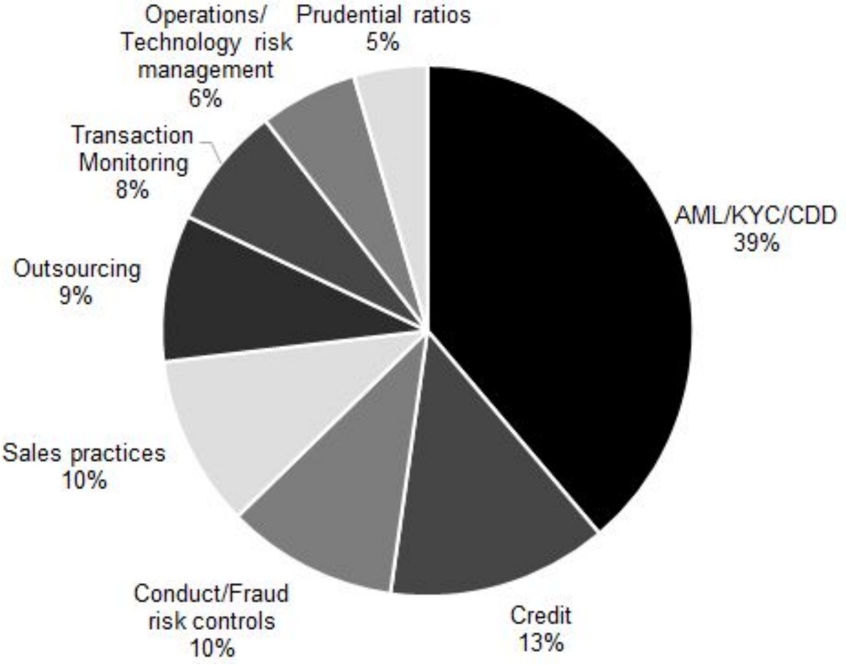
Private Banking - Building tomorrow's resiliency, Today

May 2020

It is often said that the wise learn from the experiences of others. With this philosophy in mind, we have summarised the various operational and regulatory compliance matters that came up from our audit of private banks in 2019.

Top five areas

- **AML/KYC/CDD**
- **Credit**
- **Conduct/ Fraud risk Controls**
- **Sales practices**
- **Outsourcing**



Unsurprisingly, AML/KYC remains an area many banks are still grappling with given the continuous scrutiny and heightened expectations of the Monetary Authority of Singapore ("MAS") over the years. That said, there appears to be general maturity in this space and most Financial Institutions ("FIs") are certainly in a better position compared to say 3-4 years ago. Credit risk management is a perennial issue that surfaces every year, in terms of identification and escalation of deteriorating credits. As for outsourcing, given the guidelines have been issued some time ago, it was surprising as we continue to observe a number of findings in this area.

In terms of emerging risk, conduct risk is definitely on the radar of MAS at the moment. Our observations suggest differing sales practices and varying degree of control and governance mechanisms across the industry. We have also noticed increased errors in prudential ratios computation (MLA/AMR etc) across a number of PBs in our portfolio.

Focus areas

We summarised the common areas of findings and recommendations which we had noted:

AML/KYC/ CDD

- Onboarding questionnaires on VC/ investment knowledge not accurately updated on Avaloq.
- Verification documents not obtained timely.
- Scores on investment questionnaires were not reflected on the customers' risk profiles.
- Customers on-boarded with SoW deficiency were not rated high risk.
- Incomplete definition of VC.
- Incomplete/inaccurate name screenings/disposals.
- Lack of monitoring to identify excess AUM/ expired document.

Transactions Monitoring

- Alerts clearance were overdue.
- Accounts not blocked for unresolved alerts.
- Guidelines/thresholds/scenarios not updated.
- Lack of proper documentation for clearance.

Regulatory Reporting

- Inaccuracies in calculation of ratios.
- Incompliance with regulatory requirements on definitions/computation of eligible assets and liabilities.

Investment Suitability

- **Pre-trade mismatches-** Lack of checks to identify pre-trades mismatches and ensure they are communicated and documented.
- **Governance**- Lack of management's attention and emphasis on pricing issues; no procedures in place for exceptional pricing to be subjected to approval / review.
- **Post-trade surveillance** - Inappropriate/non-tagging of solicited/unsolicited transactions. Where transaction is client-initiated, the Bank should inform client that the products are not on approved list/ inconsistent with house view.

Conduct

- **Gifts, Entertainment and Benefits** – Lack of appropriate records/ periodic reviews of the records.
- **Mandatory Leave** – Lack of monitoring framework
- **Authentication of customer instructions** – independent call-back not performed for change of static data/ out-going fund transfer.

Focus areas

Regulatory Compliance
- AML/KYC/CDD
- Transactions Monitoring
- Regulatory Reporting

Market Conduct
- Investment suitability
- Conduct
- Fraud risks Controls

Operational Risk
- Outsourcing
- Operational lapses
- Technology risk management

Credit Risk Management
- Credit Risk Monitoring
- Credit provisioning

Outsourcing

- Central record of all outsourcing arrangements was inaccurate.
- Periodic reviews on material outsourcing arrangements not performed on an annual basis.
- Assessments of required frequency and scope of independent audits and/or expert assessments according to the nature and extent of risk and impact to institution from outsourcing arrangements are not performed.
- Lack of metrics used to evaluate the performance and security of the service provider.
- Definition of 'material outsourcing' is not in accordance with the MAS Outsourcing Guidelines.

Others

- Technology Risk Assessment - Lack of framework and policies and procedures around MAS Notice 644.
- Makers and checkers controls are not properly evidenced.
- Documentation with respect to methodology, basis and assessment performed in deriving the threshold set for outgoing funds transfer grid.

Credit Risk

- Annual credit review not performed on a timely basis.
- Extension for approval of credit review renewal not obtained on a timely basis.
- Credit facilities granted are not approved by personnel with the right authority.
- Lapses on the oversight over the monitoring of credit violations.
- Approval for credit limit excess is not obtained and remedial action taken timely.
- Internal ratings mapping is not in line with the MAS Notice 612 credit grading.
- Accounting system is not set up appropriately for the ECL computation of stage 3 loans.

Emerging risks

The COVID-19 outbreak has developed rapidly in 2020 with far-reaching implications. Across the globe, unprecedented measures taken to contain the virus, including mass quarantines, social distancing, border closures and shut-downs of non-essential services, have significantly curtailed economic activities. With new ways of working, it also introduces new risks to banks.

Regulatory Compliance

1. Potential heightened risk in financial crimes – inability to identify STRs.
2. Social distancing – Inability to authenticate/verify documentation via non-face-to face measures.
3. Inability to meet regulatory reporting requirements.

Market Conduct

1. Untimely escalation/detection of issues by management
2. Market volatility/ surge in client trading – increase in pricing issues and trade mismatches.
3. Lack of a robust monitoring framework on remote working, higher propensity for fraud/conduct issues.

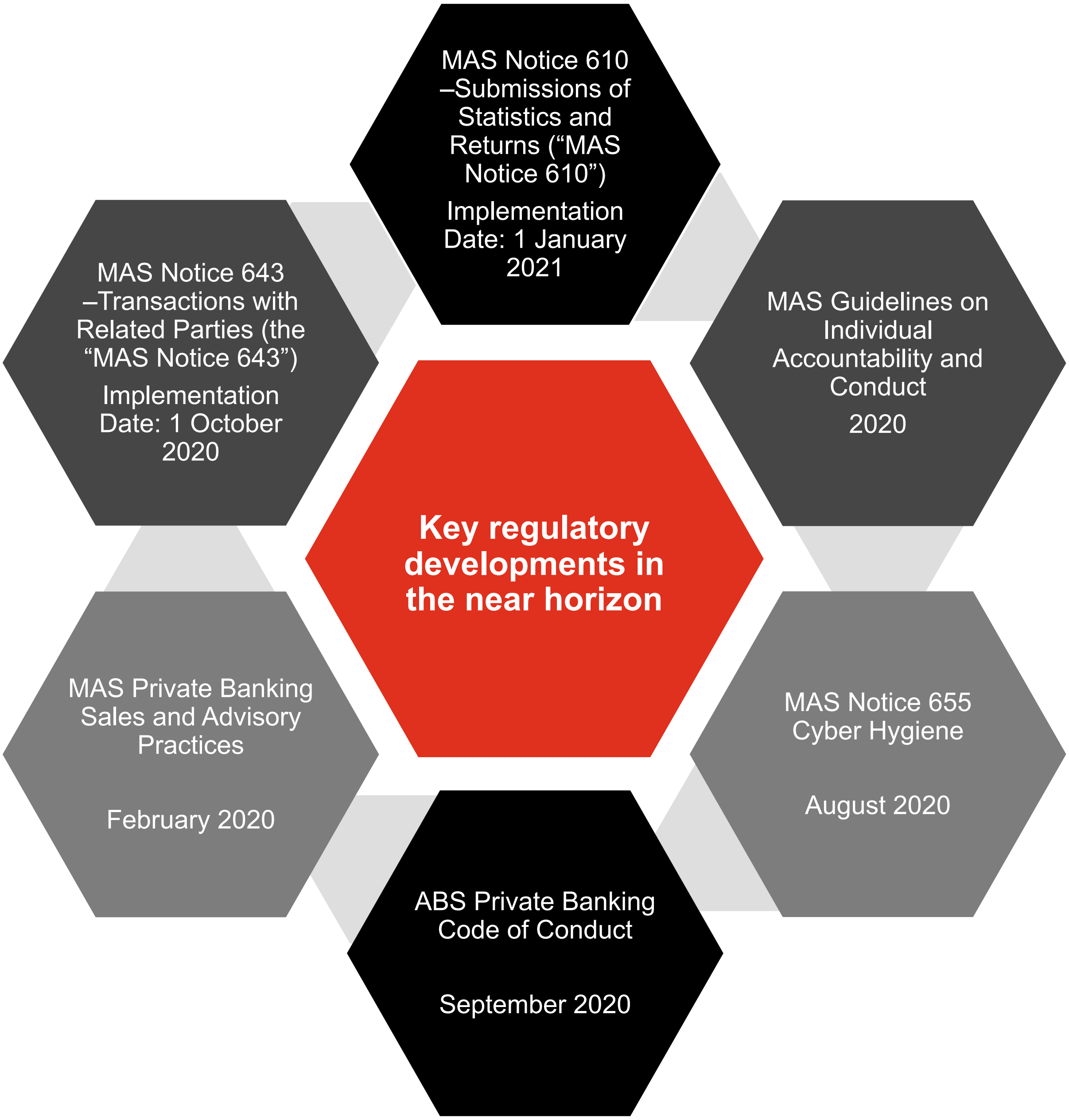
Operational Risk

1. Inability of the material outsourced service providers (including Head Office) to deliver.
2. Gaps in BCP measures resulting in operational lapses.
3. Technology challenges in ensuring data & cyber security.

Credit Risk Management

1. Credit deterioration may not be picked up on a timely basis.
2. Inability to obtain updated credit information from customers
3. Inaccuracy in expected credit loss computation.

Staying ahead



Plan your responses to these emerging risks and key regulatory developments now. Have you:

- assigned responsibility to work on critical focus areas and establish procedures to be communicated with stakeholders;
- strengthened your remote monitoring framework;
- established non face-to-face service protocols for Relationship Managers;
- set up a multi-functions task force to detect and prevent internal and external fraud, etc?

Even as the world slowly recovers from the aftermath of the COVID-19 pandemic, nobody quite knows what the new normal will be. One thing is for sure - it's never too early for organisations to scale up in preparation for the eventual upturn.

Start building resiliency today, for the opportunities of tomorrow.

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