



AML-ology

The study of AML trends and solutions

Building the Proper Customer Risk Assessment Methodology

Customer Risk Assessment Methodology
Survey Detailed Report



Conducted 1Q 2017



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Purpose of the Survey:

Late last year we received a reader request to cover customer risk assessment methodology. A customer risk assessment is an important piece of the AML puzzle. Knowing who you're doing business with, as well as their past financial behavior is critical to staying compliant with current regulation. We feel that all other financial institutions will benefit from this survey and the knowledge of how the financial community handles their customer risk assessment methodology, and possibly discover new ways to modify their own program.

In this survey, we go over some of the factors involved in creating a customer risk assessment, and how our respondents tune each of them. Some of the questions include: approximately, how many customers are included in your customer risk rating/assessment? How many risk levels do you have? How was your customer risk rating methodology developed? Do you have multiple customer risk rating models? How do you risk rate your countries?

Purpose of this Report:

The purpose of this report is to summarize and demonstrate the overall findings of this survey. A detailed version of this report showing how retail and commercial banks are addressing this issue in their institutions is available. To receive a copy, please send us an [email](#) requesting a detailed copy of the survey results.

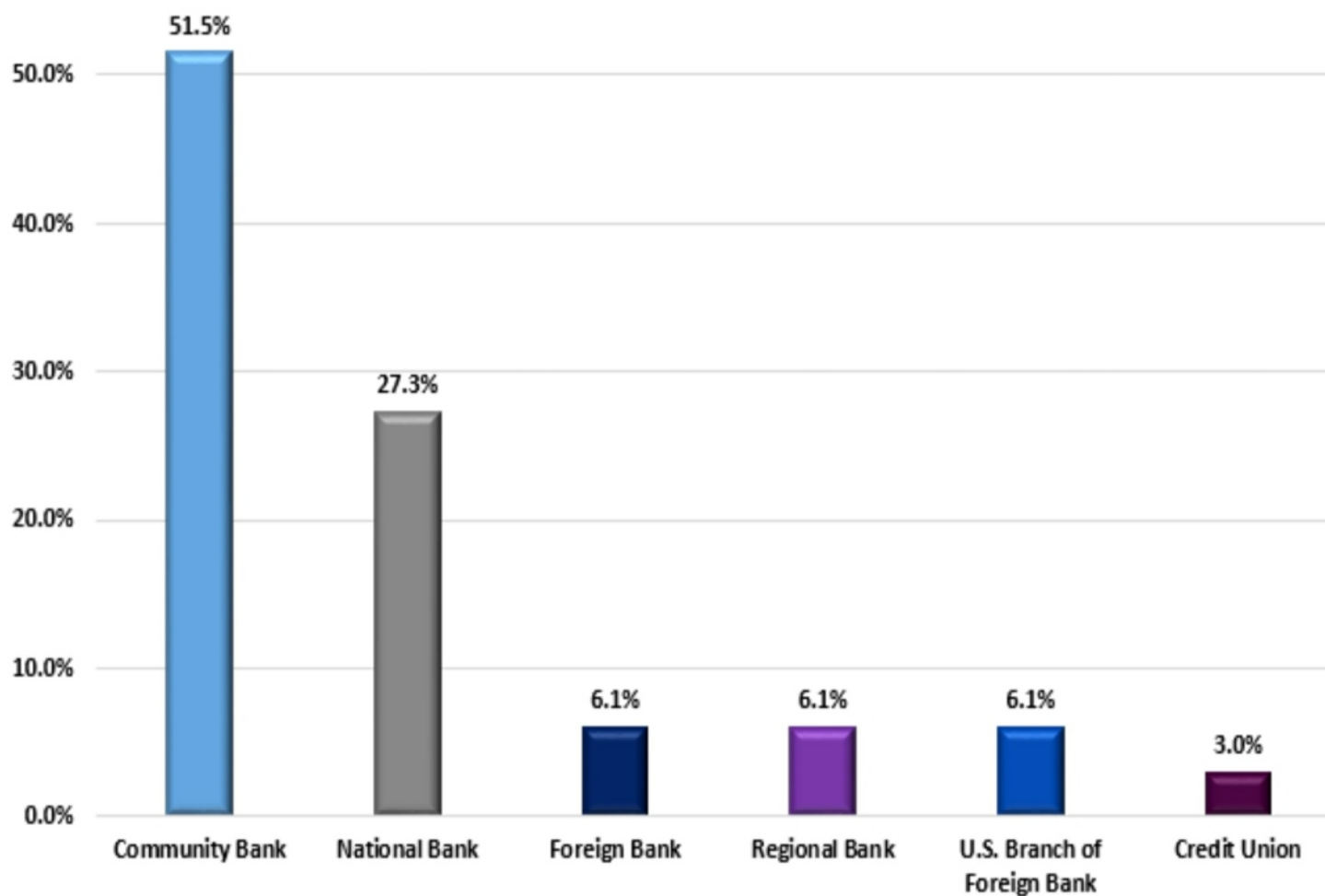




Retail Demographic Results:

Institution Type:

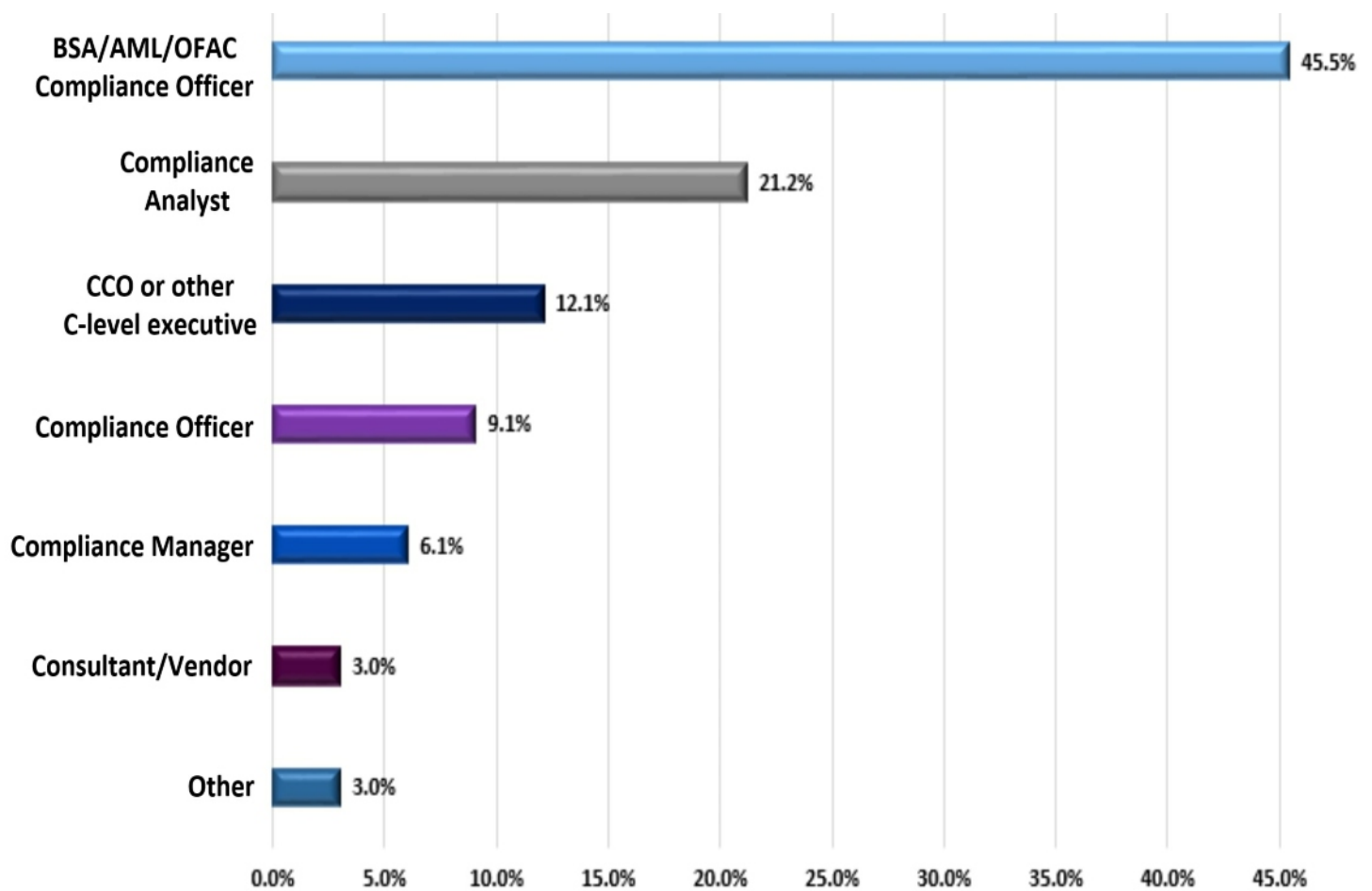
The two largest group of respondents were community banks (51.5%) followed by national banks (27.3%).





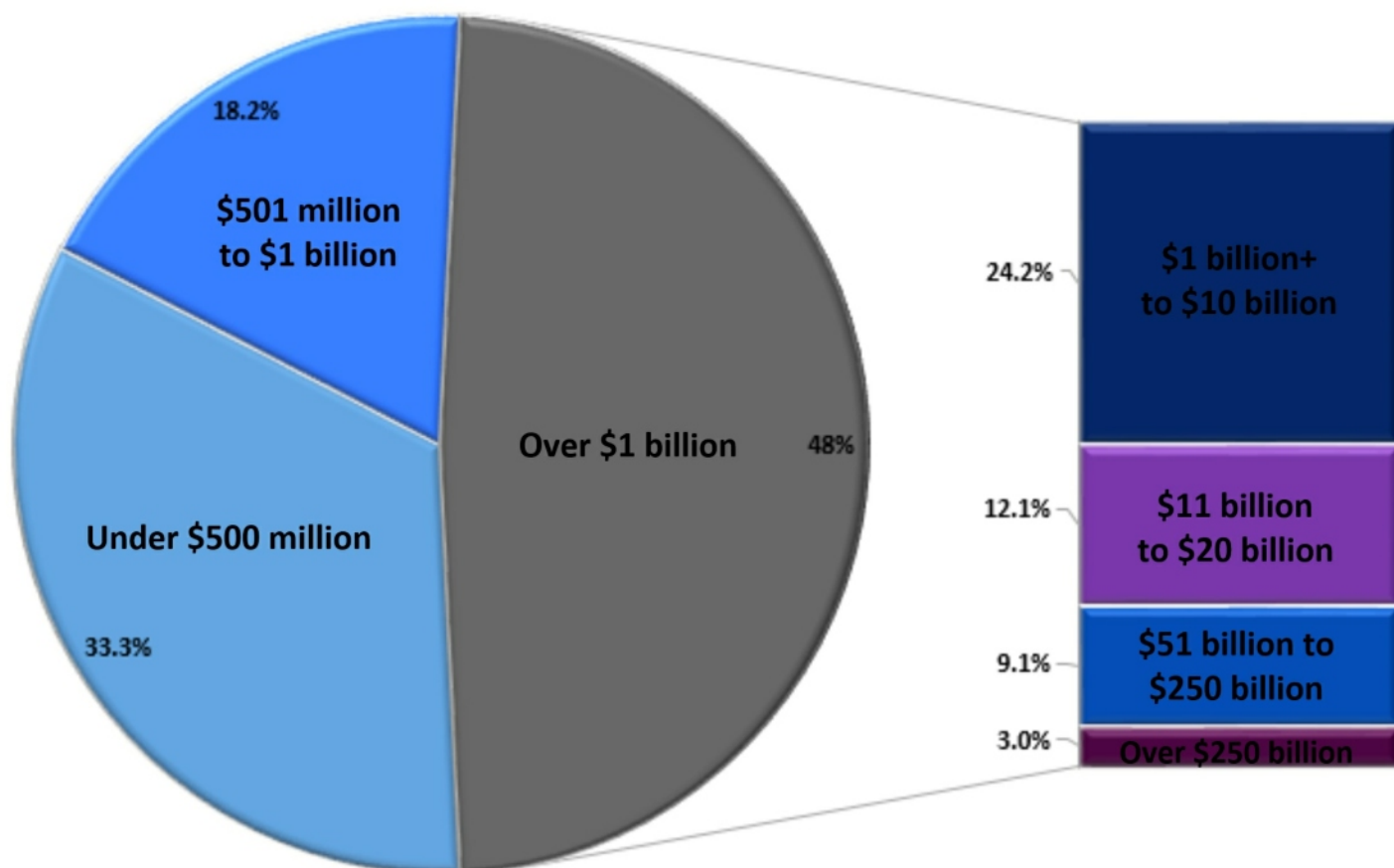
Current Position:

BSA/AML/OFAC Compliance Officer (45.5%) was the most common job title for this survey, followed by compliance analyst (21.2%).



Asset Size:

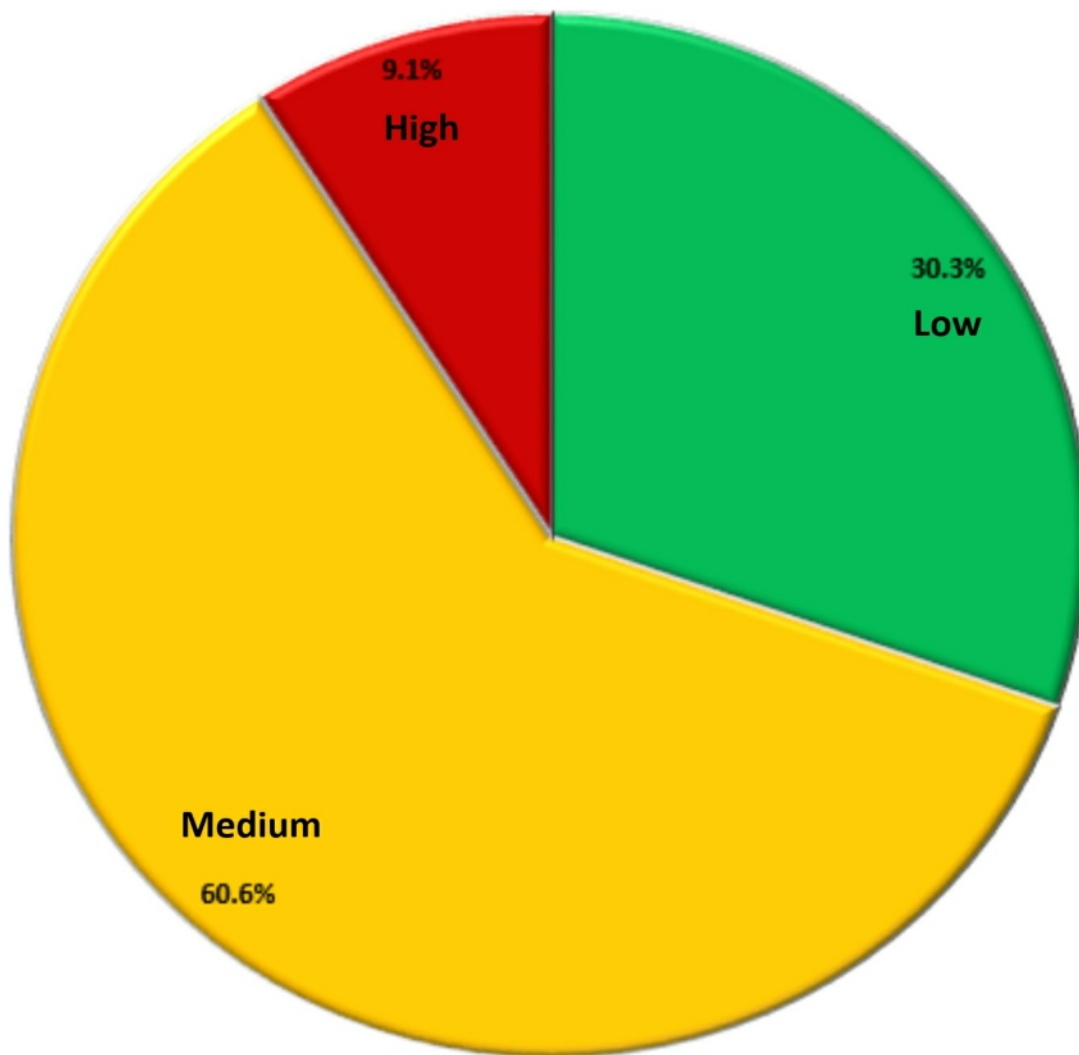
51.5% of respondents have assets below \$1 billion, and 48.5% have assets over \$1 billion. When broken down further the two most common segments were banks under \$500 million in assets (33.3%) and between \$1 billion - \$10 billion in assets (24.2%)





Risk Rating:

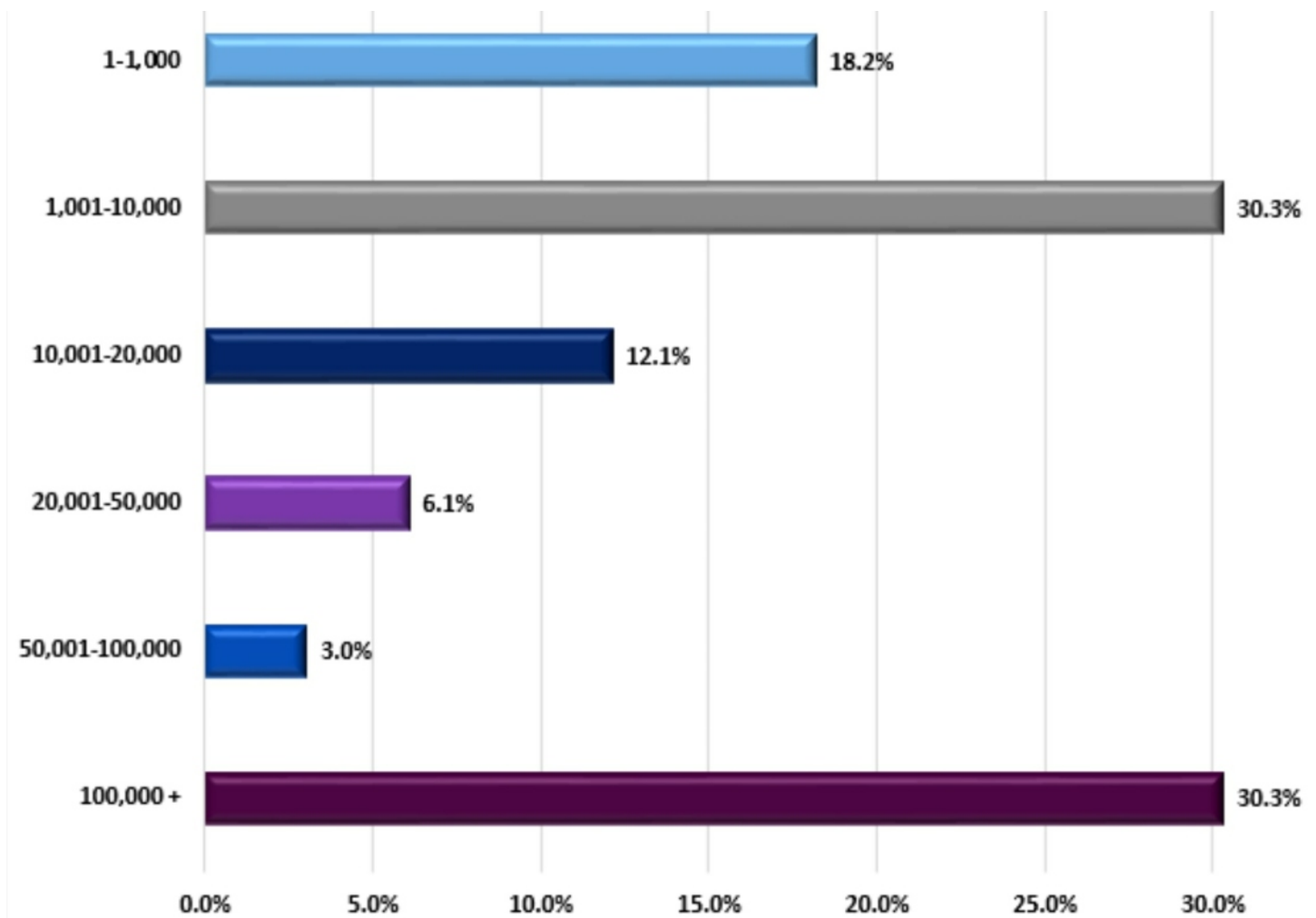
The final demographic question we asked our respondents was to describe their institution's overall risk rating. The majority stated that they have a medium risk rating (60.6%), the next most frequent answer was a low risk rating (30.3%), and finally a high risk rating (9.1%).



Retail Customer Risk Rating Questions:

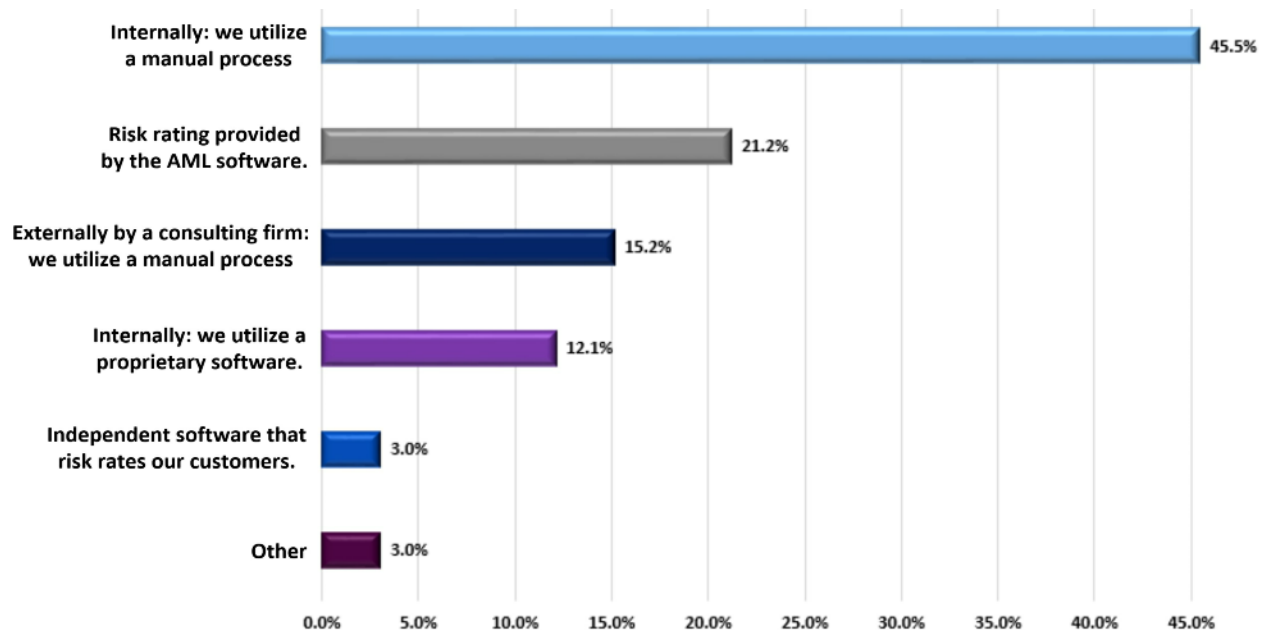
Customer Quantity

The typical number of customers included in a respondent's risk rating/assessment was tied between 1,001 - 10,000 and 100,000+ (30.3%). Respondents with 1-1,000 were close behind with 18.2%.



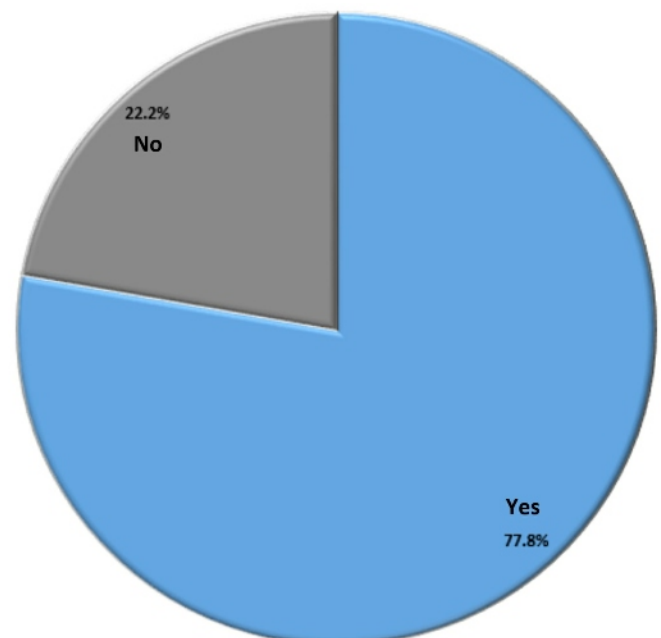
Customer Risk Rating Methodology Development

Most respondents developed their customer risk rating methodology internally using a manual process (45.5%). The second most common method was the risk rating provided by AML software (21.2%).



AML Software Configuration Modifications

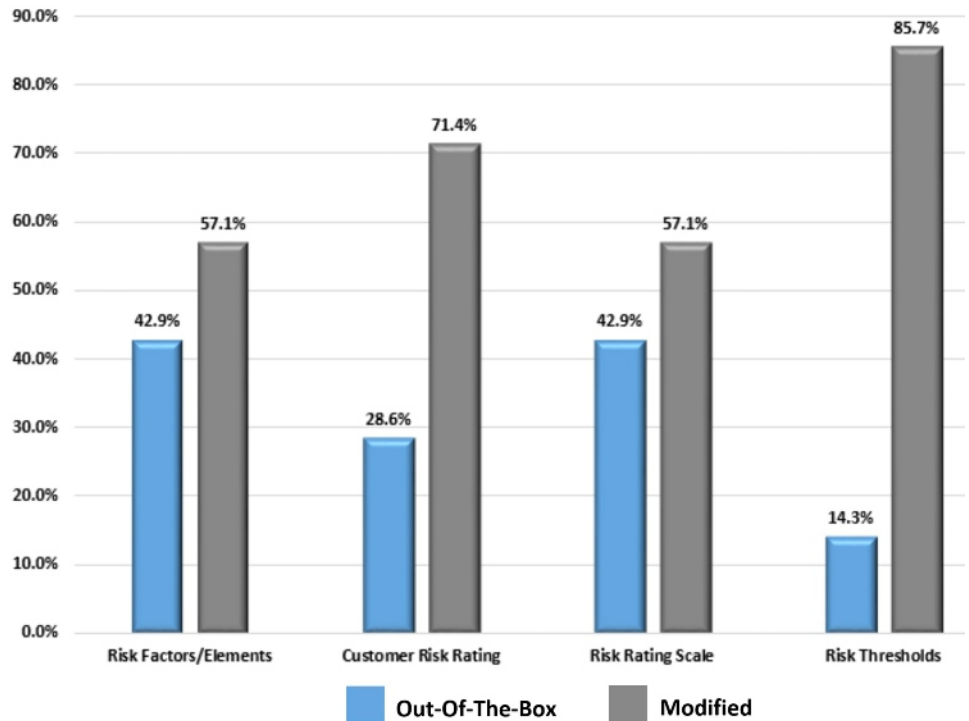
For respondents who use a vendor supplied software tool, 77.8% have modified the configurations; however 22.2% have not.





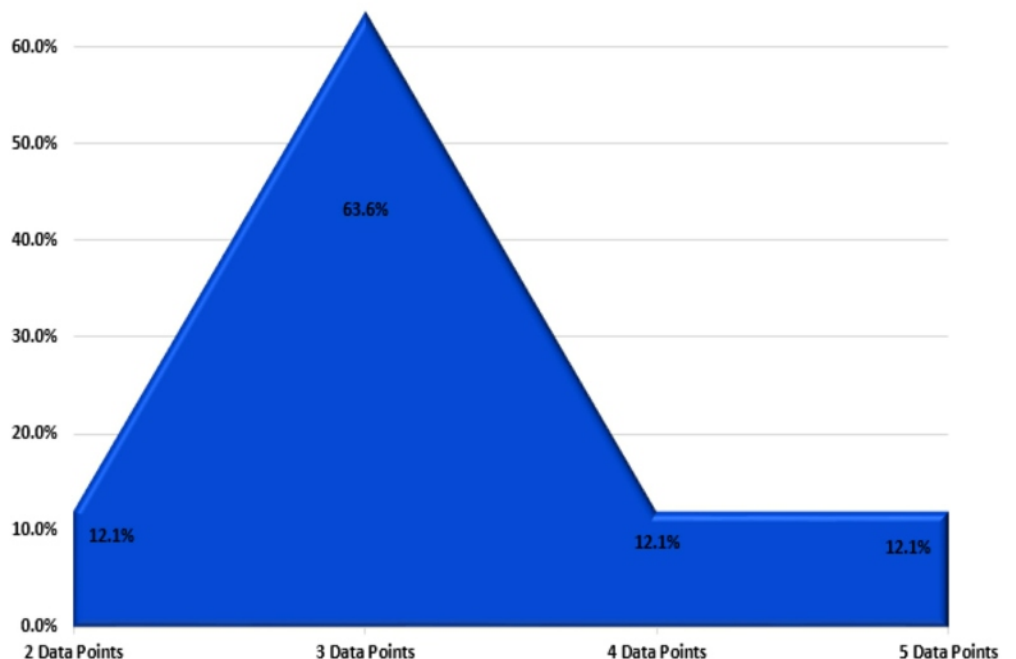
Out of the Box or Modified

The most common components of their software that respondents modified were risk thresholds (85.7%) and customer risk rating (71.4%).



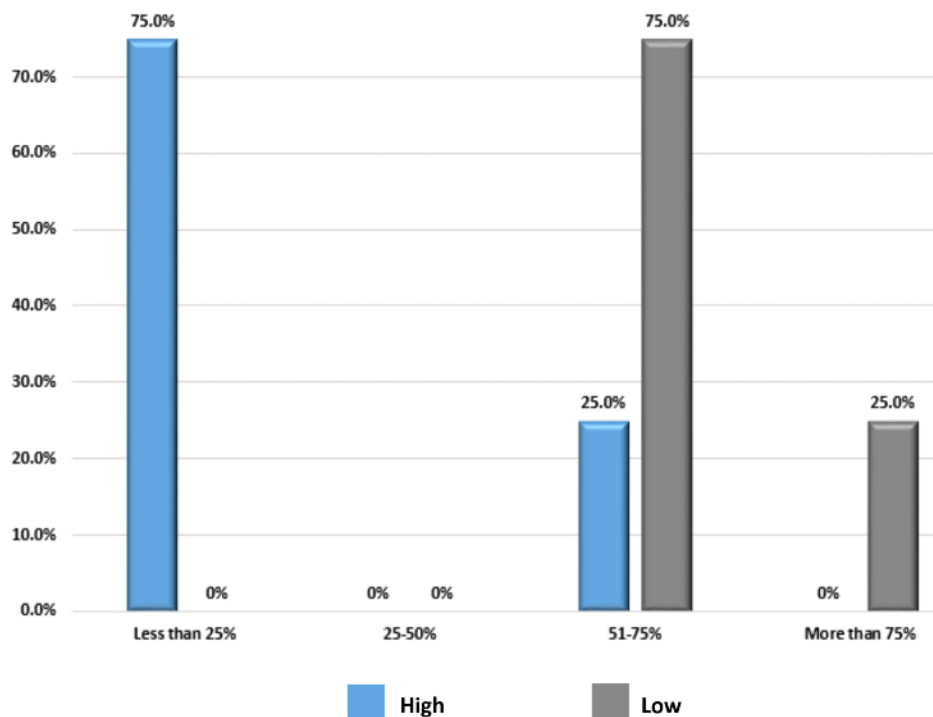
Number of Risk Levels

The overwhelming majority of respondents use three data points in their customer risk assessments (63.6%).



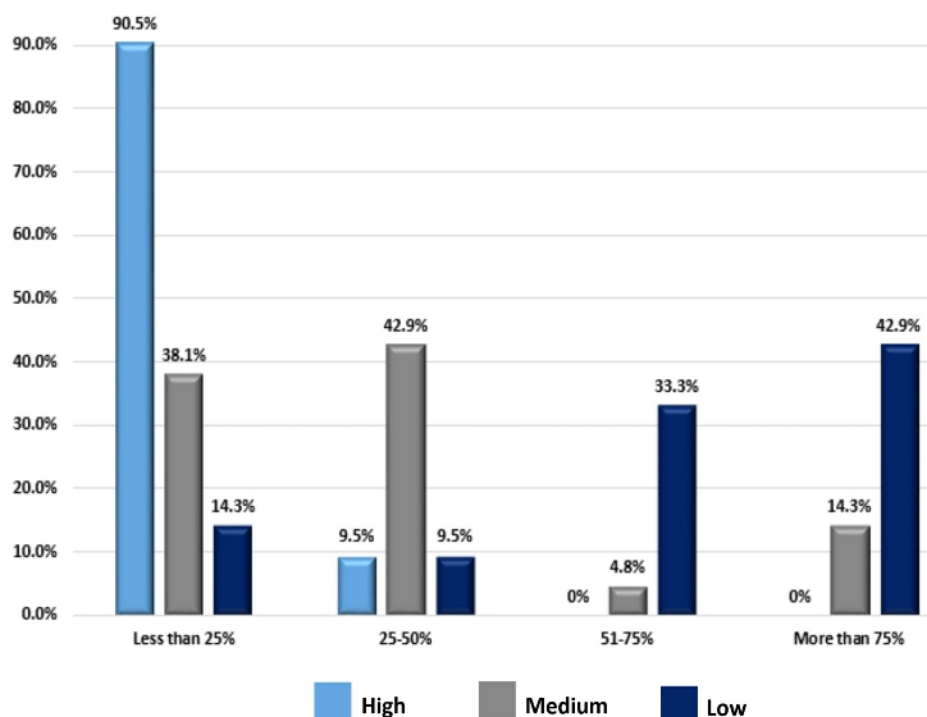
Two Data Point Risk Levels

Of the respondents who utilize two data points to risk rate their customers 75% have less than 25% high risk customers. 100% of respondents have between 51%-100% low risk customers.



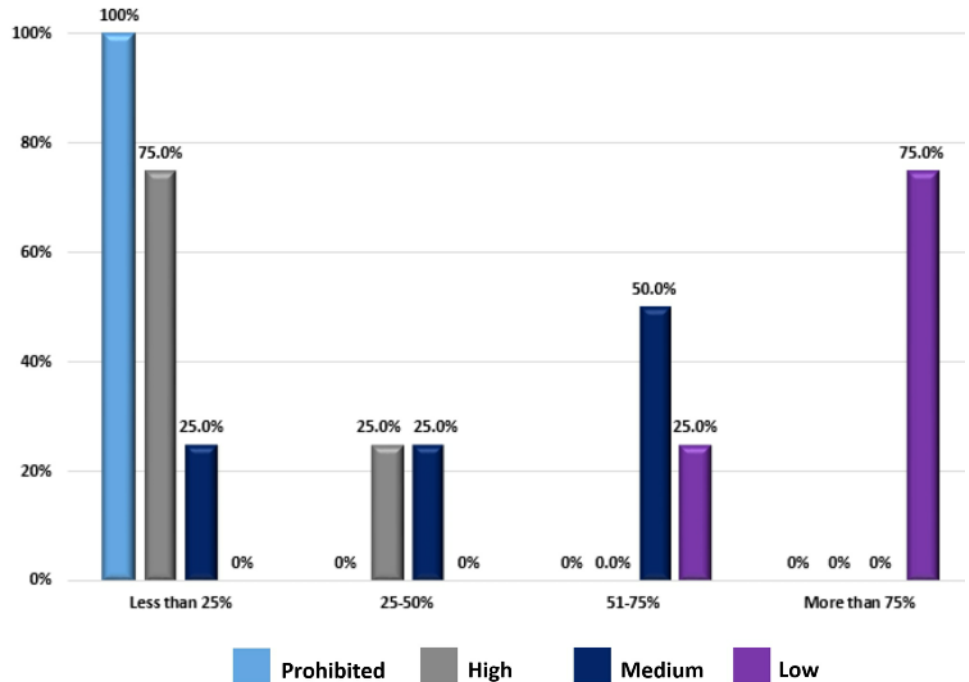
Three Data Point Risk Levels

Of the respondents who utilize three data points to risk rate their customers 90.5% have less than 25% high risk customers, 81% have between 0%-50% medium risk customers, and 76.2% have between 51%-100% low risk customers.



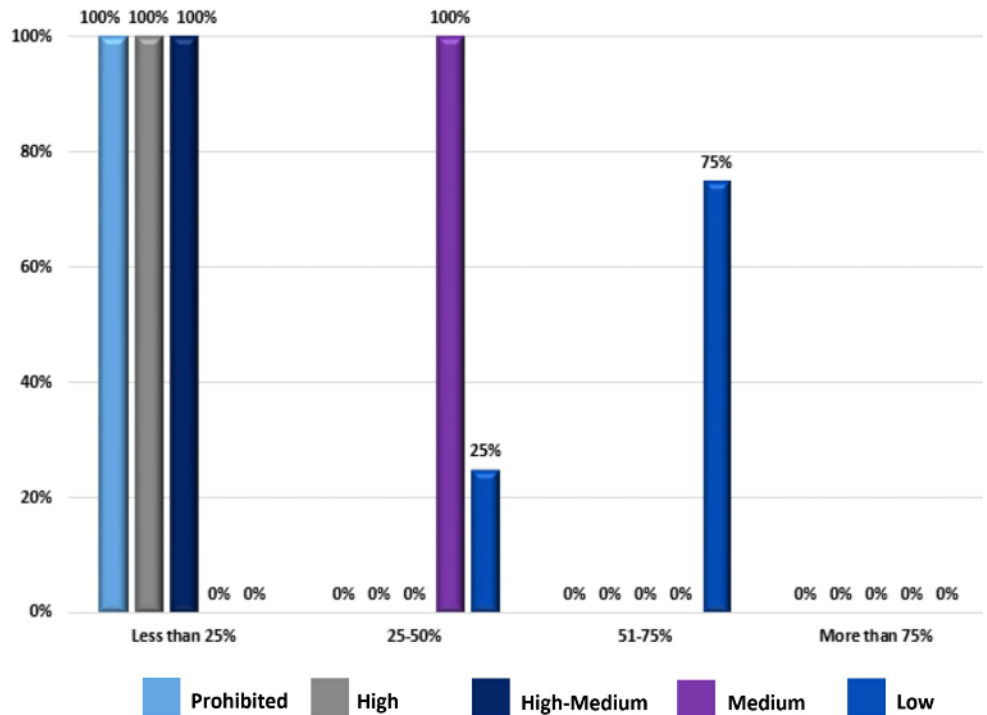
Four Data Point Risk Levels

Of the respondents who utilize four data points to risk rate their customers, 100% of respondents have less than 25% prohibited customers and 100% have between 0%-50% high risk customers. 75% of respondents have between 25%-75% medium risk customers. 100% of respondents have between 51%-100% low risk customers.



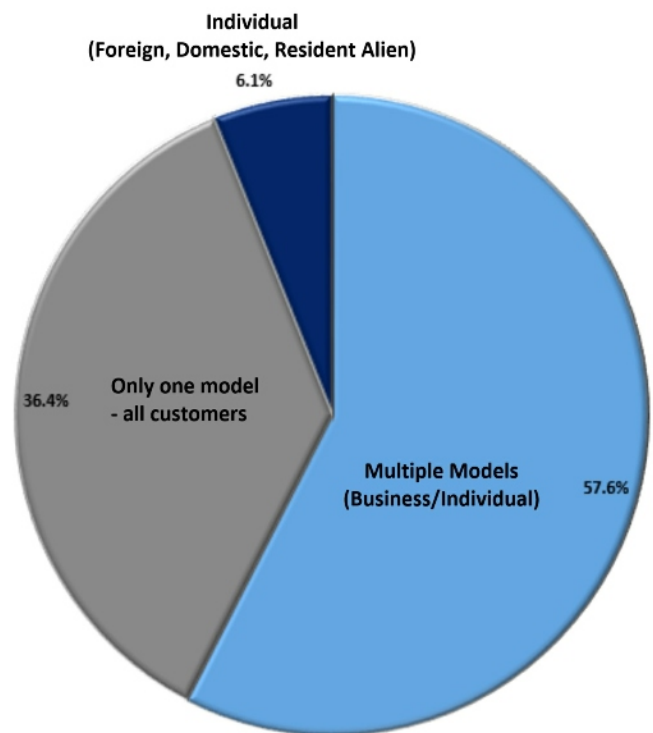
Five Data Point Risk Levels

Of the respondents who utilize five data points to risk rate their customers 100% of respondents have less than 25% of prohibited, high, and high-medium risk customers. 100% have between 25%-50% medium risk customers. 100% of respondents have between 25%-75% low risk customers.



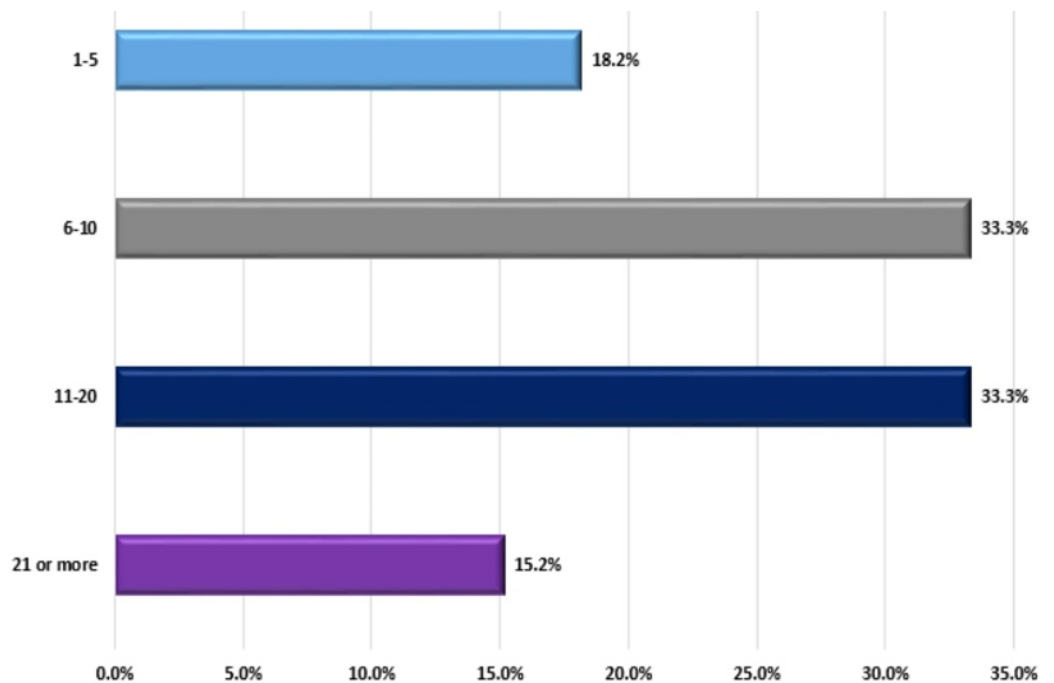
Risk Rating Models

57.6% of respondents utilize multiple risk rating models for customers, while 36.4% utilize only one model.



Elements per Model

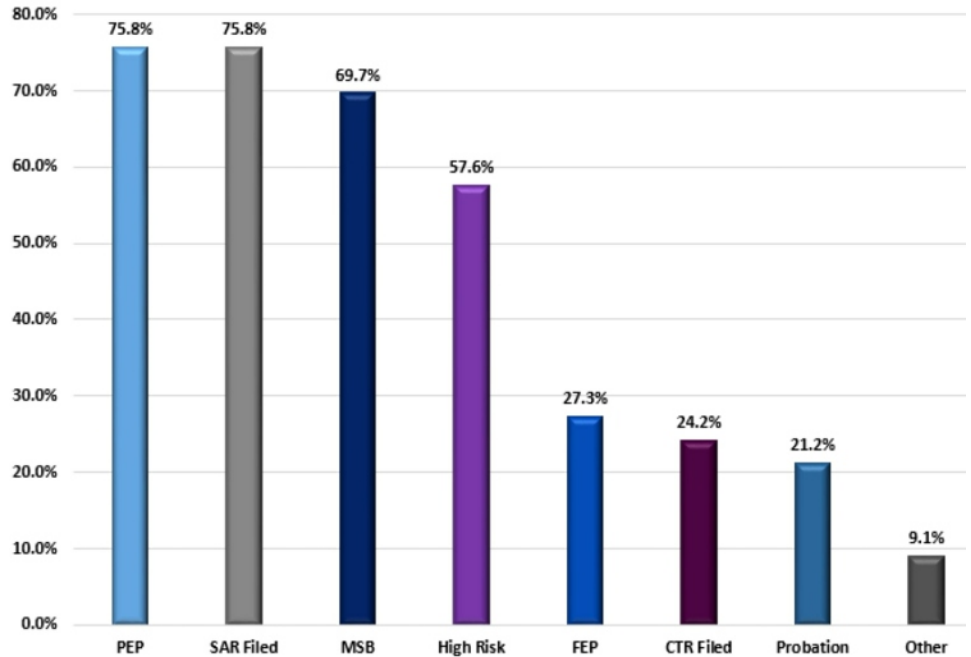
Two-thirds (66.6%) of respondents use between 6 and 20 elements (geographical, customer type, amount of transactions) per model.





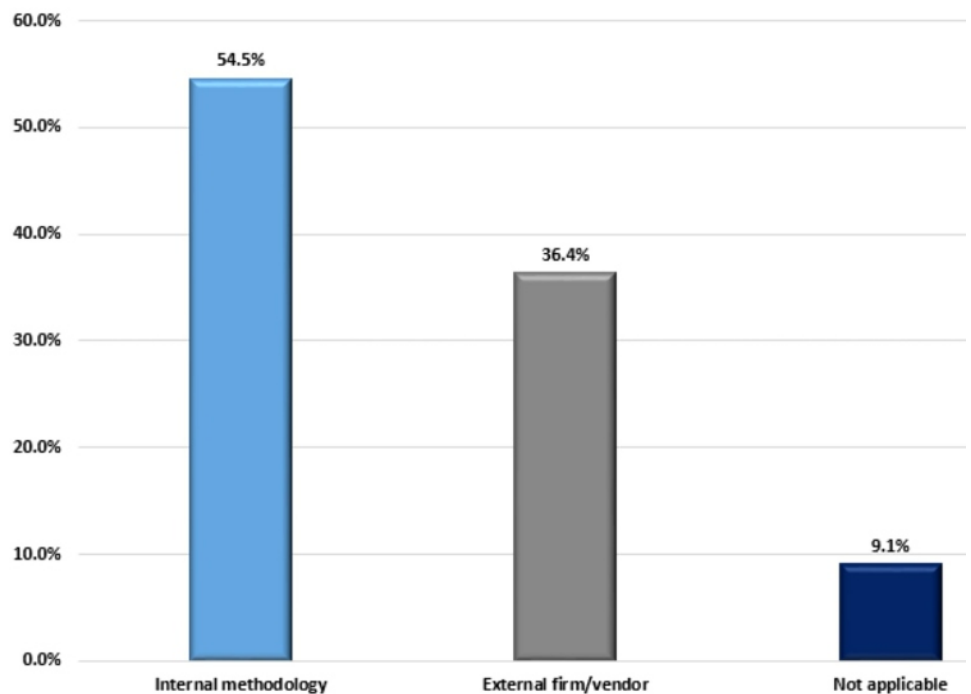
Overriding Dominant Items

75.8% of respondents believe both PEPs and SAR filing to be overriding dominant factors in their risk rating model.



Country Risk Rating

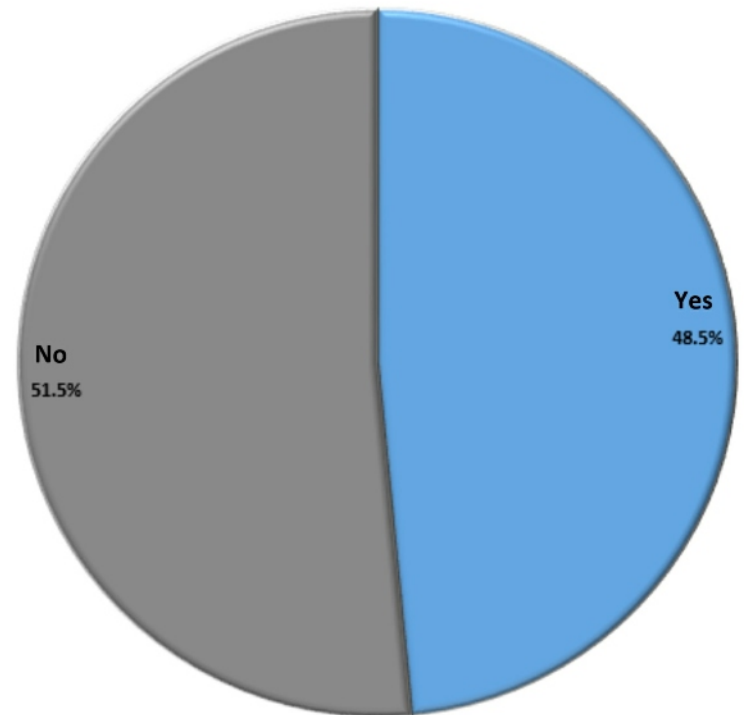
54.5% of respondents utilize an internal methodology to risk rate countries, whereas 36.4% use an external firm or vendor.





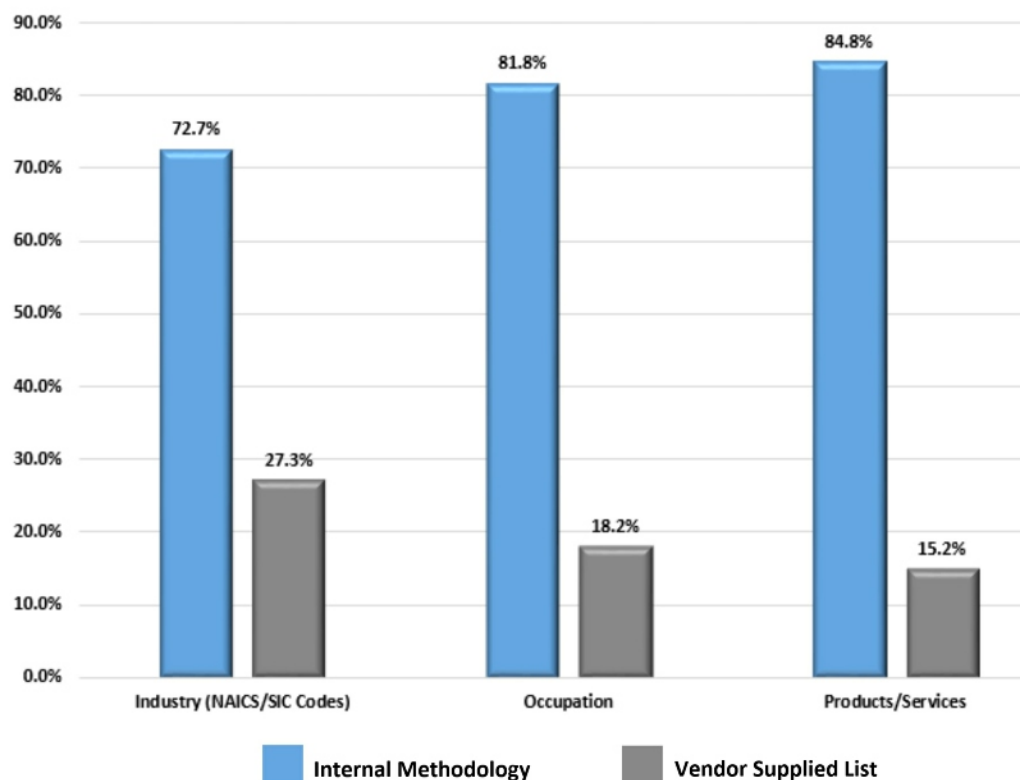
Beneficial Owners

51.5% of respondents do not consider the beneficial owners of the business in their risk model, surprisingly only 48.5% do.



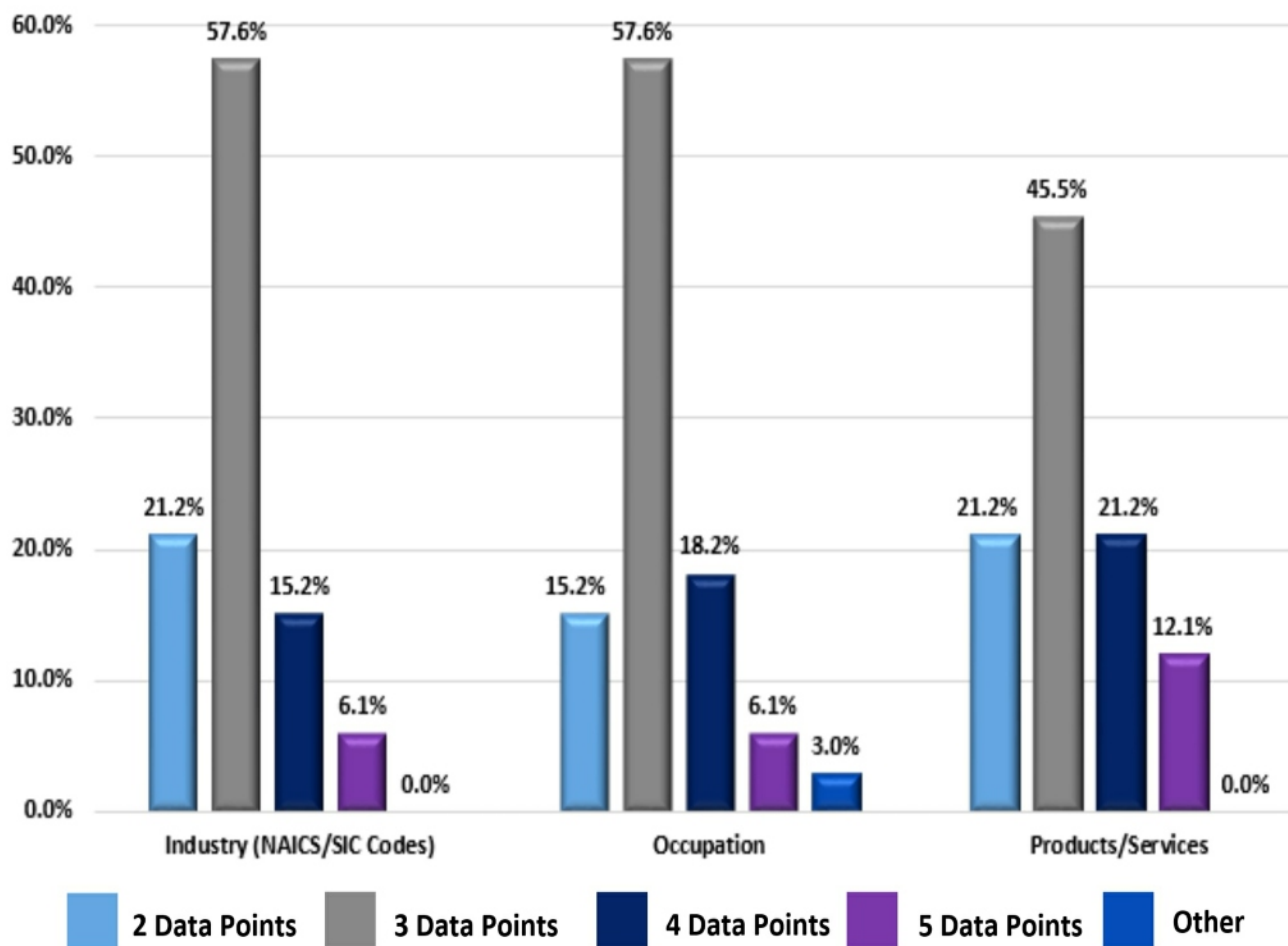
Methodology

The majority of respondents are utilizing an internal methodology for industry, occupation, and products/services factors (72.7%, 81.8%, and 84.8% respectively).



Scale

The following chart describes how many data points respondents utilize for each of the following categories within their risk model. Respondents were most likely to utilize three data points in each category: 57.6% for industry, 57.6% for occupation, and 45.5% for products/services.

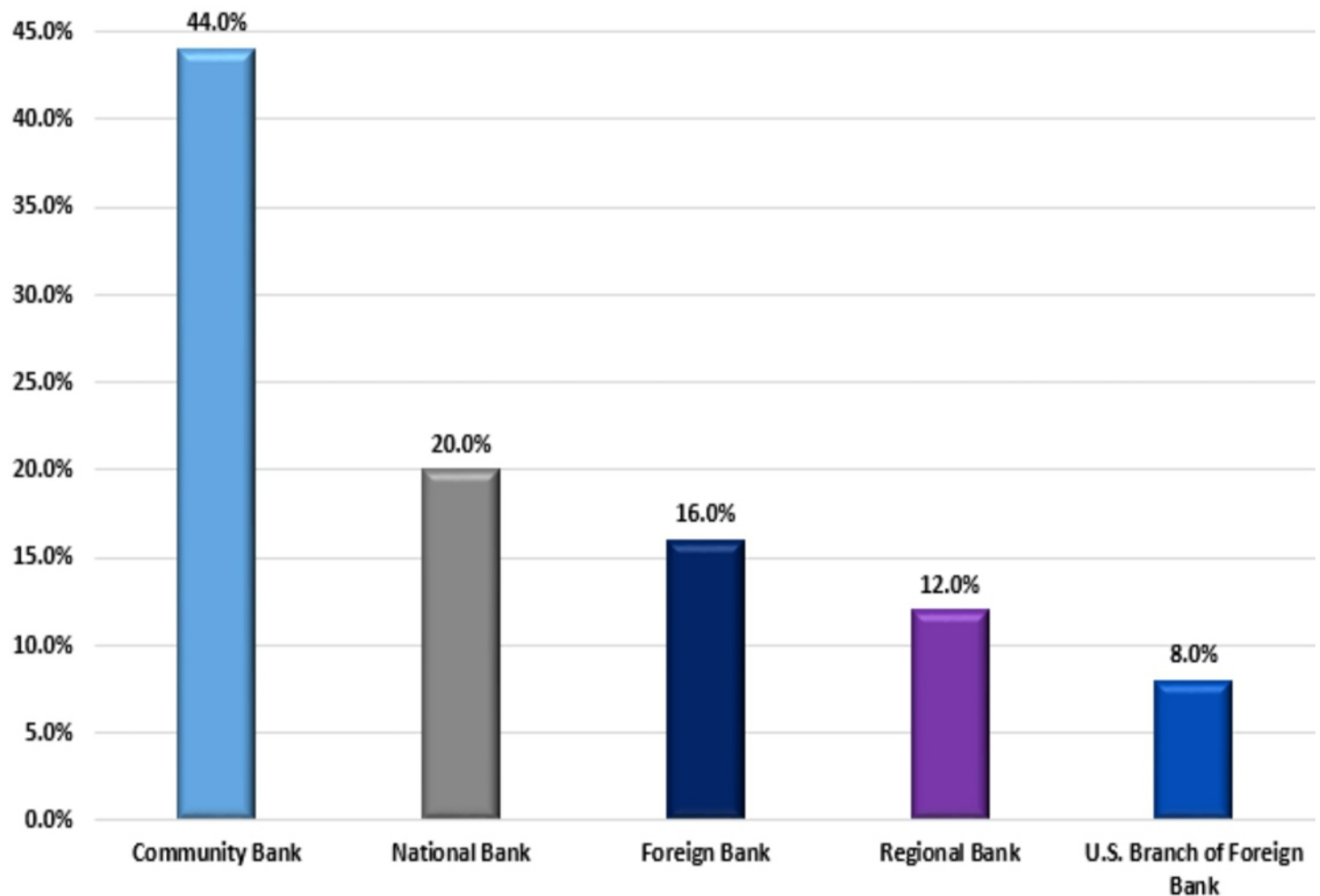




Commercial Demographic Results:

Institution Type:

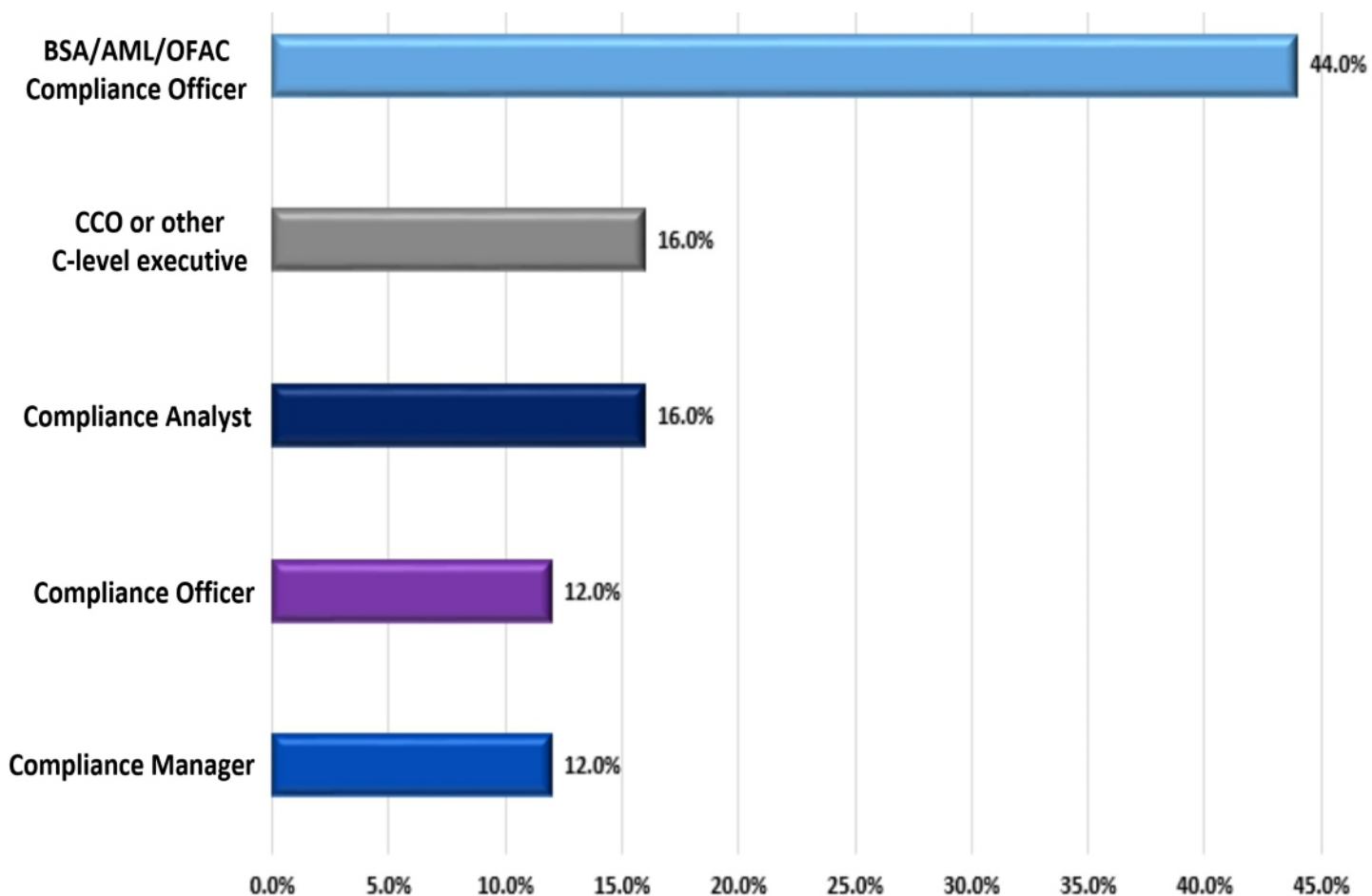
The two largest group of respondents were community banks (44%) followed by national banks (20%).





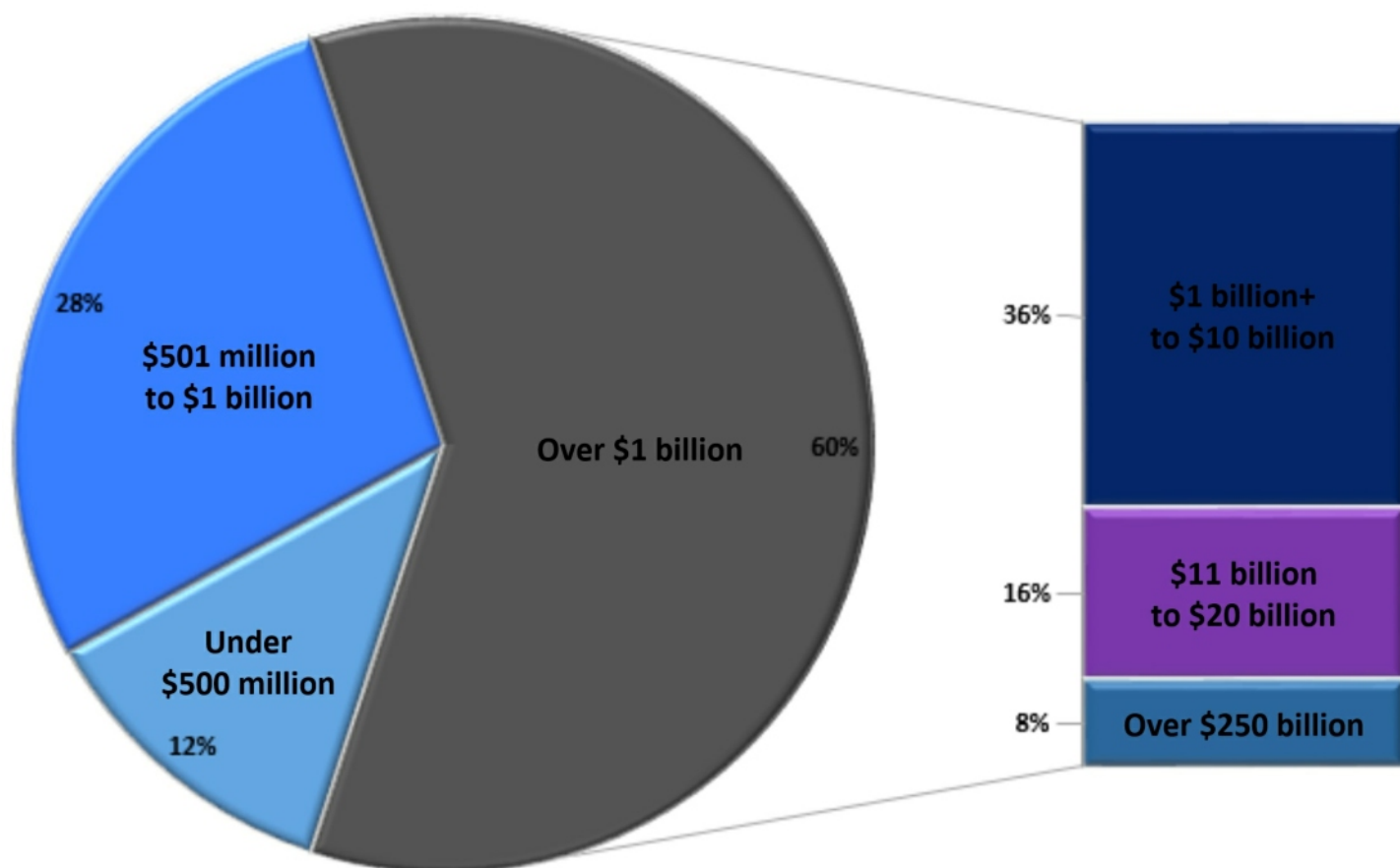
Current Position:

BSA/AML/OFAC Compliance Officer (44%) was the most common job title for this survey, with a tie of Compliance Analyst and CCO or other C-level executive (16%) for second most common.



Asset Size:

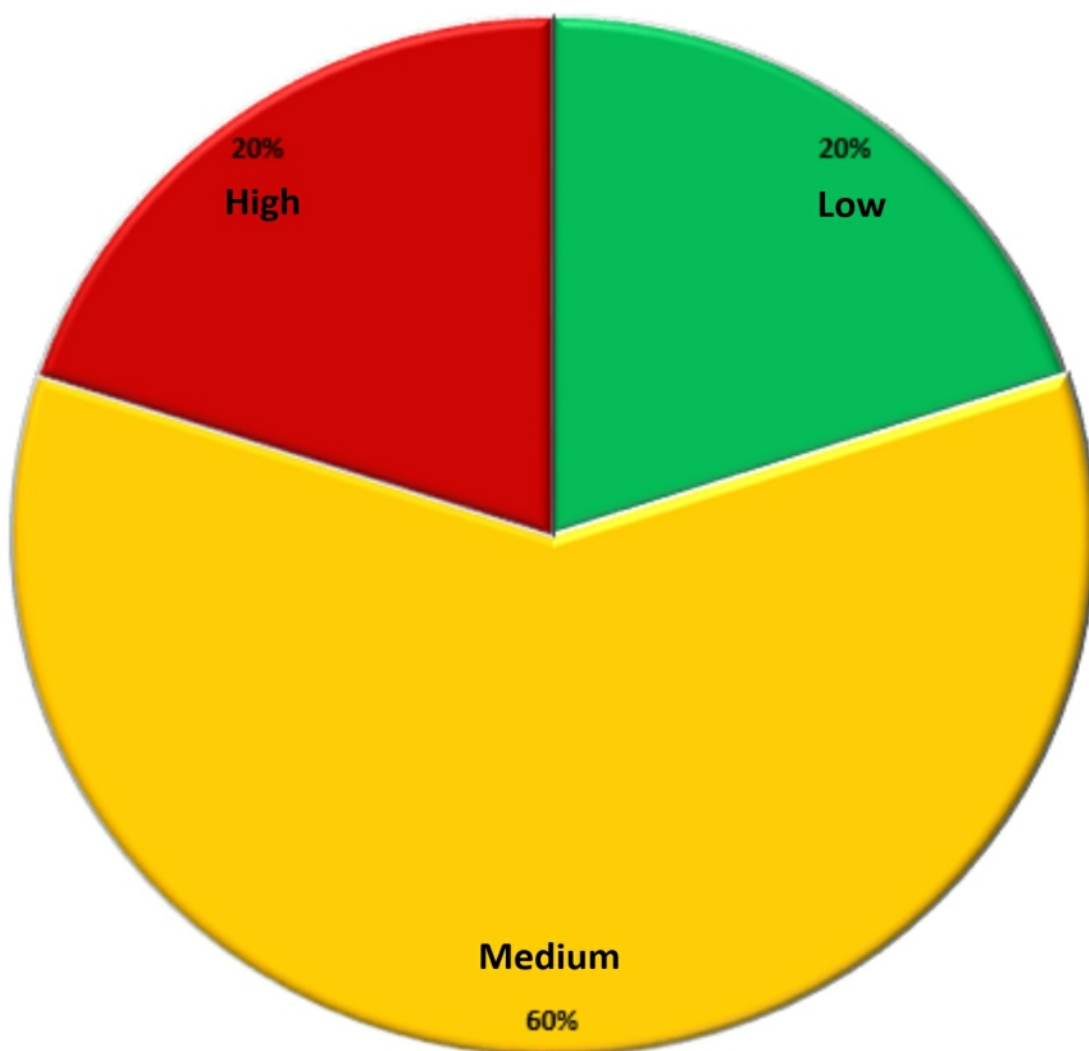
40% of respondents have assets below \$1 billion, and 60% have assets over \$1 billion. Interestingly, when broken down further the two most common segments were banks between \$1 billion - \$10 billion in assets (36%) and \$501 to \$1 billion in assets (28%).





Risk Rating:

The final demographic question we asked our respondents was to describe their institution's overall risk rating. The majority stated that they have a medium risk rating (60%). Interestingly, high and low risk rating each yielded 20% of responses.

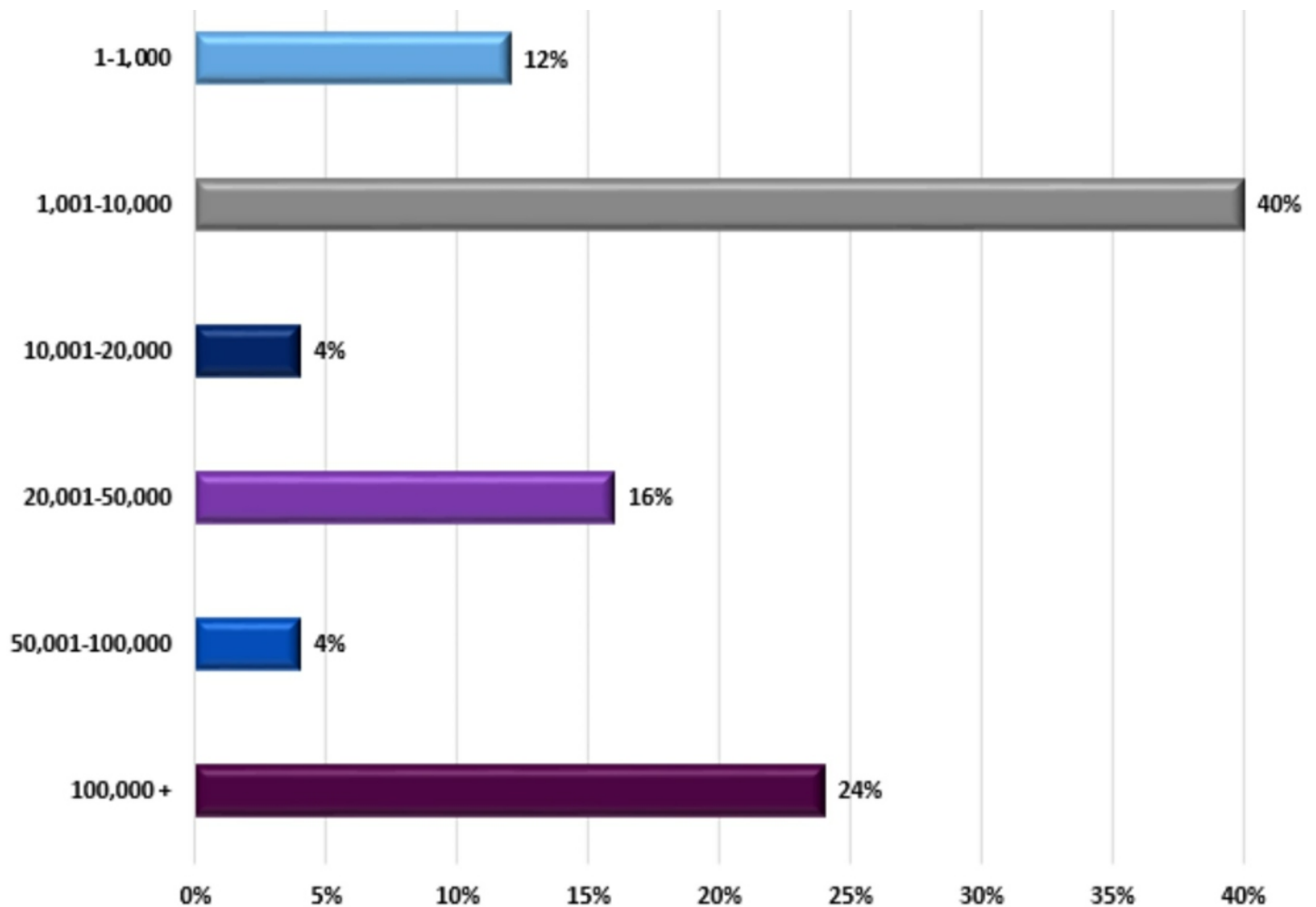




Commercial Customer Risk Rating Questions:

Customer Quantity

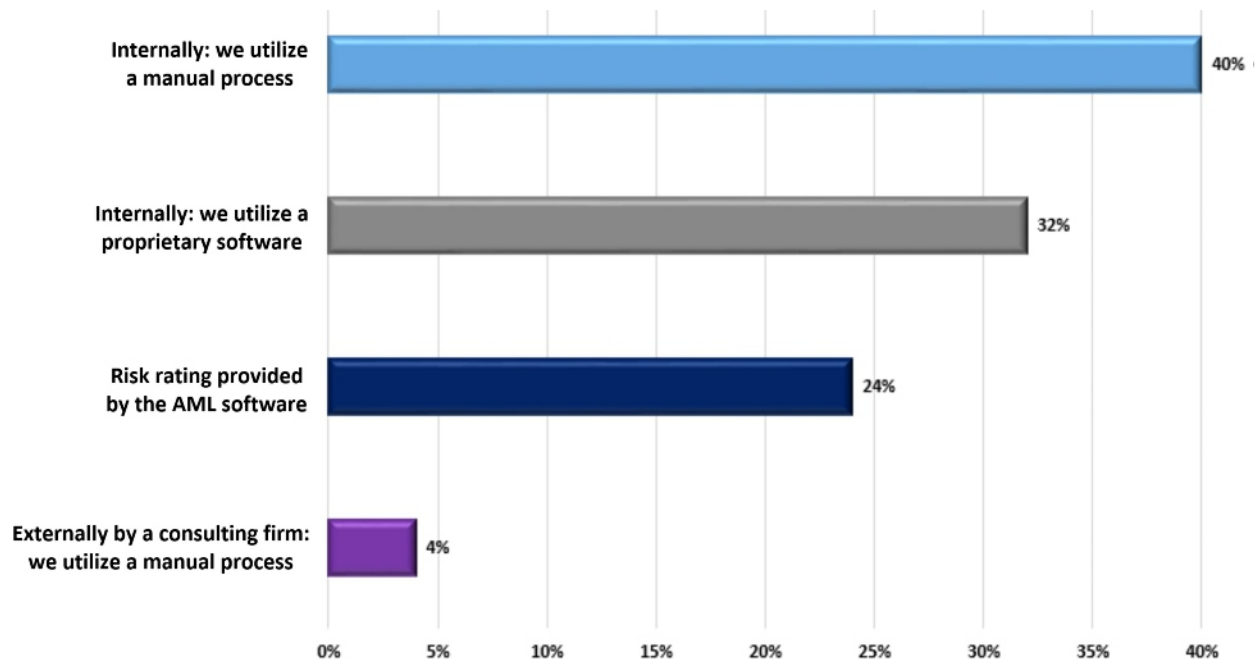
The typical number of customers included in a respondent's risk rating/assessment is 1,001 - 10,000 (40%). Respondents with 100,000+ were close behind with 24%.





Customer Risk Rating Methodology Development

Most respondents developed their customer risk rating methodology internally using a manual process (40%). The second most common method was also internally; though utilizing a proprietary software (32%).



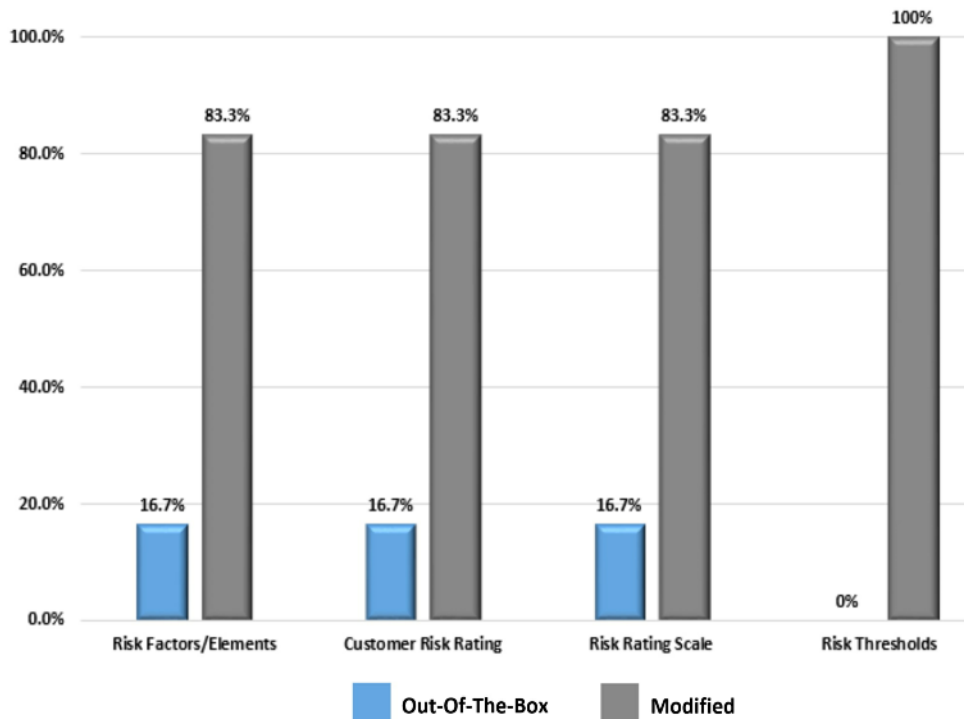
AML Software Configuration Modifications

For respondents who use a vendor supplied software tool, all 100% have modified the configuration.



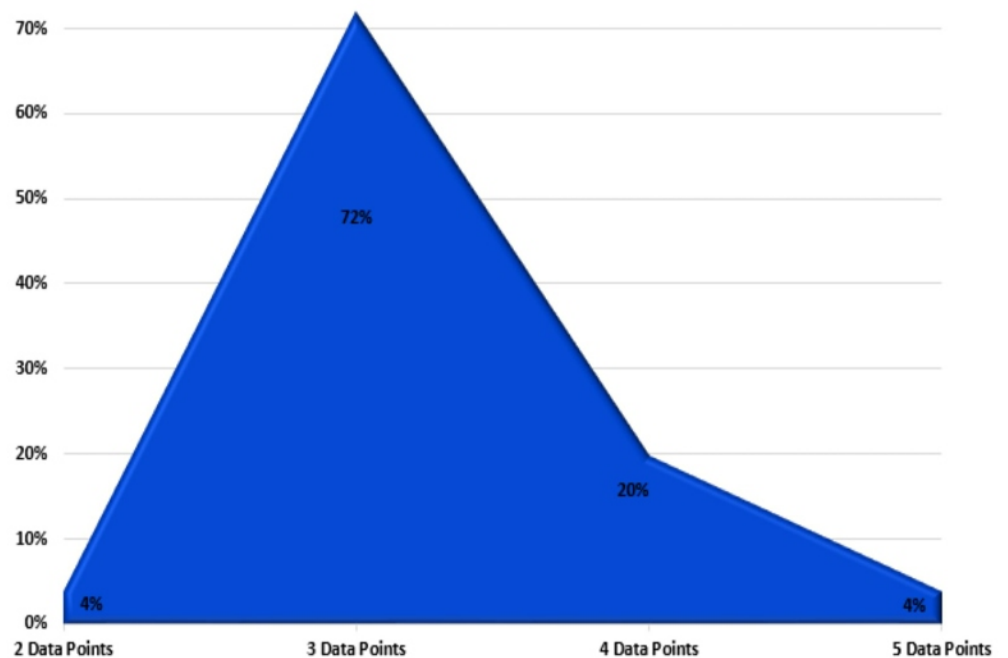
Out of the Box or Modified

100% of respondents modified their risk thresholds, while 83.3% each modified risk factors/elements, customer risk rating and the risk rating scale.



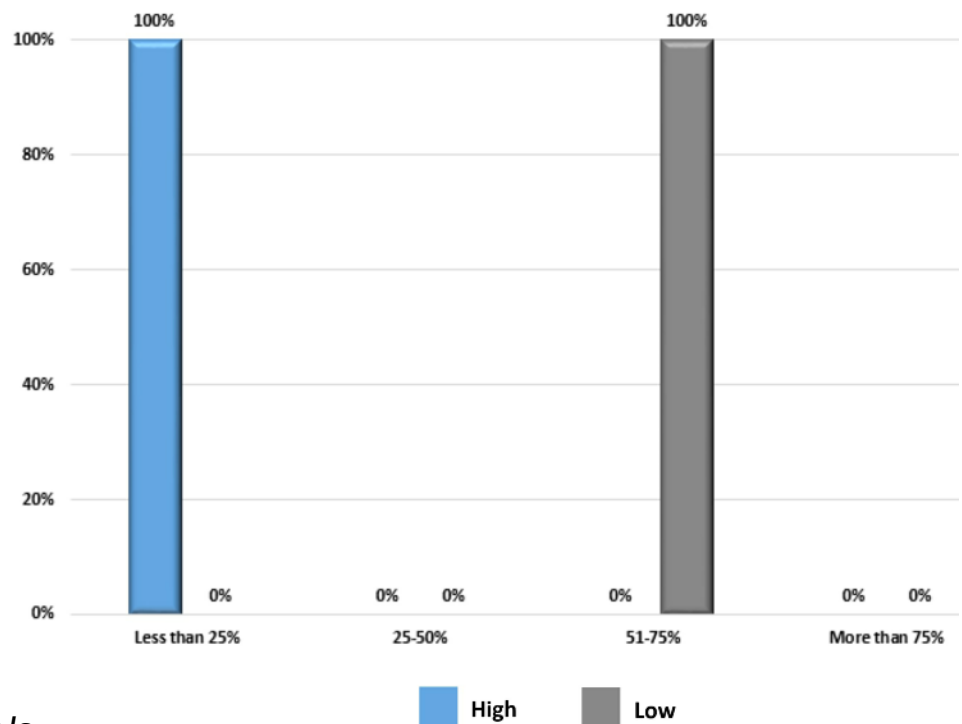
The Number of Risk Levels

The overwhelming majority of respondents use three data points in their customer risk assessments (72%).



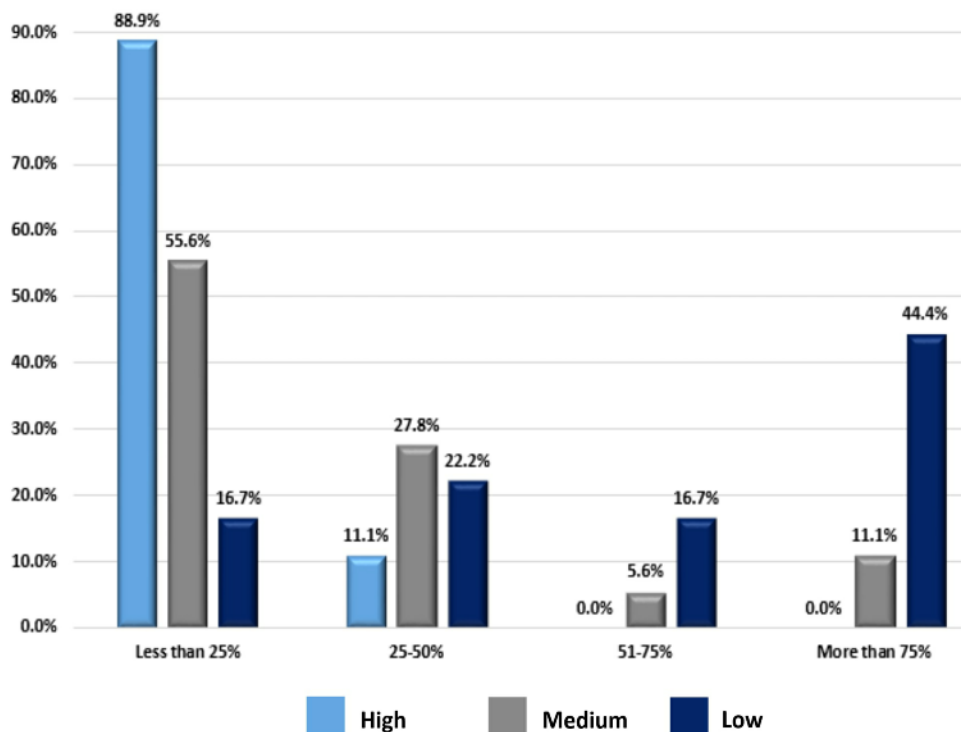
Two Data Point Risk Levels

Of the respondents who utilize two data points to risk rate their customers the majority of all respondents have roughly 75% low risk customers and 25% high risk customers



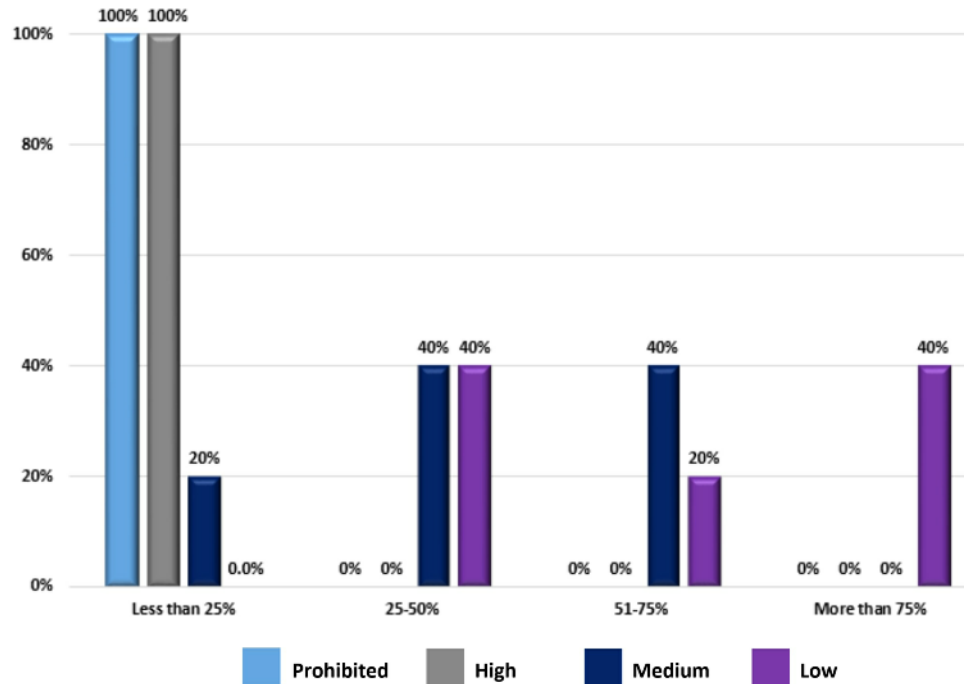
Three Data Point Risk Levels

Of the respondents who utilize three data points to risk rate their customers; the majority have less than 25% high risk customers (88.9%), less than 50% medium risk customers (83.4%), and more than 50% of low risk risk customers (61.1%).



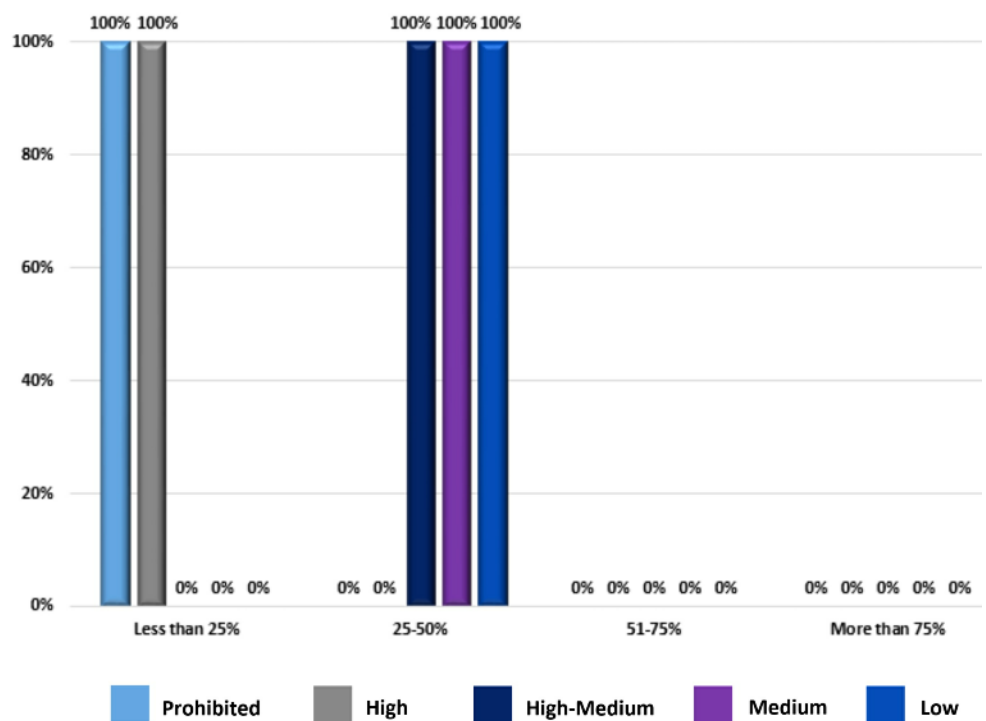
Four Data Point Risk Levels

Of the respondents who utilize four data points to risk rate their customers all respondents have less than 25% prohibited and high risk customers. 80% of respondents have between 25%-75% medium risk customers, and all respondents have between 25%-100% low risk customers.



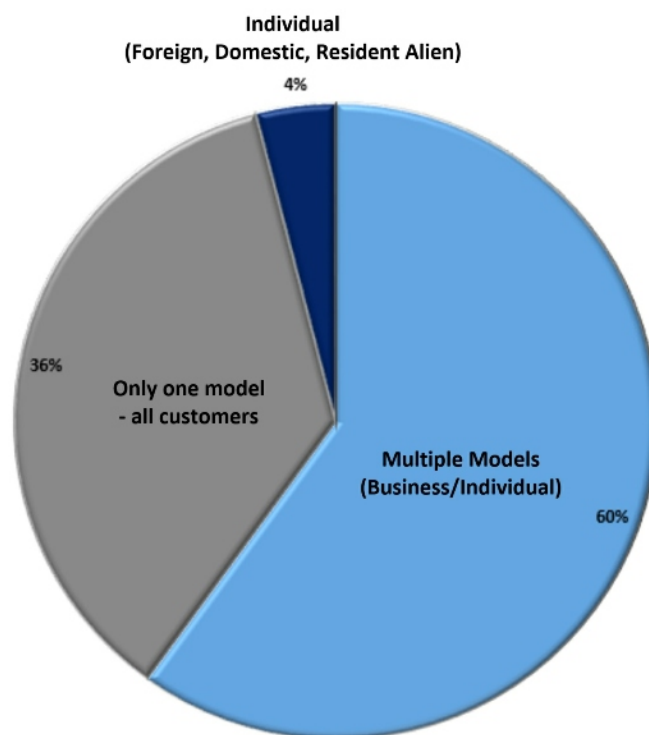
Five Data Point Risk Levels

Of the respondents who utilize five data points to risk rate their customers, their customer mix looks like they have 25% high-medium, medium, and low risk customers each, and less than 25% of prohibited and high risk customers.



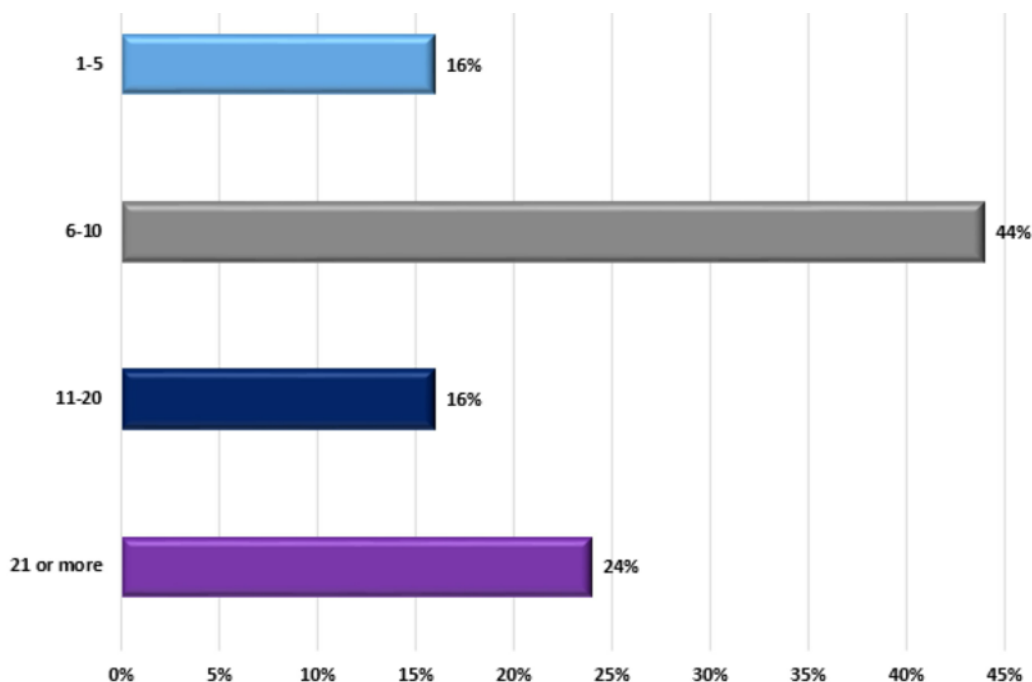
Risk Rating Models

60% of respondents utilize multiple risk rating models for customers, while 36% utilize only one model.



Elements per Model

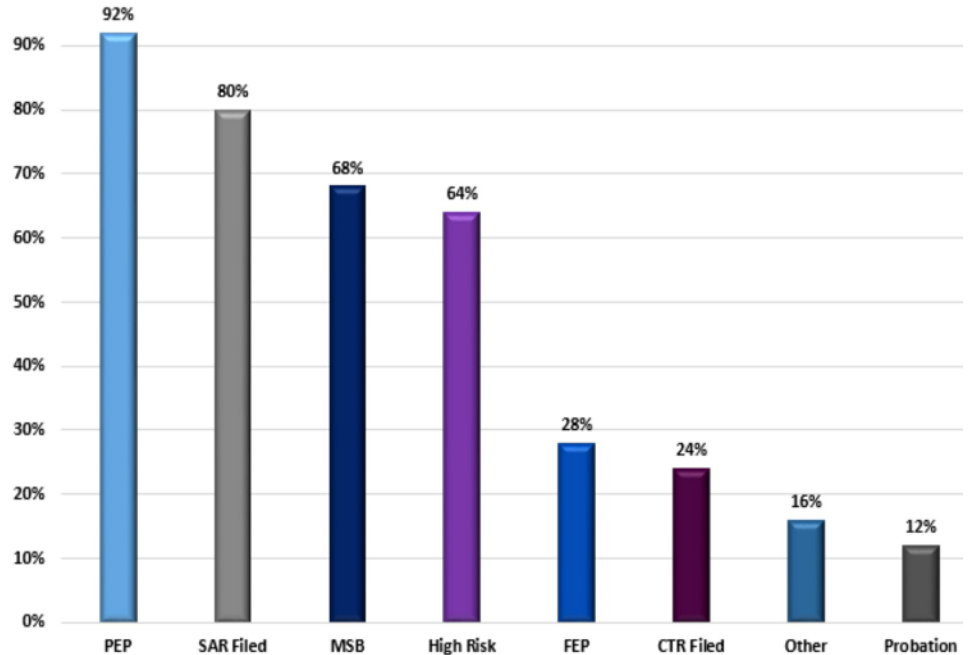
Most respondents (44%) use between 6-10 elements (geographical, customer type, amount of transactions) per model. Another 24% use 21 or more.





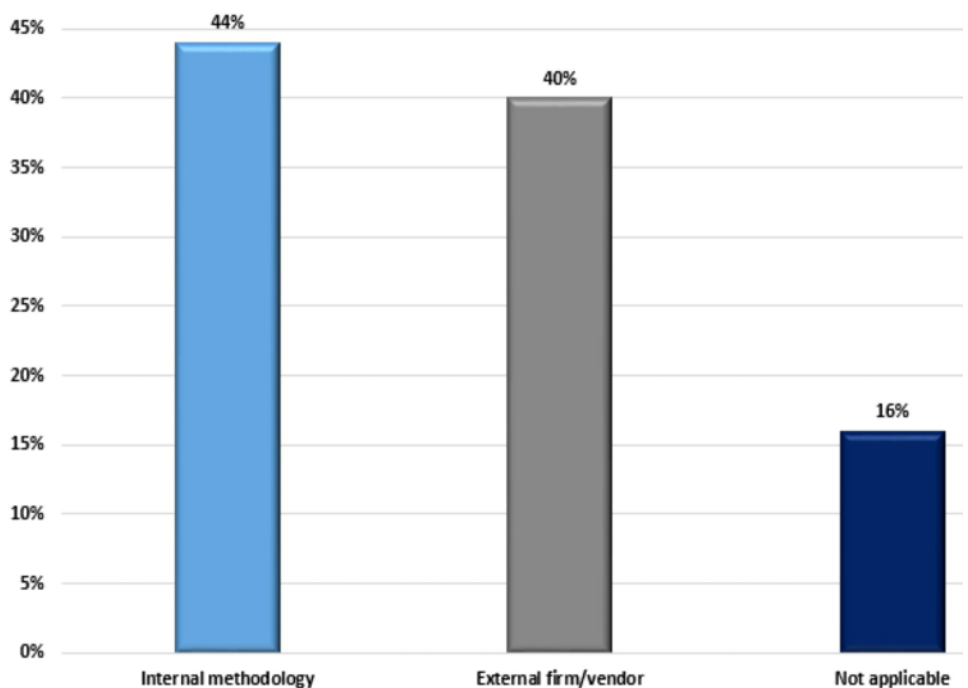
Overriding Dominant Items

92% of respondents believe PEPs to be an overriding dominant factor in their risk rating model, followed a SAR filing (80%).



Country Risk Rating

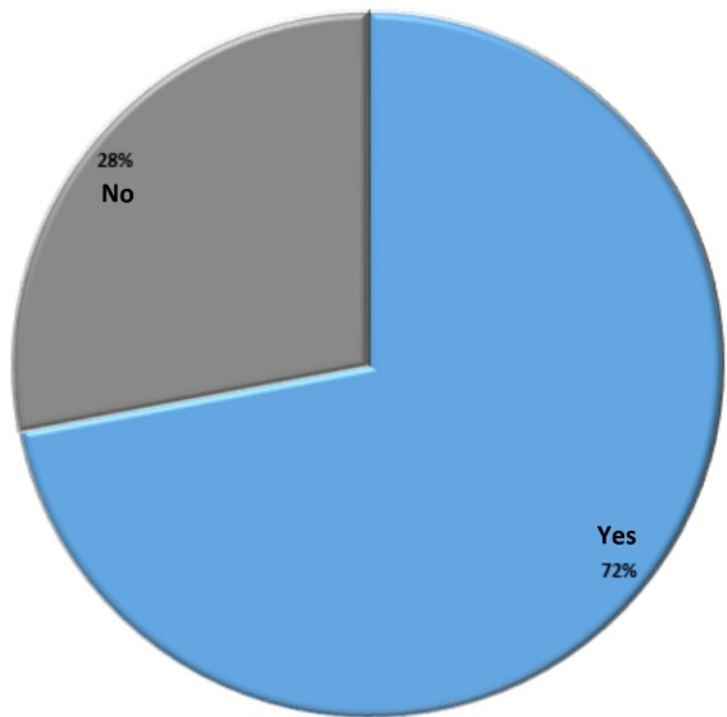
44% of respondents utilize an internal methodology to risk rate countries. Respondents who utilize an external firm/vendor were close behind at 40%.





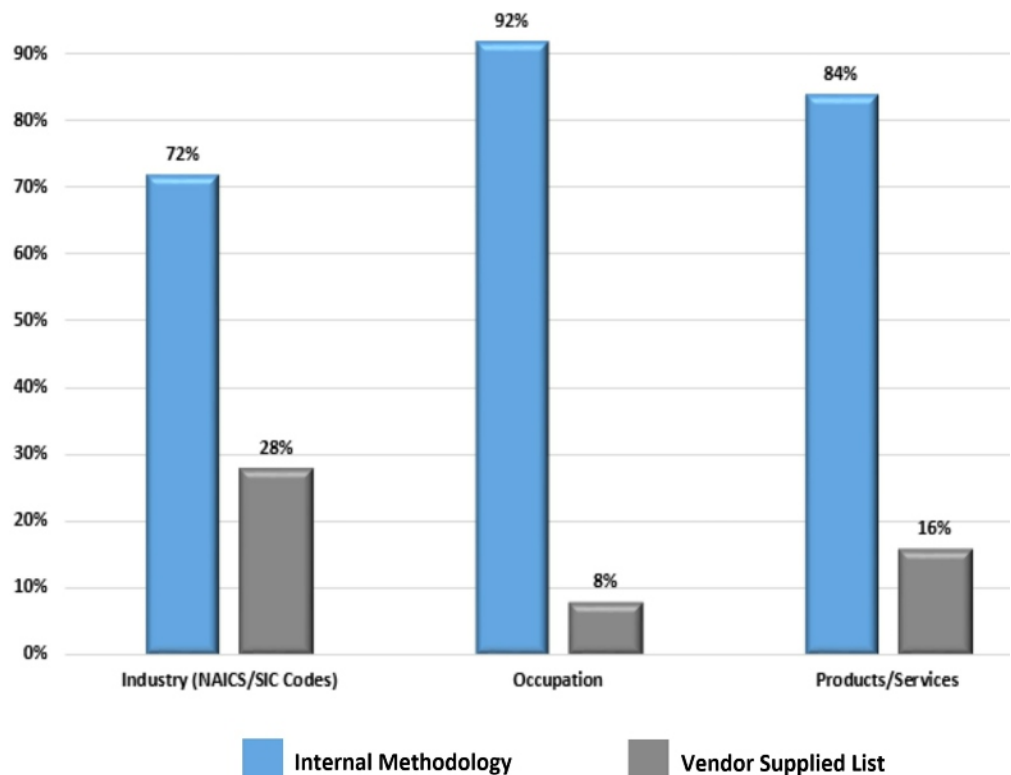
Beneficial Owners

72% of respondents consider the beneficial owners of the business in their risk model, surprisingly 28% do not.



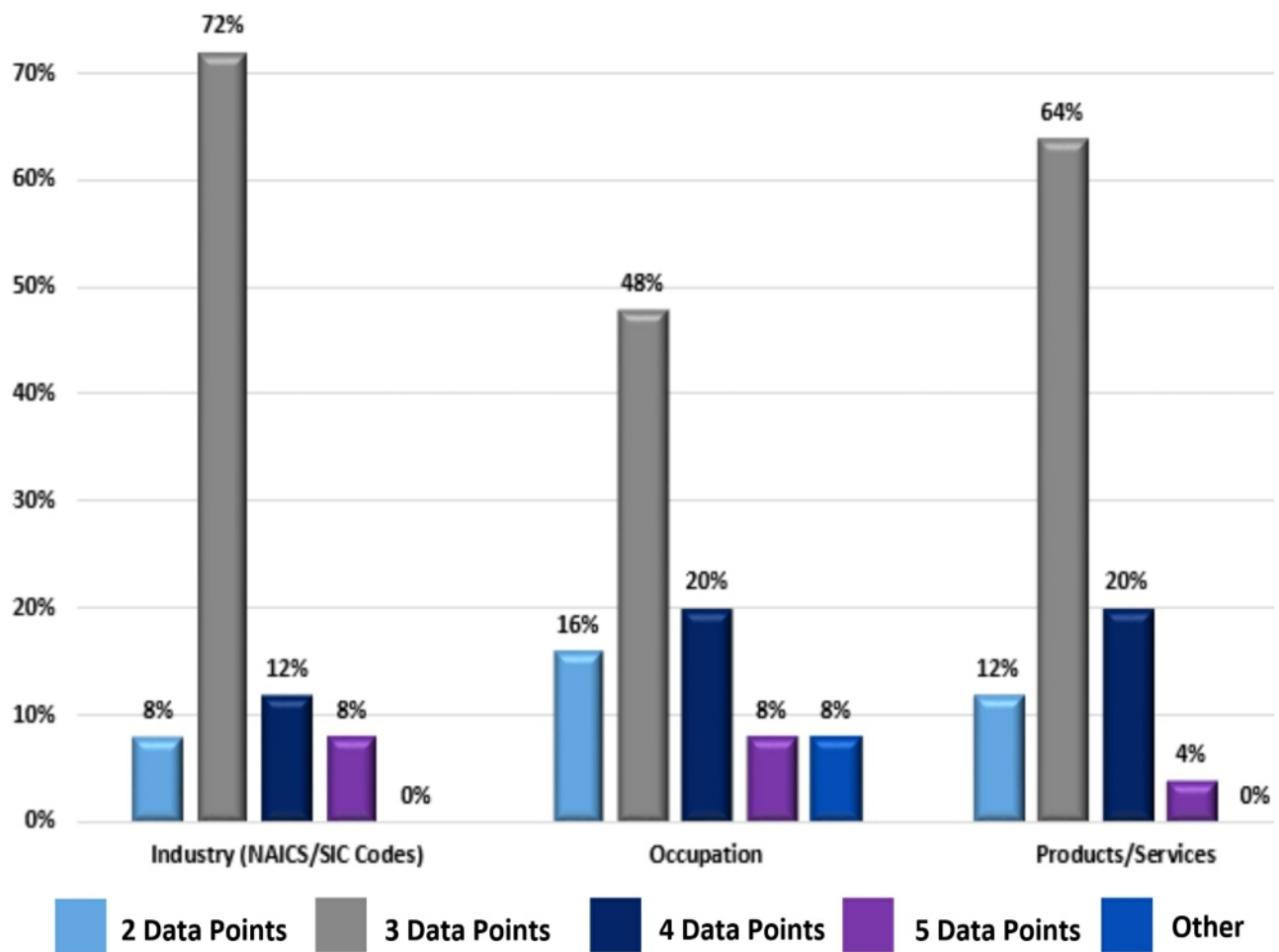
Methodology

The majority of respondents are utilizing an internal methodology for industry, occupation, and products/services (72%, 92%, and 84% respectively).



Scale

The following chart describes how many data points respondents utilize for each of the following categories within their risk model. Respondents were most likely to utilize three data points in each category: 72% for industry, 48% for occupation, and 64% for products/services.



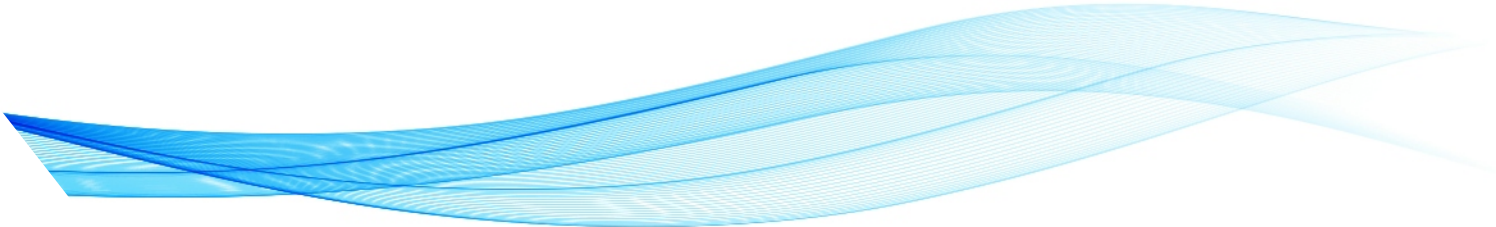
Conclusion:



A customer risk assessment is an important piece of the AML puzzle. Knowing who you're doing business with, as well as their past financial behavior is critical to staying compliant with current regulation. It's also important to be conscious of what best practices are, lest you be caught unaware down the line; thinking you were doing everything correctly.

Overall, our survey participants represent a BSA/AML/OFAC compliance officer at a commercial or retail community bank with over \$1 billion in assets and a medium risk rating. Most of our respondents have about 1,001 - 10,000 customers included in their risk rating/assessment and develop their risk assessment methodology internally through a manual process. The respondents who use a vendor supplied software tool typically modify the configurations rather than using the configurations 'out-of-the-box'. When asked which common components found in AML software they modify, the overwhelming majority said they modified their risk thresholds, followed by their customer risk rating.

Typically respondents utilize three data points within their customer risk assessments, as compared to two, four, or five data points. Regardless of the amount of data points utilized, we confirmed that banks across the board typically maintain a low percentage of prohibited/high risk customers and a higher number of low to medium risk customers. However it was surprising to find that 44.6% of respondents only utilize one model (all customers). We were expecting a much lower percentage with a heavier concentration on multiple models (business/individual) or individual (foreign, domestic, resident alien). there are too many variables involved to properly evaluate a risk rating through only one lens. Within our respondents' models, they typically include about 6-10 elements (geography, occupation, products/services, etc); however, a large percentage also utilize 11-20 elements which again was surprising to us. Too many elements may start to 'confuse' the rating.



Almost all of our respondents had some type of overriding dominant item involved in their risk rating model. The most commonly included item were PEPs, and having a SAR filed was a close second. An MSB (Money Services Business) and being high risk were also common overriding dominant items cited.

When asked how they risk rate countries, 50.8% of respondents utilize an internal methodology versus an external firm or vendor.

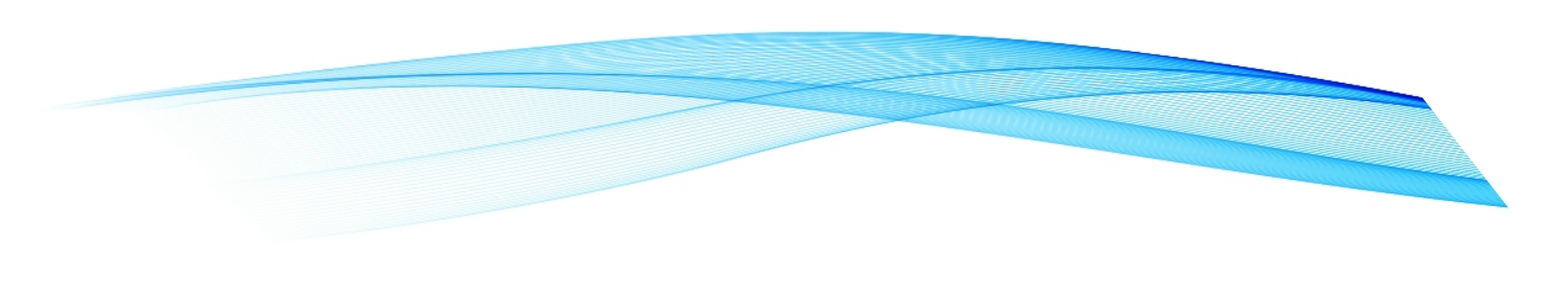
It was interesting to see that 36.9% of our respondents do not consider the beneficial owners of the business in their risk model. Again, we thought that almost all respondents would include some type of consideration in regards to their beneficial owners. However with the new CDD rule on beneficial owners, we expect this to change.

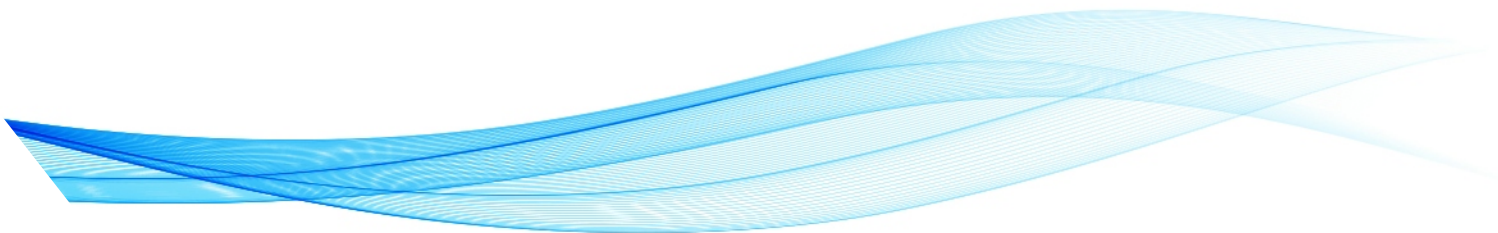
Finally, our respondents typically use an internal methodology when it comes to Industry (NAICS/SIC Codes), Occupation, and Product/Service risk factors. When asked what sized scale they use in regards to these risk factors (Industry [NAICS/SIC Codes], Occupation, Products/Services), most respondents using a scale of three data points.

Some of the responses surprised us and some did not. Regardless, given the new CDD rule regarding beneficial owners, we expect to see this evolve, so it would be interesting to revisit this topic in the future. A more detailed report for retail and commercial banks provides more specific details for those institution types and is available if you visit <http://www.arcriskandcompliance.com/surveys/>

Comparisons:

- Retail banks represented community banks just slightly more than commercial banks (51.5% and 44% respectively).
- The largest group of respondents for both retail and commercial banks were BSA/AML/OFAC compliance officers (45.5% and 44% respectively).

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- When it came to the asset size of the institutions, retail banks had a larger percentage of banks under \$500 million (33.3%) while commercial banks had a larger percentage of \$1 to 10 billion (36%).
 - Both retail banks and commercial banks had almost the exact percentage for medium risk ratings (60.6% and 60% respectively). Interestingly, retail banks had a noticeably higher percentage of low risk ratings compared to commercial banks (30.3% and 20% respectively).
 - Retail banks top response for number of customers included in their risk rating was a tie between 1,001-10,000 and 100,000+ (30.3% each) while commercial banks' top response was singularly 1,001-10,000 (40%).
 - Retail banks were slightly more likely to utilize an internal manual process than commercial banks (45.5% and 40% respectively); though it was still the most common answer for both.
 - For banks who use a vendor supplied software tool, the majority of retail bank respondents and all commercial banks (77.8% and 100% respectively) modified their software's configurations.
 - For both retail and commercial banks risk thresholds were the most likely component to be modified; however, commercial banks were more likely to modify this component (100% and 85.7% respectively).
 - Commercial banks were more likely to utilize three data points in their customer risk rating than retail banks (72% and 63.6% respectively); though three data points was still the most common answer for both.
 - Of the banks that utilize two data points, commercial banks were clearly divided between high risk customers at less than 25% and low risk customers at 50%-75%; however, retail banks had a greater combination of response.
 - Of the banks that utilize three data points, many of the responses were similar among both commercial and retail banks, except that retail banks had a heavier concentration of medium to high risk customers.



- Of the banks that utilize four data points, there was a heavier concentration of medium to low risk customers for commercial banks compared to retail banks.
- Of the banks that utilize five data points, retail banks were less likely to have prohibited, high, or high-medium risk customers at more than 25% than commercial banks.
- Commercial banks were slightly more likely to utilize multiple risk rating models compared to retail banks (60% and 57.6% respectively).
- Retail banks top response for the amount of elements per model was a tie between 6-10 and 11-20 (33.3% each) while commercial banks' top response was singularly 6-10 (44%).
- Retail banks top response for overriding dominant items was a tie between PEPs and a SAR filing (33.3% each) while commercial banks' top response was singularly PEPs (92%).
- The majority of both retail and commercial banks utilize an internal methodology to risk rate countries (54.5% and 44% respectively).
- Retail banks were more likely to not consider the beneficial owners of the business (51.5%) in their risk model, while commercial banks were (72%).
- Retail banks were more likely to utilize an internal methodology for product/service factors (84.8%) while commercial banks were more likely to use an internal methodology for occupation factors (92%).
- Both retail and commercial banks are most likely to utilize a three data point scale for each of the categories listed, however retail banks had a tie of 57.6% for the most common category (industry and occupation) while commercial banks' most common category was industry (72%).

About AML-ology

AML-ology is the study of AML (anti-money laundering) trends and solutions by providing newsletters and survey reports to AML dedicated professionals. A monthly newsletter is sent with a scientific or academic approach to an AML hot topic. A survey is conducted each quarter based on the hot topics being discussed by the AML community. To sign up to receive the AML-ology newsletter or survey, please visit [here](#).

We provide this report as a value-add to the compliance community to better the anti-money laundering community as a whole. Thank you to everyone who participated. We hope you will participate in future surveys as well.

About ARC Risk and Compliance

ARC Risk and Compliance (www.arcriskandcompliance.com) is a consulting company that specializes in anti-money laundering (AML) compliance and the technology that supports your AML compliance program. For us, this specialization includes BSA, OFAC, KYC/CDD and FinCEN 314(a). We are “The AML Specialists”.

We can bridge the communication gap between what compliance needs and IT can support with the system they have. We believe that in order to bridge the gap between compliance and IT, the expert needs to be able to communicate to both departments, have knowledge and experience in both, and provide experienced solutions. We’ve been able to combine that knowledge and experience for a more thorough solution addressing both the compliance and IT requirements. Nearly all of our services have an element of technology and compliance so our approach reassures a better rate of success.

Many of ARC Risk and Compliance’s team helped pioneer AML technology in the industry. They were leaders in designing, developing and deploying the leading AML software vendors of today. In addition, our team has a strong compliance background that can assist banks with their regulatory challenges and other compliance matters.

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“The AML Specialists”