BANKING & FINANCIAL SERVICES | BPO

A Quick Guide to Dynamic Risk Management and Monitoring

Financial institutions often bear the brunt of financial crimes, racking up hundreds of millions of dollars in fraud-related losses every year. Online fraud is one of the most difficult problems to predict and control, and this has become even more difficult during the pandemic. As trillions of dollars pass through global financial networks, industry leaders are looking for more efficient and effective ways to mitigate the risks of regular exposure to money laundering attempts.

Complicating these risk remediation efforts are the webs of networks that entities or parties engaged in financial crimes often create, which increases the reach of such crimes. COVID-19 has also disrupted compliance controls and processes, opening up banks and financial institutions to significant compliance risks. Given these risks, banks need a better approach to customer due diligence (CDD). When checking a customer's information, for example, you now need more frequent and efficient methods of regulatory risk management.

One option, dynamic risk management and monitoring, tracks chains of customer affiliations to help mitigate risk. In a dynamic risk model, you can gather information about your customers to form a sufficient understanding of the nature and purpose of each customer relationship, not only when opening an account but throughout your entire relationship with a customer, with active and passive transactions.

In this guide, you'll learn how to strengthen your CDD process with dynamic risk management and monitoring.

The problem with traditional risk management

Financial institutions face different types of risks, such as business/strategic, market, credit, liquidity, operational, legal, reputational and compliance. Using effective policies, processes and procedures provides you with a critical framework to comply with regulatory requirements, including monitoring and reporting any suspicious activities, to safeguard the organization.

Traditional risk management practices focus solely on regulatory compliance, rather than continuously assessing customer risk holistically. They also tend to be siloed, with no attempt made to reassess as and when better data becomes available. Dynamic risk management offers many benefits over traditional risk management.

Benefits of dynamic risk		
Features	Dynamic risk	Traditional risk
Customers are reviewed based on relative risk score	✓	–
The risk code reflects current estimated risk	✓	–
It can be used to upgrade or downgrade risk regularly	✓	–
It learns from historical patterns of risk changes	✓	–
It leads to a focused view of risk of the customers	✓	–
The cost of review is proportionate to the risk	✓	–
It is compliance-based approach	✓	✓
It is dynamic-based risk approach	✓	–

Being able to trace all current customer transactions and predict any likely future transactions is the objective of an effective dynamic risk management approach.

This strategy allows you to foresee monetary transactions, customer contacts and chains of customer affiliations, as well as investigate anything suspicious. To comply with regulatory requirements, you need to be able to develop and implement appropriate risk-based procedures for continuous dynamic risk management.

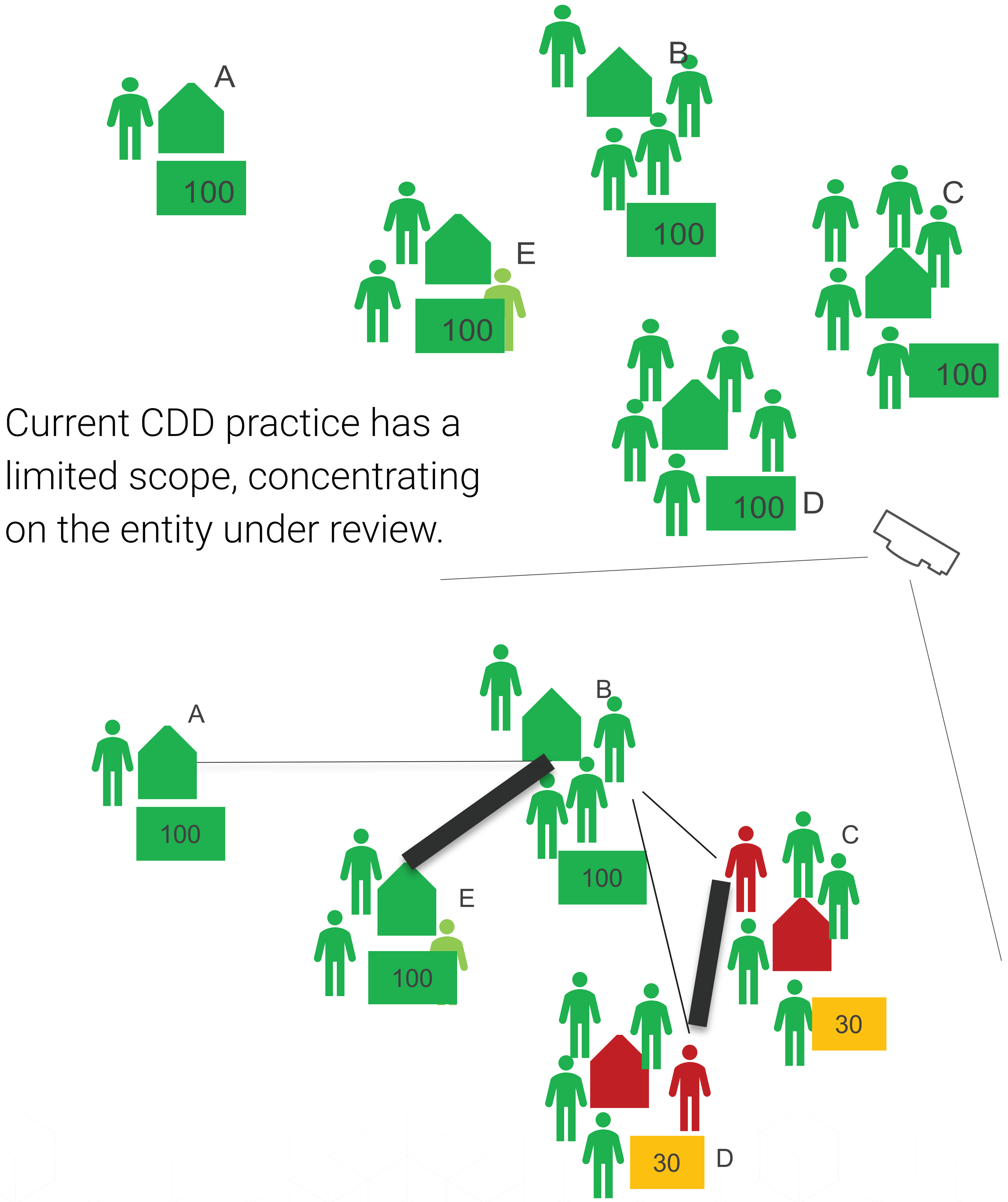
To do this you should:

1. Establish risk-based procedures to develop a **customer risk profile**
2. Obtain and analyze sufficient **customer information** to create each customer's risk profile
3. Conduct **ongoing monitoring** to identify and update customer information on beneficial owner(s) of legal entity customers
4. Maintain and regularly **update** customer information on risk basis
5. Match customer data with the bank's **anti-money laundering risk profile** and increase the focus on higher risk customers
6. **Review** and update changes to a customer's risk profile
7. Provide **standards** for conducting and documenting analysis associated with the risk management process, including guidance for resolving issues when insufficient or inaccurate information is obtained

Changes in risk management practices

Dynamic risk management and monitoring is a radical shift in risk management practices. It identifies hidden patterns and links between customers, and then evaluates risks from connected parties. This approach constantly reassesses the risk individuals and groups pose based on new information.

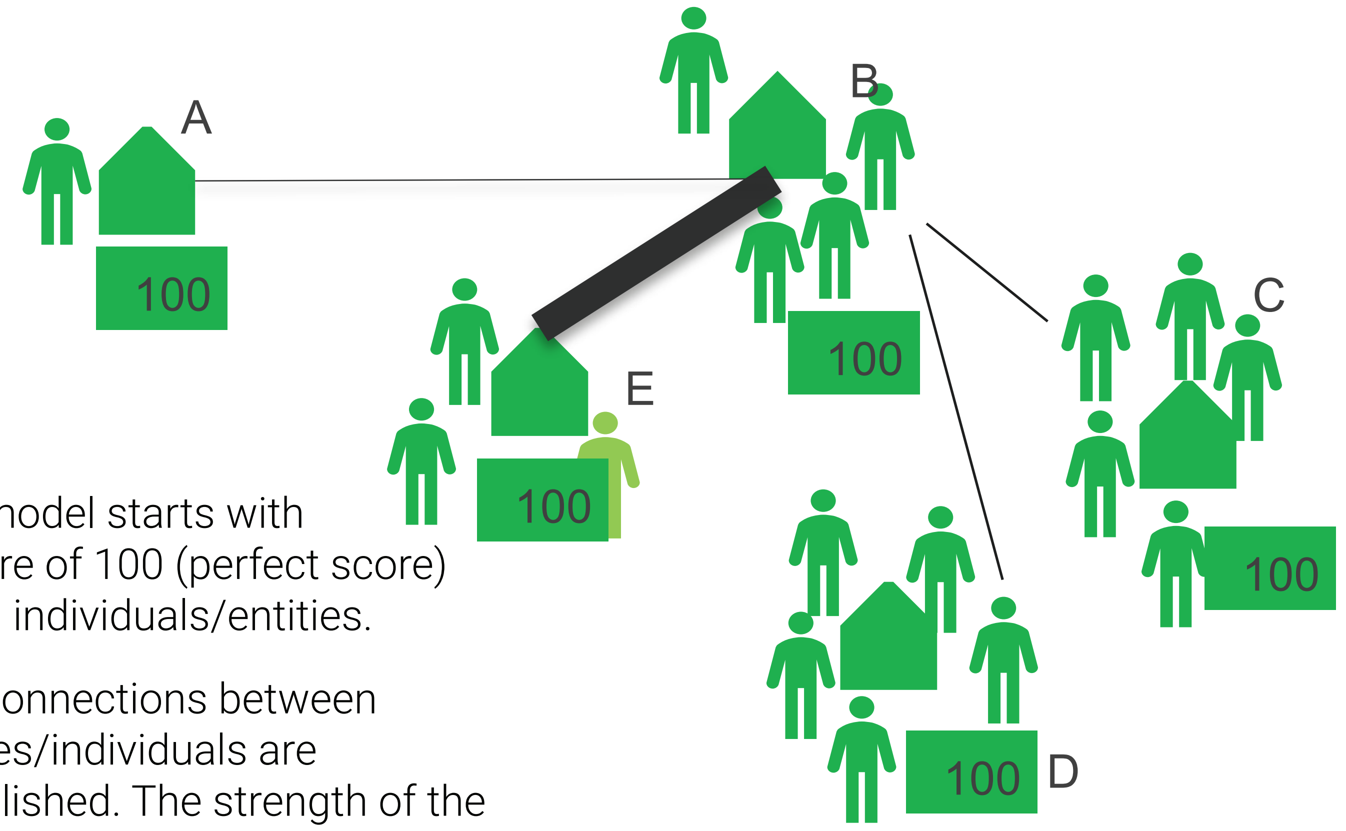
The data sources for network modeling are key personnel changes, suspicious activity and politically exposed person reports, sanction alerts, networked entities or suppliers, related individuals' employment and all transactions. Data gathered from all structured and unstructured sources is used to develop the deep learning-based network risk propagation model and build a unique risk scoring methodology.



Dynamic risk management and monitoring takes a holistic view, transferring risk/goodwill from related entities. It's a continuous process.

Deep learning-based network risk propagation model

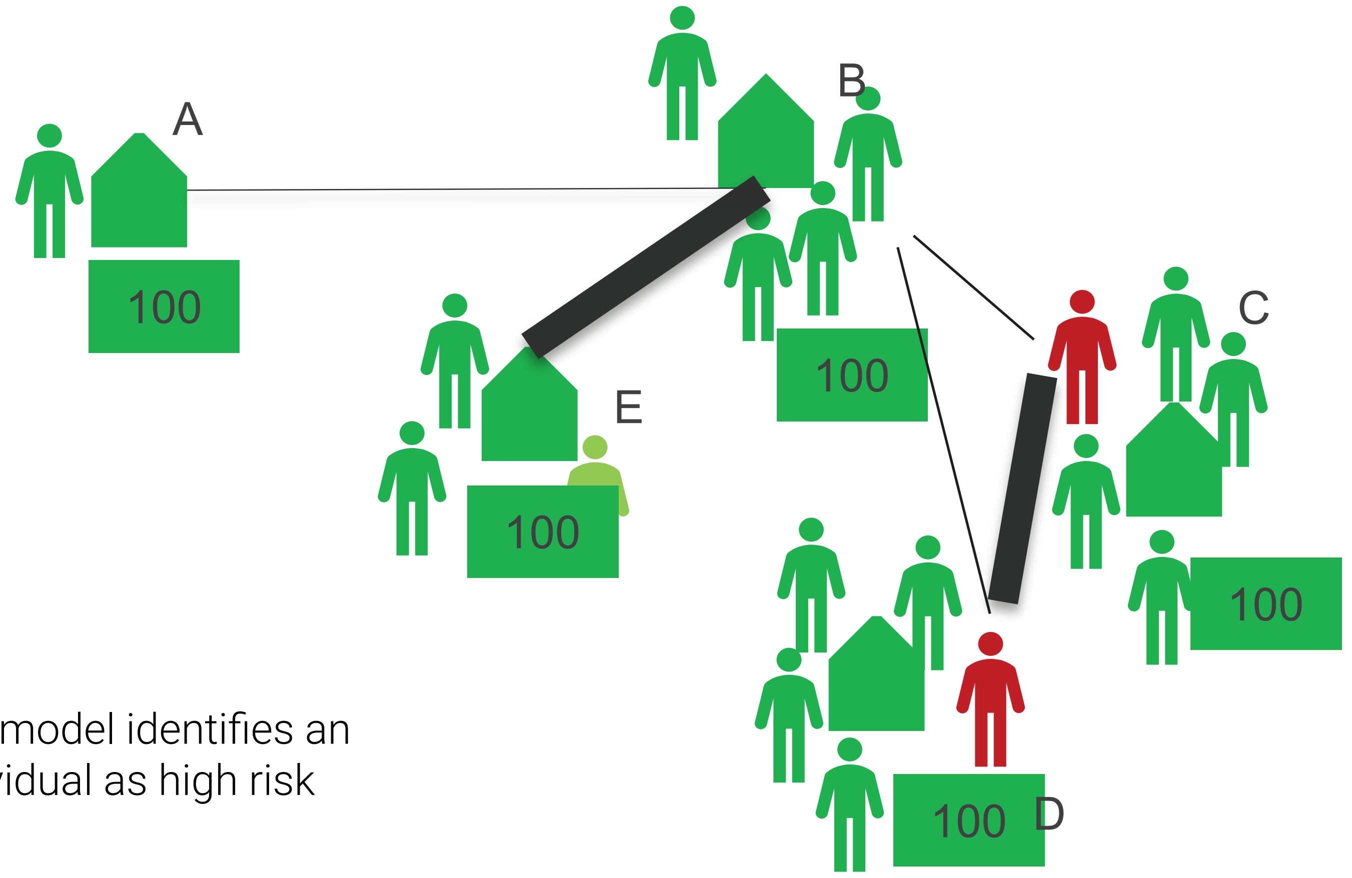
1.



The model starts with a score of 100 (perfect score) for all individuals/entities.

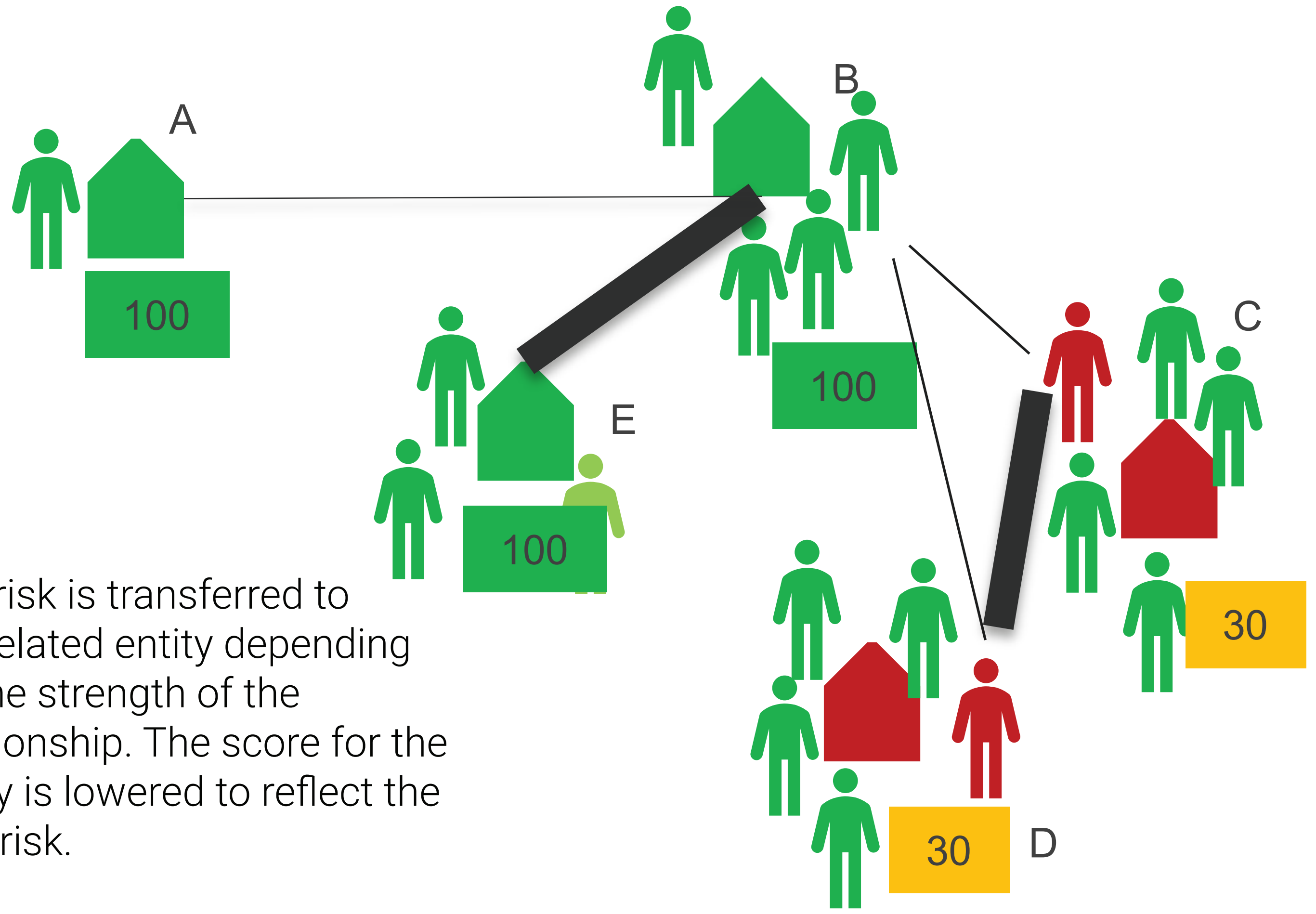
The connections between entities/individuals are established. The strength of the relationship is identified.

2.



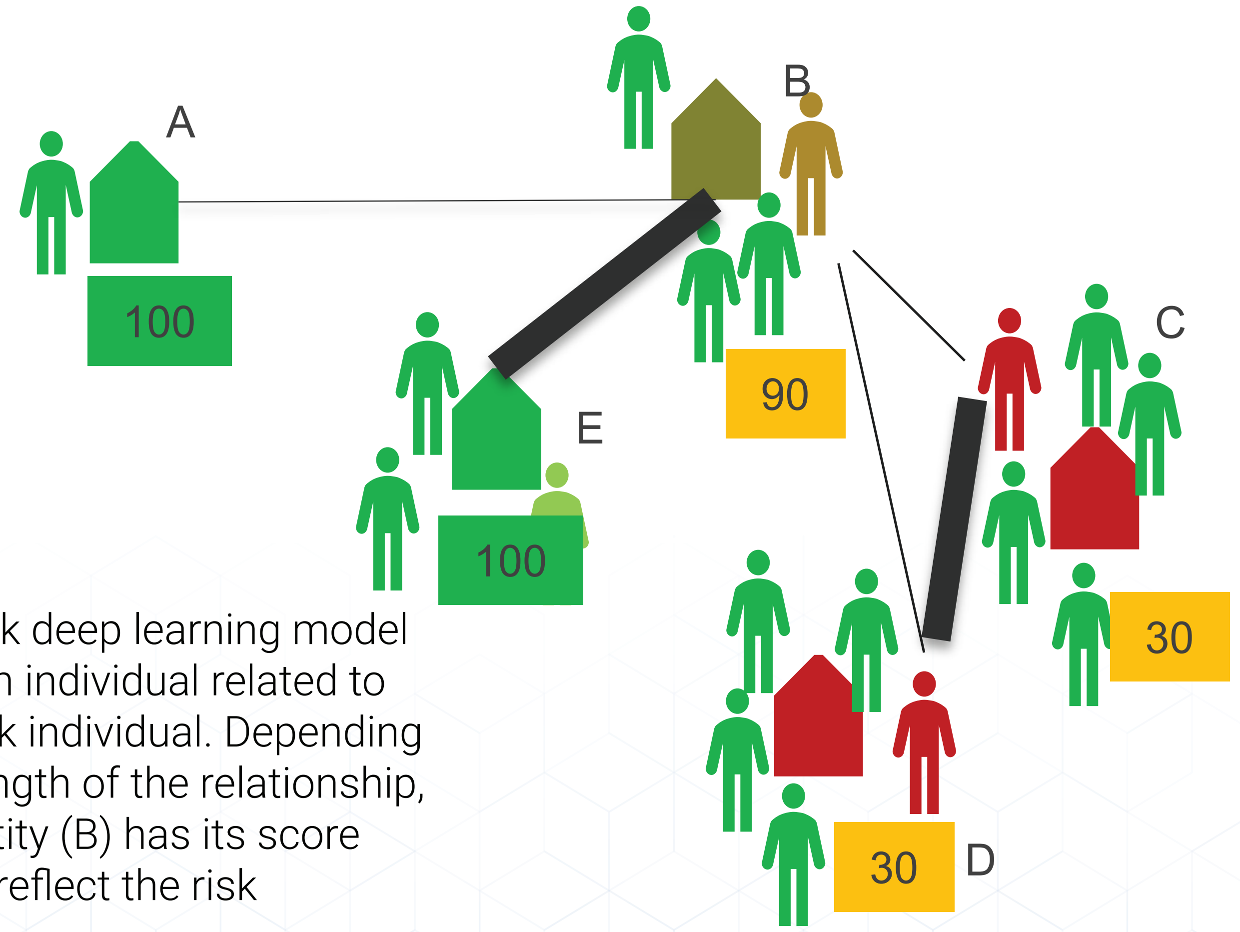
The model identifies an individual as high risk

3.



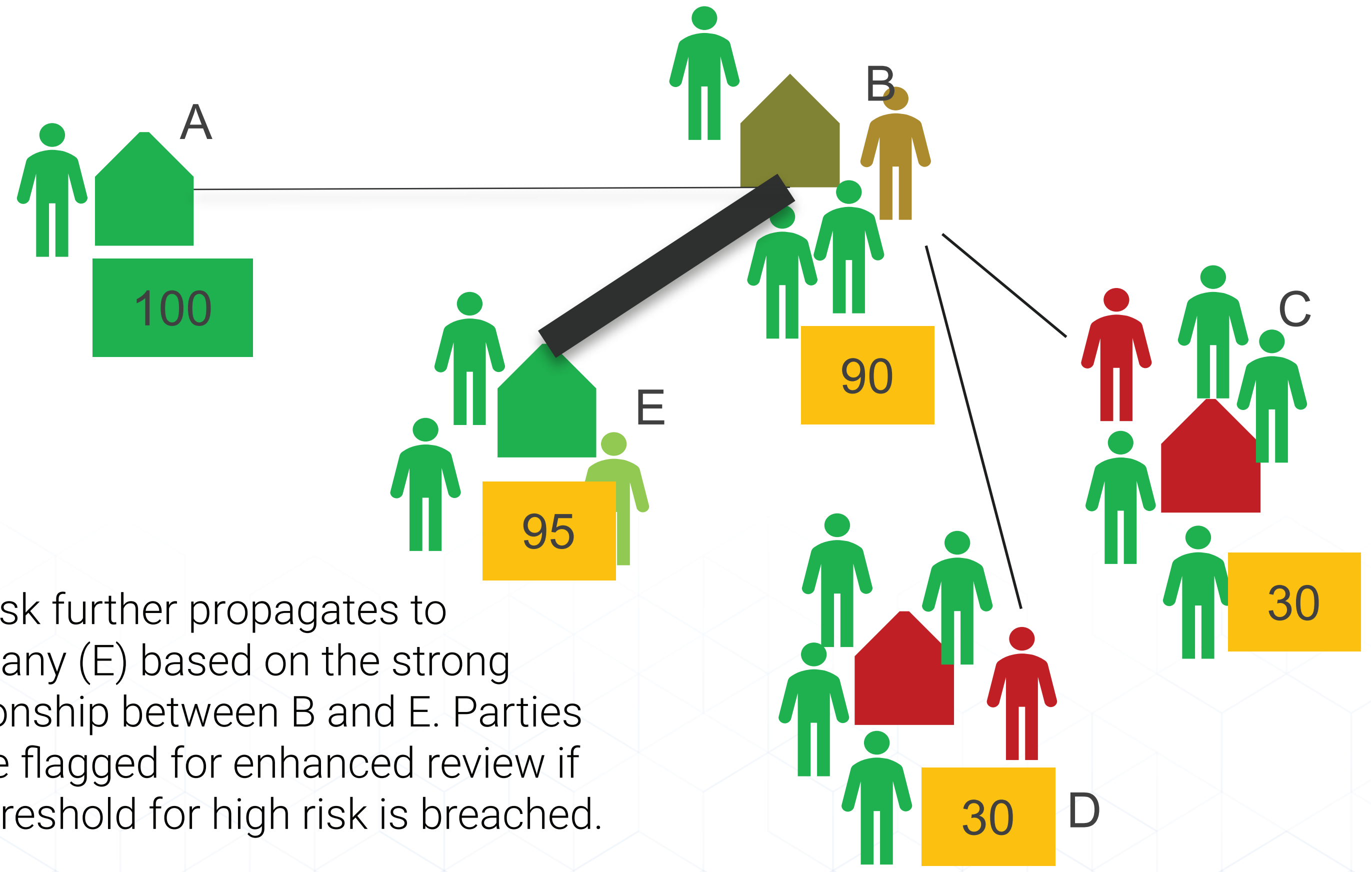
The risk is transferred to the related entity depending on the strength of the relationship. The score for the entity is lowered to reflect the new risk.

4.



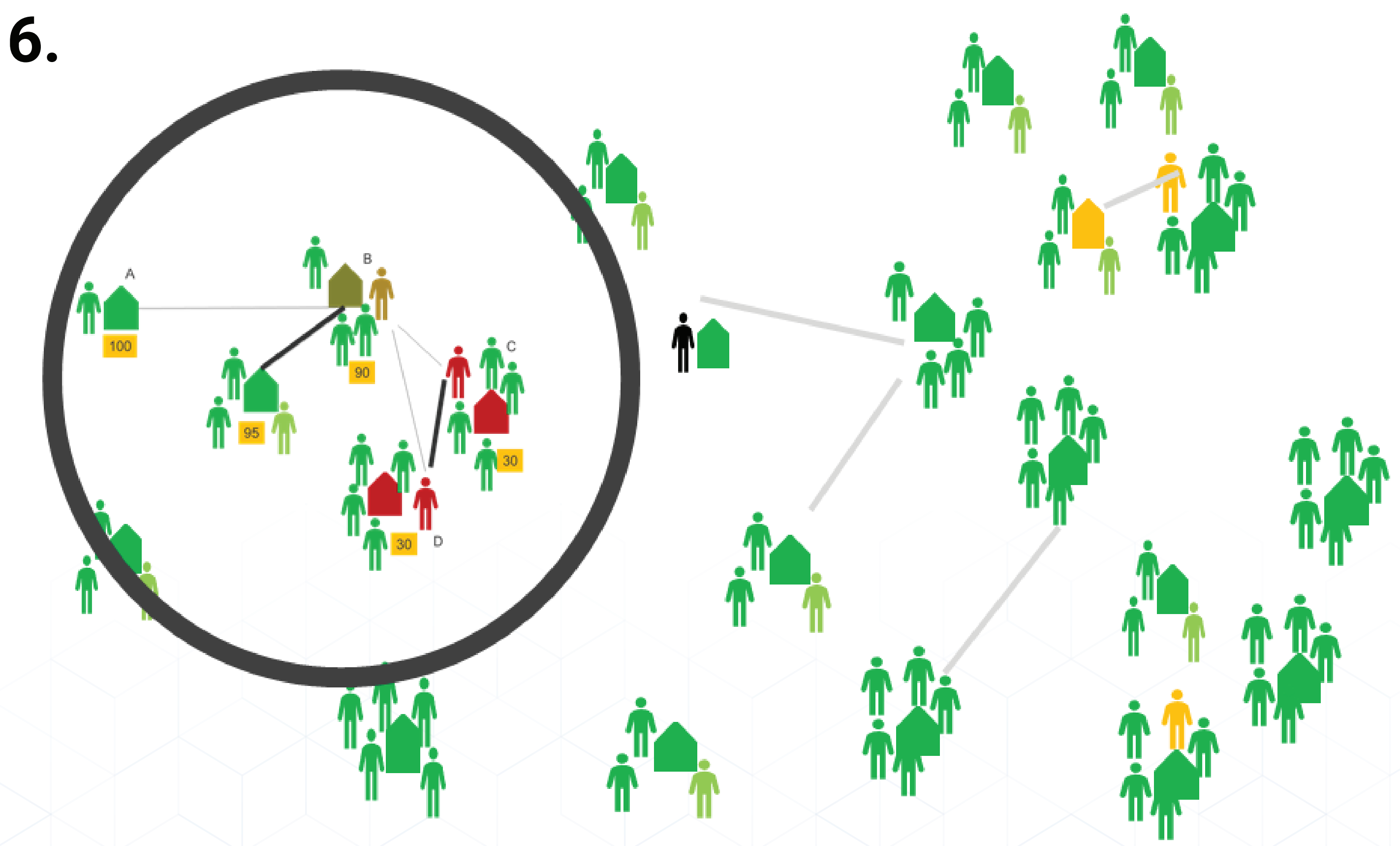
The network deep learning model identifies an individual related to the high-risk individual. Depending on the strength of the relationship, the new entity (B) has its score lowered to reflect the risk

5.



The risk further propagates to company (E) based on the strong relationship between B and E. Parties will be flagged for enhanced review if the threshold for high risk is breached.

6.



Leveraging a deep learning-based network risk propagation model allows you to preset thresholds and flag an event when those thresholds are breached. Thresholds for review trigger set responses using AI-based predictive analytics for evaluating risks.

This is important, because when dynamic risk isn't part of the risk management program, the risk of exposure to unscrupulous entities or customers increases. The potential for damage to your bank's reputation will outweigh the costs of establishing a comprehensive risk management practice. By introducing dynamic risk management with deep learning techniques into your CDD program, you'll be able to take a proactive approach to risk management and be better prepared for what lies ahead.

Ready to get started?

Partner with NTT DATA to redefine your CDD program.
Contact us at bpo@nttdata.com or visit nttdataservices.com/bpo to learn more.

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Shabi is a management professional with over 23 years in corporate planning, technology implementation, solution design and analytics, with demonstrated value additions in global project implementations and bottom-line impact valued at over $80 million. A key contributor to financial strategy, he has played a critical role in architecting more than $100 million in deals. Shabi directs know-your-customer/customer due diligence/enhanced due diligence/banking operations for global financial services clients, including service design, delivery, partner management and coordination with global teams.

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Dr. Paul is a business process and strategy senior manager in the compliance arena who has more than 18 years of experience. He is responsible for tracking the company's financial performance against budget, analyzing business performance and market conditions to create forecasts, and helping senior management make tactical and strategic decisions by providing periodic reports. Dr. Paul has authored research articles in many peer-reviewed journals, as well as presented papers at both national and international conferences.

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