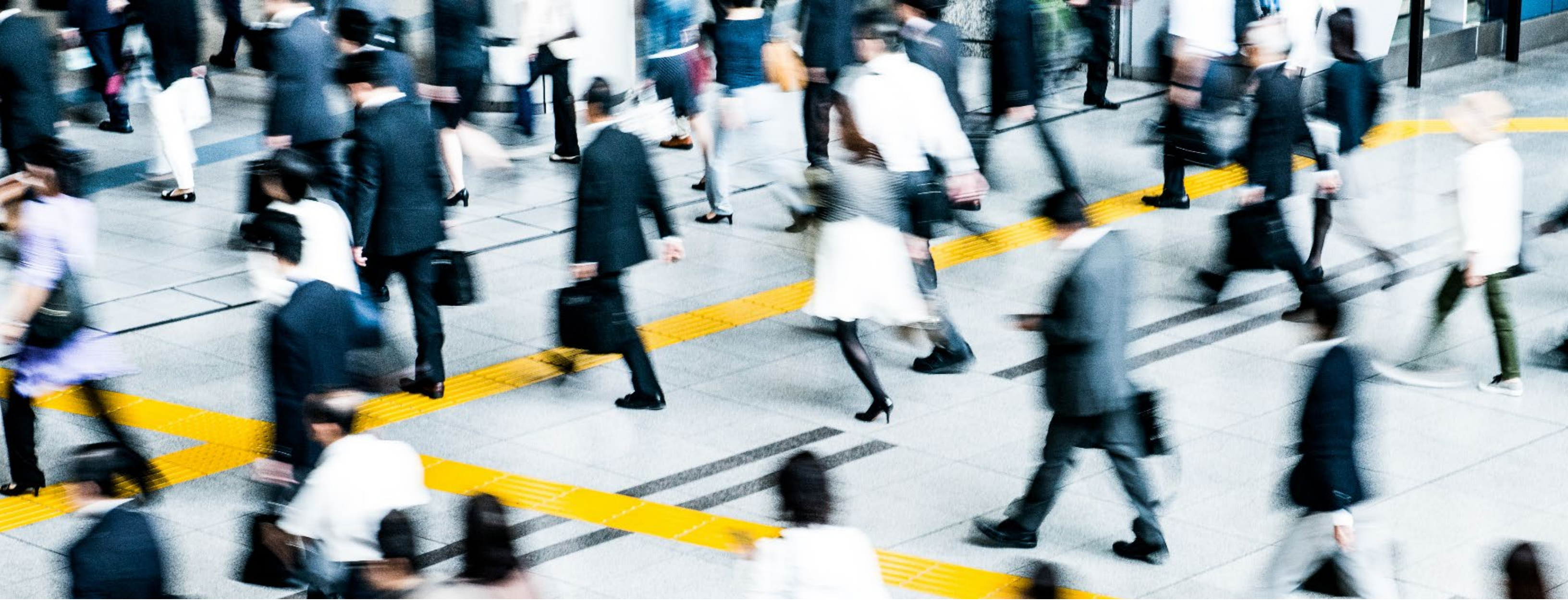
Deloitte.

The new era for KYC processes

Financial Industry Risk & Regulatory l Risk Advisory 2021



Customer identification and verification, or the Know Your Customer (KYC) process, is a vital part of the anti-money laundering (AML) activities of financial institutions, the development of which has been on the rise for the past decade. As the KYC process is also a very visible part of banking activities for the customers of financial institutions, the functionality of the KYC process has significant implications for customer satisfaction, further increasing its importance.

However, in early 2020, the pandemic essentially shut down the world in a matter of weeks and caused a shift in both criminal behaviour and a financial institution's ability to interact with their customers. As a result, this highlighted several areas within the KYC process that still crucially need development.

According to the Deloitte Regulatory Outlook 2021, due to the unstable situation in the world, financial crime has increased. As technology advances, cybercrime becomes more diverse and tracking down criminals is more complicated due to the anonymity enabled by the Internet. A decline in the use of cash has meant that illicit funds are more commonly transferred using cryptocurrencies and online wallets. The Internet enables real-

Furthermore, customer onboarding processes and other customer contacts have also moved online, making it more difficult to identify or interact with customers due to insufficient existing digital solutions. As cybercrime has increased, the online processes of financial institutions have resultingly become a common target of cyberattacks, thus making both the proper information and cyber security of the new technologies vital. From the customers' point of view, the shift to online channels has impelled them to switch from traditional branches to online banking regardless of their age group. As such, it is particularly important that banks find a balance in the services and channels that they offer as the use of digital services may create challenges for certain elderly customers.

All of these factors have had a significant impact on financial institutions and their ability to perform the customer due diligence process in accordance with AML regulatory standards. At the same time, however, these challenges create an excellent opportunity for banks to further develop their KYC processes so that they are more diverse and customer-friendly, and in order to keep up with both criminal activity and the continuous changes in the world.

The most up-to-date trends affecting KYC processes and their development

Digital identification

In the past, the need for physical ID and document verification made the onboarding process of new customers, and the process of providing any new products/services for existing customers, time-consuming, complicated and costly for both the customer and financial institution. This often resulted in poor customer experiences and, in some cases, the abandonment of the process altogether.

With the pandemic, and the resulting restrictions regarding social distancing and the closing down of some physical banking branches, the process of the physical face-to-face identification of customers, a vital step of the KYC process, has become problematic and, in some instances, has been suspended completely. Unfortunately, this has significantly affected financial institutions as many still rely heavily on hard copy documentation in order to verify the identity of their customers. In fact, according to a survey conducted by Signicat in their published study, The Battle to Onboard 2020: The Impact of COVID-19 and Beyond, 41% of customers across Europe have been unable to open new bank accounts or services due to the restrictions brought about by the pandemic and the lack of digital channels currently offered by their banks.

This has opened the door for innovative thinking and the need for digital transformation in the KYC market. With the replacement of physical documents with digital IDs and technology allowing customers to present their identity documents virtually, financial institutions could offer new customers a seamless and faster onboarding process without the need for a physical appointment. This would also provide a straightforward way for existing customers to acquire new products/services and update their KYC information. In addition to heightened customer experiences, this would allow financial institutions to save money while ensuring that they know their customers and remain compliant with both AML regulations and current coronavirus restrictions. In fact, the use of virtual identification using a smartphone, for example, combined with anti-impersonation and anti-fraud tools, would not only result in the successful remote identity verification of customers but could also be more accurate than viewing the identity document in person. Resultingly, in the Guidance on Digital Identity published in 2020, the Financial Action Task Force (FATF) encouraged financial institutions to develop and use digital identification methods whenever possible.

This, however, should not be viewed as a temporary solution to the KYC process for the duration of the pandemic as the customer identification process was taxing for both the customers and the institutions prior to the pandemic as well. Once the restrictions are lifted and we move into the post-COVID world, financial institutions should continue to offer and develop digital identification solutions as a means to attract new customers and ensure both customer-friendly and efficient customer onboarding and ongoing KYC due diligence.

Virtual banking tools

As mentioned previously, the lack of digital channels currently offered by banks has caused significant issues for financial institutions and their customers. Consequently, in addition to the need to develop digital identification tools, the restrictions brought about by the pandemic have highlighted the need to develop virtual and video banking tools as well. This important development would allow financial institutions to be able to see and interact with their customers with the use of web cameras, for example, and would thus enable financial institutions to carry out both the customer onboarding process and the required KYC procedures both virtually and remotely, all the while taking into account AML regulations. Additionally, this would allow the customers themselves to reach out and communicate virtually with their banks from the comfort of their own home, regardless of the day of the week or the time of day (for example, when required to update any missing or outdated KYC information). Once again, this would allow financial institutions to remain compliant, reduce costs and greatly improve customer experiences as the flexibility of the virtual banking tools would allow everyone involved to save both time and energy.

Even without the restrictions of the pandemic, the use of virtual banking tools, alongside traditional physical meetings, will be an essential way to accommodate the needs and timetables of each customer in the future. As such, as the world begins to open up and people's lives continue as normal, virtual and video banking tools, and their continuous development, will be vital for the future of a timely, diverse and customer-friendly KYC procedure.

The utilisation of analytics

Technological advancements create great opportunities to develop KYC processes amidst the many changes brought about by the pandemic. As financial crime moves to the Internet, criminals subsequently have a much wider playing field for different forms of financial crime and banks must be able to react quickly. In order to successfully prevent financial crime, obtaining up-to-date KYC data is of vital importance. However, the current processes of the manual collection and verification of KYC data – and if necessary, enhanced due-diligence measures – may take several days for the expert to gather and analyse. Therefore, obliged entities, such as financial institutions, need modern technology to enable an interactive and automated process for gathering data swiftly, giving experts the necessary time to focus on the investigation of relevant material changes and suspicious events. As such, developing and utilising analytical technology is vital, especially when working with high-volume and repetitive manual activities, in order to achieve the greatest benefits in a cost-effective manner. In terms of KYC, in addition to robotics, the use of artificial intelligence (AI) and machine learning processes are the hottest trends of the moment, bringing both agility and intelligence to the KYC process.

The aforementioned customer onboarding process, for example, can be simplified and streamlined through analytical functions. The AI and machine learning model can be used to build methodologies that respond to information provided by the customer (e.g. in Politically Exposed Person (PEP) monitoring) or changes in transactions. When changes to customer information or transactions can be reacted to immediately, customers can be categorised into the correct risk ratings, and as a result, valuable resources can be allocated to the right customers and better assessments can be made as to which resulting measures are essential and which are less important.

In the best-case scenario, utilising analytics in the KYC process will also result in heightened customer experiences when each stage of the process is smooth and intelligent. Analytical functions and robotics can be used to avoid ‘unnecessary’ obligatory customer contacts as data can be automatically and rapidly retrieved from official data registers and the information previously provided by the customer can be compared with actualised transactions. Customer data collected through analytics can also be used to benefit the financial institution’s various commercial processes as the sales operations may focus on their sales and marketing in a specific manner, according to specific customer needs. Therefore, the use of analytical technology will not only support financial institutions in keeping up with the increasingly fast-paced nature of evolving financial crime, it will also benefit the institution as a whole.

A unified remote workflow for KYC processes

As a result of the pandemic, work has largely shifted to a remote environment. Working remotely has also had a significant impact on the workflow of the various stages of the KYC process, which typically pass through the different systems and communication tools used by each financial institution. Traditionally, the stages of the KYC process have included physical customer encounters and access to the bank's core internal and secure databases, which have required process steps to be completed by employees in a banking environment due to restrictions on remote access. The sudden move to remote work meant that certain stages of the KYC process have become more difficult to complete, creating gaps in the KYC process flow. Therefore, in order for financial institutions to be able to carry out all the necessary KYC procedures seamlessly, it is absolutely essential for financial institutions to develop and achieve a fully digitalised workflow in order to connect both the different stages of the KYC process and the various teams working on them to all the internal and external stakeholders involved in the process. Most importantly, the functionalities of the systems must be developed to ensure that they operate comprehensively in a remote environment. Utilising cloud services, for example, could enable financial institutions to handle data management services in both a cost-effective and secure manner. Moreover, as the protection of confidential data must be taken into account when working remotely, the use of cloud solutions could also guarantee the implementation of security standards, authentication and encryption methods, as well as the secure backing up of data.

From a customer experience point of view, it is vital that the workflow between the various KYC process steps is straightforward and unified in order to avoid any increased customer waiting times. When the world opens up, it goes without saying that hybrid working will be here to stay, and thus, the development of a unified workflow for the KYC process will allow customers to be served using more flexible and multi-channel methods outside the normal and traditional opening hours of a financial institution's branch office.

Along with a number of important benefits, developing remote working tools for a seamless KYC process comes with certain risks as well. As many stages of the KYC process have been linked to a financial institution's core banking services, their development may take a long time. Further, handling sensitive and private customer information at home using a VPN connection raises risks of data leakage or the breaking of banking secrecy, which makes proper employee training a necessity. However, when these risks are effectively identified, tested and managed, the long-term benefits significantly outweigh the risks.

Turning challenges into opportunities

While the negative effects of the pandemic on financial institutions, including the increased financial crime, have been discussed at length, it is evident that it has brought about the need for a number of positive changes and developments within KYC as well. Due to these exceptional times, institutions are encouraged to actively develop and digitalise the processes and services used during the various stages of the KYC process as a means to offer customers increasingly versatile and customer-friendly experiences, and in order to remain compliant with AML regulations. Accordingly, technological development is also an important part of an institution's brand image, and as a result, these important developments within KYC will undeniably be an important way to attract customers in the future.

Feel free to contact us if you want to discuss further:

Laura Valo
Assistant Manager, Regulatory Risk
Laura.Valo@deloitte.fi

Linda Lamminpää
Senior Consultant, Regulatory Risk
Linda.Lamminpaa@deloitte.fi

Kaarle Pohjavuori
Director, Risk Advisory
Kaarle.Pohjavuori@deloitte.fi

Deloitte.

Deloitte refers to one or more of Deloitte Touche Tohmatsu Limited ("DTTL"), its global network of member firms, and their related entities. DTTL (also referred to as "Deloitte Global") and each of its member firms are legally separate and independent entities. DTTL does not provide services to clients. Please see www.deloitte.com/about to learn more.

In Finland, Deloitte Oy is the Finnish affiliate of Deloitte NSE LLP, a member firm of Deloitte Touche Tohmatsu Limited (“DTTL”), and services are provided by Deloitte Oy and its subsidiaries. In Finland Deloitte is among the nation’s leading professional services firms, providing audit, tax, risk advisory, legal, consulting, and financial advisory services through 600 people in 3 cities. Known as an employer of choice for innovative human resources programs, Deloitte is dedicated to helping its clients and its people excel. For more information, please visit our website at www.deloitte.fi.

This communication contains general information only, and none of Deloitte Touche Tohmatsu Limited, its member firms or their related entities (collectively, the "Deloitte network") is, by means of this communication, rendering professional advice or services. Before making any decision or taking any action that may affect your finances or your business, you should consult a qualified professional adviser. No entity in the Deloitte network shall be responsible for any loss whatsoever sustained by any person who relies on this communication.

© 2021 Deloitte Finland