



Seminar on Thematic Review of AIs' Sanctions Screening Systems

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- This presentation provides guidance to authorized institutions (“AIs”) on issues relating to their politically exposed person (“PEP”) & sanctions screening systems. The presentation is provided for training purposes and does not form part of the formal legal and regulatory requirements of the HKMA. It should not be substituted for seeking detailed advice on any specific case from an AI’s own professional adviser.
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- Background
- Methodology & Testing Process
- Observations
- Issues and good practices
- Next Steps



- Geopolitical developments
- Increasing complexity of sanctions
- HK vulnerable to abuse as conduit for illicit funds
- Response:
 - Sanctions compliance
 - Information and intelligence sharing



- “Anti-Money Laundering / Counter-Terrorist Financing: United Nations Sanctions” – Jan 2018
- “FATF Guidance on Counter-Proliferation Financing”; and discussion with stakeholders – March 2018
- “Feedback from Thematic Reviews of AIs’ Sanctions Screening Systems”; providing industry guidance after thematic reviews – April 2018

Thematic Review - Background



- During June 2017 the Hong Kong Monetary Authority (HKMA) conducted a Thematic Review of the automated sanction screening systems within the Hong Kong Authorised Institutions and global institutions with a physical presence in Hong Kong.
- The HKMA appointed the service provider to assist in conducting the review to provide analysis, benchmark the results and provide feedback.
- The HKMA's intention was to :
 - ✓ assess the **effectiveness and efficiency** of the AI's screening system
 - ✓ facilitate remediation of the AI
 - ✓ To enable HKMA to assess sanction screening risk associated with each bank, giving them the ability to put in remedial plans, to ensure stability of the banking sector
- A number of AIs were included within the Thematic Review, with the overall process being carried out in 4 stages:
 1. 'Kick-Off' Workshop
 2. Technical On-Boarding
 3. Test Execution
 4. Feedback Sessions

Testing Process – The Key Aims



The aim of the HKMA Thematic Review has been to understand the effectiveness and efficiency of each of the financial institutions' screening systems, with particular attention placed on five key considerations:

1. Does the institution's system generate an alert when an 'un-manipulated' sanctioned name is screened?

Demonstrates 'Pure' match capability and the 'completeness' of sanction lists within the institution.

2. Are the 'fuzzy matching' rules, configuration and threshold settings effective, such that a 'manipulated' sanctioned name generates an alert?

Assesses how well individual matching rules are implemented and the ability of the screening system to generate an alert when a 'minor' manipulation is applied to a sanctioned name.

Testing Process – The Key Aims



3. Are the levels of ‘False Positives’ or ‘Noise’ within operable levels?

When an alert/match is triggered, are the number of matches generated acceptable and operable within a BAU environment.

4. Is the system performance in line with the institutions’ expectations and in line with ‘peer’ performance?

This ensures that the Regulator is confident that they understand the capability of each of the institutions screening systems (bank v bank) and, not only understand any weaknesses, but also have a clear understanding of any remediation steps that are required to maintain a consistent benchmark across both the Hong Kong jurisdiction and globally.

Testing Process – The Key Aims



5. Overall, what testing regime has been adopted/implemented and is it sufficient?

Is any testing currently carried out? how frequent is it and is it of a sufficient level of granularity to provide confidence to the regulator?



- Should consider the risk of sanctions breaches and determine the appropriate level of sanctions screening to manage the risk
 - Demonstrate proven methodology for determining system settings and performance
 - Justify any deviations from group-wide policies
- Role of Management Information

Expectations: Testing on New Systems / Upgrades



- Onus on the bank to demonstrate thorough testing and tuning before system deployment
- System upgrades
- Documentation of testing and analysis should be duly conducted

Expectations: Frequent Ongoing Monitoring, Testing & Tuning



- Adequate understanding of obligations under HK and other overseas sanctions regimes (as applicable)
- Frequency of testing on system effectiveness and efficiency
 - Ongoing
 - Should result in an adequate understanding of system filter performance

Expectations: Adequate Skills and Knowledge



- Clear and demonstrable understanding of system filters employed in the institution's screening technology
 - Employing and equipping staff with the skills and knowledge to support system deployment
- Clarity around ownership and accountability of risk
- Monitoring of suppression / good guy / white lists

Expectations: Achieving System Effectiveness and Efficiency



- Understanding the relationship between effectiveness and efficiency
- Types of activity by which that is demonstrated
 - Monitoring levels of false positives
- Demonstrating reasoning for rules or threshold changes implemented to deal with levels of false alerts
 - In line with the institution's business requirements and risk appetite



- Als are expected to:
 - Give consideration to adopting the good practices, where appropriate
 - *gap analysis at a minimum*
 - Put in place regular sanctions screening system testing
- Information collection in Q3 2018; further review on a risk-based approach



- Significant legal and reputational risk of operating ineffective sanctions screening systems
- Cost of inefficient screening systems should not be underestimated
- The objective of this exercise is to provide AIs with the right information needed to optimize system performance
- Regular system testing is vital for AIs
 - Widely agreed upon, practiced by other regulators