HARNESS THE UNPREDICTABLE

SHARING KYC

POSITION PAPER

CHALLENGES, STRATEGIES AND CONSTRAINTS OF FINANCIAL INSTITUTIONS

To meet stringent regulatory requirements for anti-money laundering and countering terrorism financing, financial institutions must maintain the customer experience.

To this end, several actions have been implemented, including leveraging KYC information and documents already held by another institution within the same group or even outside their organization. Currently, several models exist for sharing KYC information, establishing a framework of producers and consumers of customer KYC. However, the consumption and sharing of KYC information face regulatory and technical constraints that complicate this process.

Despite this, it is essential to optimize the sharing of elements that constitute risk. Simultaneously, there is a need to enhance the efficiency and reduce the costs of the KYC process while adhering to the risk-based approach.

SUMMARY

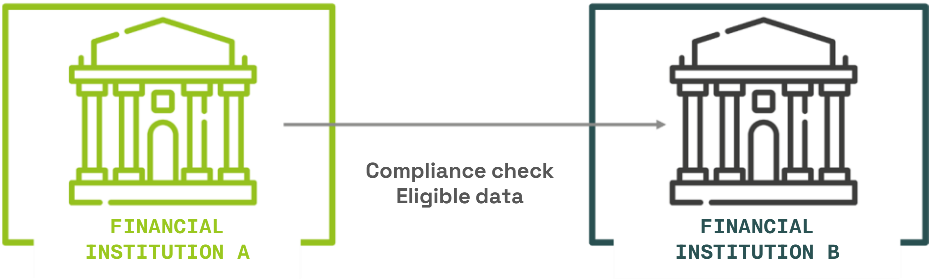
THE CHALLENGES OF KYC PRODUCTION AND CONSUMPTION

DEFINITION AND SPECIFIC CHALLENGES

The financial sector has witnessed the growth and diversification of relational and contractual dynamics with customers. Banks can collaborate with one or more partners or other entities within the same banking group to manage various activities: banking, insurance, structured finance, consumer credit, asset management, and more. Banks, their subsidiaries, and partners must all adhere to the same regulatory standards concerning customer knowledge.

THE THIRD PARTY INTRODUCTION

Third party introduction is the most common practice encountered within the banking/insurance industry. This practice sees an entity of a group, most often a subsidiary, benefit from a KYC file carried out by another entity of the same group. This type of agreement establishes a logic of producer of KYC in front of a consumer of the same KYC file. This approach can reduce the costs and time associated with obtaining new KYC information. However, it requires a high level of trust between the two financial institutions and assurance that the issuing institution has carried out adequate KYC checks. Be careful, there are certain pitfalls that make its implementation complex: the risk profile is necessarily the one calculated by the producing entity, the supporting documents are not held by the consuming entity. For instance, in the event of the end of a client's relationship with the KYC producer, the entity that consumes the KYC will benefit more from the update made by the producer.

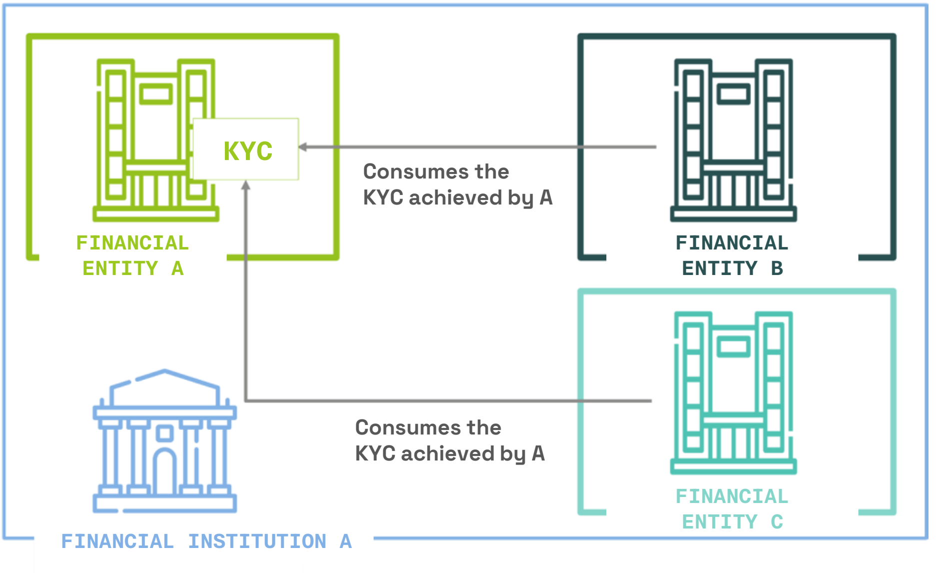


INTERNAL POOLING

Internal pooling, on the other hand, proposes to pool KYC information within the same financial institution, between different branches or divisions of a bank. For example, if a client is already known and verified by the investment banking (CIB) arm, the KYC information can be "green flagged" to the retail banking branch, avoiding the need to ask the client again for the same information. This approach can improve efficiency and the customer experience, but it requires good internal coordination and a secure information-sharing infrastructure.

It is important to note that while the concept of a "green flag" may simplify the process of transferring information, it should be used with caution. KYC and AML regulations are complex and differ from jurisdiction, and financial institutions must ensure that they comply with all regulatory requirements.

It is necessary to designate the actor in charge of the periodic or event-based review of the customers concerned.

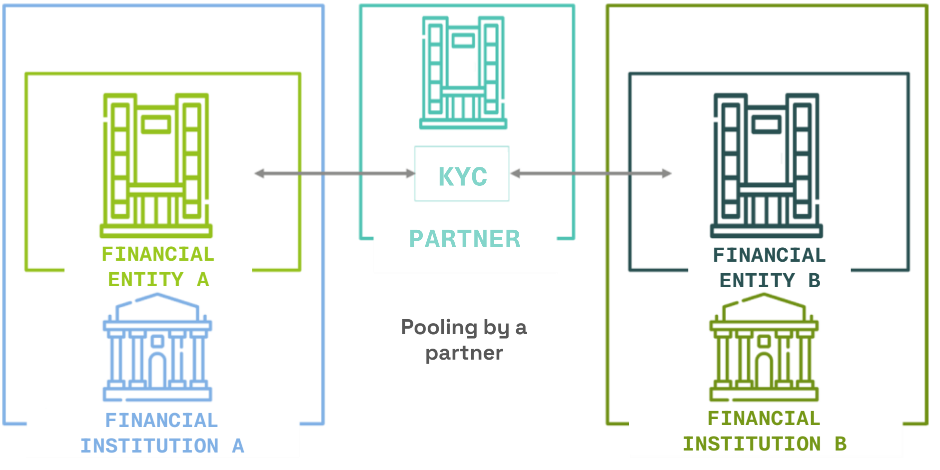


[1] Anti Money Laundring

EXTERNAL POOLING

The last modality is the external pooling of KYC. This approach is based on collaboration between different financial institutions. The main feature is the sharing of the building blocks of KYC, which does not take away the responsibility for KYC from each party involved. This approach requires meaningful cooperation between financial institutions and confidence in the model implemented.

This different way of operational sharing, highlight issues related to data quality, as technical solutions allow communication between entities in a fluid and efficient way.



Pooling by a partner

IMPLEMENTATION STRATEGIES

MANAGEMENT POLICIES IN DIFFERENT SHARING MODELS

When it comes to the implementation of sharing methods, there is no "one size fits all". There is great variability from one institution to another, with high ambitions for KYC sharing and exchanges to be smoother in the future.
The question of liability, for its part, is also variable. Some participants are already talking about a materialized boundary between producers and consumers, while others are still in the definition phase between entities to determine "who does what". Responsibilities are not uniform from one institution to another.

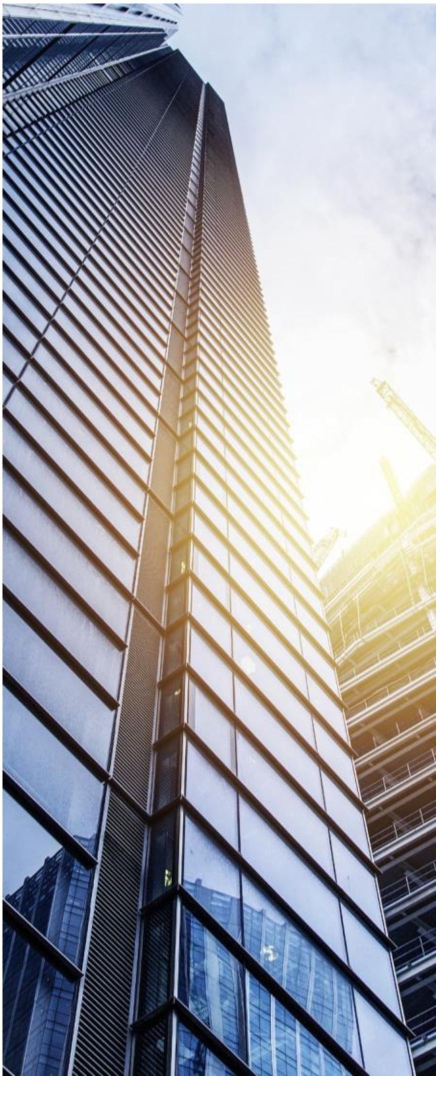
However, there is a common desire to limit the effort around KYC and to pool the information collected as much as possible. This limits the risk of duplication and reduces the cost of carrying out KYC.

The different players have relatively similar strategies at very different degrees of maturity. Some have already implemented accurate chargeback, while others are still thinking about it.

As far as models are concerned, there are SLAs, contracts and general and specific conditions that inform the customer. These documents also serve as a clarification tool for entities in terms of the requirements to be followed.

[2] Service Level Agreement

THE CONSTRAINTS AND CHALLENGES OF SHARING KYC



THE CASE OF ORPHANED CUSTOMERS

Carrying out KYC for these customers presents a particular challenge in terms of operational execution because banks no longer have a contact form for them for legal and regulatory reasons (CNIL / GDPR).

Although the distributor (in this case the customer's bank) may rely on third parties (group entity/partner) to perform KYC, the ultimate responsibility for monitoring and compliance still lies with the distributor. The lack of a live business relationship can make it difficult to accurately track the client's transactions and activities, which can increase the level of risk.

It is also a technical challenge for banking players, as they must set up systems capable of clearly identifying the orphaned customer and being able to distinguish on his behalf the services for which he is eligible.

REGULATORY AND TERRITORIAL CONSTRAINTS

Regulation plays a key role in sharing KYC data. For example, the GDPR in Europe imposes the need to collect customer consent for data sharing. Additionally, customers have the right to access their data and request its deletion if it is misused. This can have consequences on the maintenance of the commercial relationship.

Territories such as Hong Kong, Singapore or China require strict separation of data and documents collected for other entities (sometimes referred to as a "Chinese wall" or "ring-fencing"). However, this does not prevent entities from setting up data indicators without explicitly sharing the data, thus helping to justify the level of risk or completeness of a KYC.

The fact remains that the regulatory and legal framework is not always aligned with the legislator. The 2022 experiment conducted by ACPR in France to share transaction data and monitor customer transactions across the banking system is a concrete example of this. This initiative aimed to eliminate disparities in the information available to an individual who held an account at multiple banks. However, the CNIL stopped the project, considering that it did not comply with the requirements in terms of freedom and security for the customer.

THE TECHNICAL CHALLENGES OF SHARING KYC

The technical challenges of sharing KYC are also significant. The main obstacle is the heterogeneity of information systems and the structure of the data. Each entity has a different approach to KYC, which results in a variety of data formats and structures. However, experiments are underway to overcome these obstacles.

In the case of internal pooling, collecting complex information like financial statements or revenue data can be a challenge. This information could be retrieved through other means, for example during the credit risk assessment or when an entity has set up financing or recent data collection on the same customer.

As for external pooling, the focus is on documents or documents that are time-consuming for the customer to obtain and that banks find difficult to retrieve due to the complexity of their customers' structures. This is particularly the case for Corporates.

Some platforms allow the KYC documents of professional customers to be pooled and made available to banks (Compliance, in particular). After obtaining the customer's authorization, each bank can use the documents to complete its KYC process.

Initiatives in the insurance and banking sector in France (such as Excellcium) have been launched to pool KYC (customer identity and address) information.

Financial institutions should continue to explore technologies and approaches that can help them improve the principle of sharing KYC. In addition, alignment with the regulator is a key success factor in considering an effective model.

Indeed, certain situations such as the provision of the register of beneficial owners highlight the need for increased communication between stakeholders to make these mechanisms effective. In the same way, the provision of certified solutions at the European Union level could accelerate the implementation of a model recognized by all (e.g. the EIDAS V2 regulation).

ABOUT KYC BY TNP CLUB

Every two months, the KYC by TNP Club brings together banking responsible for KYC to discuss the regulations and their interpretation, KYC best practices and accelerators, the difficulties experienced, etc.

The Club now has more than 25 active members, belonging to the major banks of the market neo-banks, corporate banks and asset managers.

Topics addressed during the meetings are proposed by TNP and selected by the Club's participants. Position papers summarize the discussions of the members around the selected themes.

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ABOUT TNP

Founded in 2007, TNP is an international independent and hybrid consulting firm specializing in operational, regulatory and digital transformations. HYBRID, because it is bilingual business-technology. INDEPENDENT, because it is the best way to freely practice our profession and to offer solutions that are truly adapted to the expectations of our customers.

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