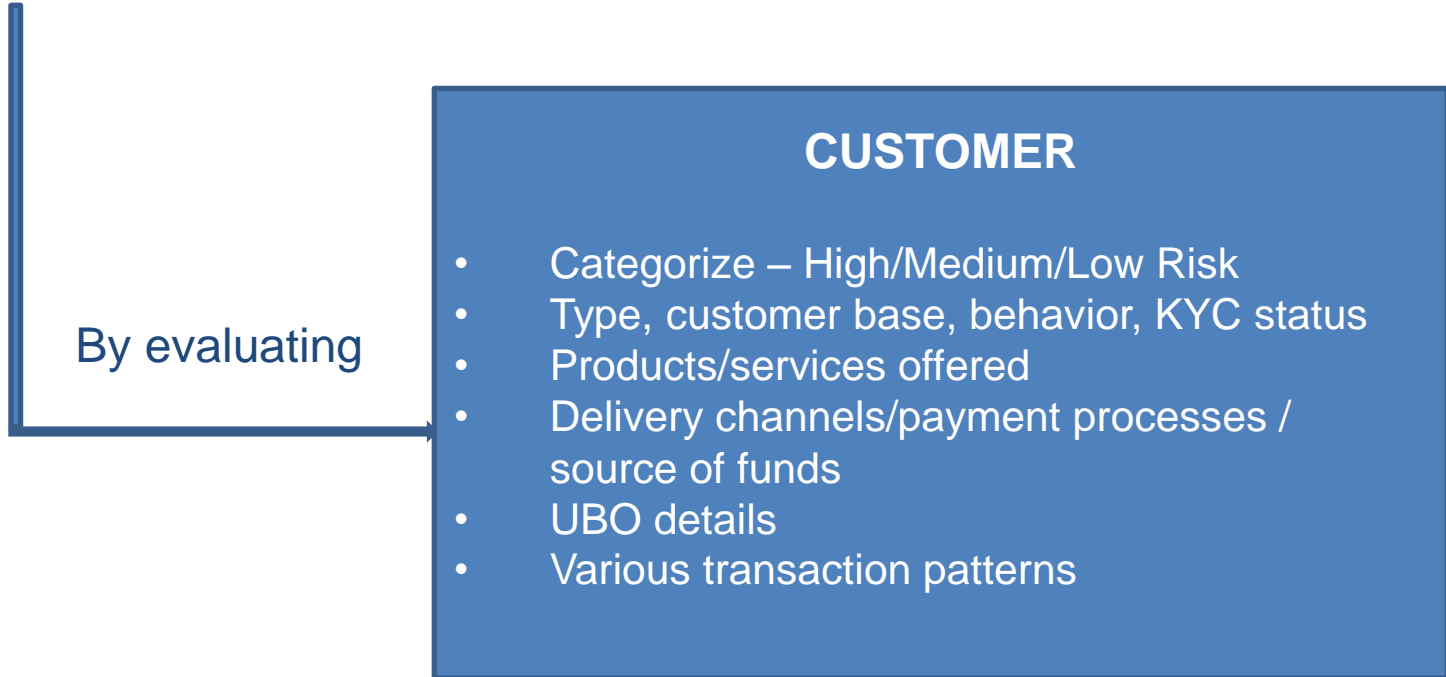
- Inherent risks of products/services
- Customer Base
- Geography

Controls



Customer Risk Assessment

Identifies Vulnerabilities



Controls



DNA of an AML Risk Assessment Program

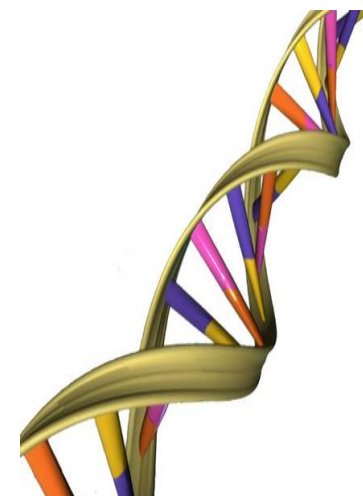
****Four Pillar Approach****

- **Overarching Contours**

- Single, consistent enterprise-wide model across business lines and geographies
- Formally defined structures, taxonomies and reporting forums for senior management review

- **People**

- Need for an experienced and mature Chief Risk Officer
- Have a equally experienced, knowledgeable & dedicated team
- Continuous training - create an internal center of excellence
- Board and senior management commitment



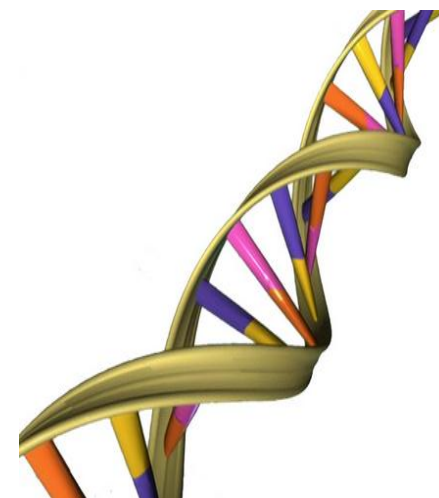
DNA of an AML Risk Assessment Program

- **Process**

- Globally consistent and standardized methodology
- Standard language and descriptions
- Equal emphasis on automated scoring and individual judgment
- Incident sharing and best practices

- **Technology**

- Automation to facilitate speedy analysis
- Define standard risk factors, conduct trend analysis, continuously validate control environments
- Dynamic real time reporting and escalation
- Central repository of data and knowledge



The Full Cycle of Risk Assessment

Risk Assessment

Identify and Analyze Risk

- Products
- Certain types of customers
- Geographic locations or hotspots

Put in place

Robust

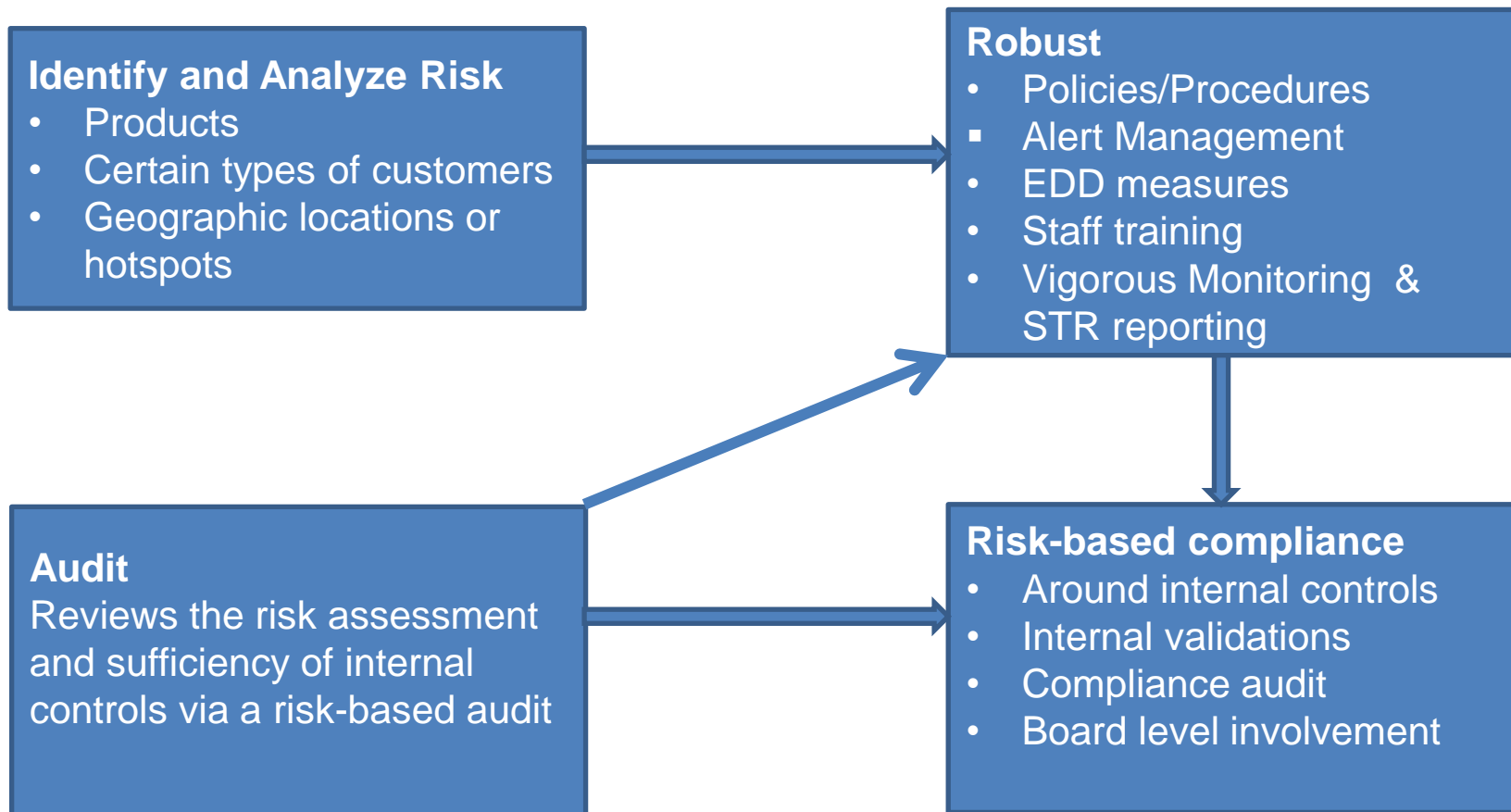
- Policies/Procedures
- Alert Management
- EDD measures
- Staff training
- Vigorous Monitoring & STR reporting

Audit

Reviews the risk assessment and sufficiency of internal controls via a risk-based audit

Risk-based compliance

- Around internal controls
- Internal validations
- Compliance audit
- Board level involvement



Challenges/Solutions – AML Risk Assessment

- **Timeline pressures**
 - Regulators demand frequent and periodic reporting
 - Time lag between requesting AML data and completing assessment
- ✓ **Solutions:** Automate, quality data feeds, emphasis on high risk areas

- **Resource constraints**
 - Limited experienced AML talent
 - Limited automation budgets
- ✓ **Solutions:** Invest in trained talent and automation/tools

- **Current process limitations**
 - Perceived as tick-box activity
 - Risk factors not weighted or defined appropriately
 - Risk assessment process not adequately documented
- ✓ **Solutions:** Risk culture, standard risk rating scale, process documentation

- **Data**
 - Cumbersome processes to collect qualitative / quantitative data
 - Limitations of data granularity affecting suitability of data
- ✓ **Solutions:** Simplify data generation, focus on high risk, red flag indicators and alert management systems



Best Practices – AML Risk Assessment

- Ideally be compatible with FATF Recommendations / Domestic guidelines
- Nurturing a compliance and risk culture
- Must be bespoke to the risk profile of the business
- Periodic, informed, documented risk assessments – focus on high risk
- Must be a lean and efficient model
- Regular staff training and engagement
- Must incorporate a change management system
- Identify red flags and monitor them closely
- CRO must play a key role in launch of new products/ services
- Exception handling – only at the highest level
- Board level engagement in risk assessment review is critical

Key Takeaways



- **Protecting your entity's reputation should be of primary concern**
- **You owe it to your stake holders – knowing risks and assessing them are different**
- **Risk assessment should have a judicious mix of automation and human intelligence**
- **Risk should be assessed/reviewed on a continuous basis – cannot be a one time activity**
- **Train, train, train and document all risks / mitigating steps**
- **Lastly, culture of risk plays a defining role in successful implementation**