

KYC-Digitalization for Compliance & Marketing

1 The Importance of Client Master Data

Historically banks had branch managers or relationship managers who knew about the occupation of their retail clients or about the business of their corporate clients. Within private banking they were aware about the origin of client's assets and to whom those assets were designated. People were doing business with other people and thus the manager was familiar with the **client's private and commercial situation**.

Hence those front office managers looked at the enforcement of mandatory KYC-rules as formalism. Free text KYC entries, captured by the bank's staff in in the late 1980s due to those „new-fashioned money laundering laws“, might have been compliant at that time. But they were never able to adequately substitute the knowledge of the bank's managers – not even after regulations like MiFID, Withholding Tax or CRS largely increased the number of mandatory attributes.

Using the language of digitalization it can be said that the manager had saved the relevant attributes in his brain. The same was true for the algorithms to transform the attributes into relevant knowledge. For this reason reducing the number of relationship managers means losing relevant knowledge – unless the transfer of both attributes and algorithms into the bank's systems succeeds. But unfortunately, many attributes have only been captured (even today) because the bank is obliged to do so – and not even thinking about using the data to gain additional insights.

This minimalistic approach is unlikely to lead to knowledge about the **client's private and commercial situation**. In the best case the bank is compliant, but the client's wishes, needs and „peculiarities“ remain unknown. This gap will happily be closed by non-banks taking business from the banks. Apple, Amazon and the likes were not even thought of at a time when banks had already started the digitalization of their business. But today Apple Pay works, and it will not be long when ordering the book „Ways to your own house“ will lead to the buyer also receiving offerings for mortgages; of course only if the buyers address indicates a good rating in a sought-after neighborhood.

The number of relationship managers will further decrease. Attributes and their interdependences are probably not organized well – correlating with their age. Responsible officers for taxes, compliance or marketing are natural allies when it comes to data quality, as even the best algorithms will fail without input in good quality. Let us have a look on how and why banks should focus on having high-quality client master data.

2 Structure of Data

2.1 Person vs. Relationship

For every client related information in the bank's system it must be clear if the data is related to a person (natural person or legal entity) or to the client relationship (contract). The older the system used for managing the master data, the higher the likelihood that this differentiation is not properly implemented. This makes it even more important that the attributes are fully understood and correctly assigned when defining the algorithms.

The date of birth for an individual is related to a person, similar to the name. Looking at addresses, things get more tricky already. If 2 persons hold 1 relationship to the bank, hopefully both have a domicile address. Meanwhile mailing instructions are connected to the relationship. Here a P.O. box would be allowed too. Or an Email-address – or is this not better

stored at the person level? Address data is actually seen as the easy part of the game, but even here there are pitfalls. Which address for example is used for a credit rating or a marketing mailing?

2.2 Persons and Roles

No matter if a person acts as account holder, beneficial owner, p.o.a. or all together in several relationships: one individual (or one company) is stored only once in the master data system. Inconsistent marketing activities are harmless, compared to the breach of AML regulation. And such breaches are going to happen, if one individual in real life is stored five times in the system - which is unable to detect this virtual multilocation; especially if the five persons have different domicile addresses.

If the bank's systems cannot handle this today (because different systems are used for defined roles), an additional database is required as master system for all person related data. Replication procedures are essential for consistency. Otherwise not only peculiar mailings will occur, but also the authorities will turn nasty very fast.

2.3 Legal Form and Wording

Is a limited partnership a non-incorporated company? How is an US LLC to be treated under German tax laws? Setting attributes should only be done by those who really know what they do, as incorrect encoding might cause a massive impact on downstream applications, e.g. for taxation or documentation purposes. What matters even more than processes is a corporate culture allowing staff to ask when in doubt.

Trying to apply international standards can be even more difficult. The British trust is not the same as the US family trust. And the translation of any legal term from English into German might lead to different results for Switzerland and Austria. A bank's glossary for an international data project must cover such cases.

2.4 Data Fields vs. Data Usage

Capturing the quota of a beneficial owner's participation might be useful, but only once for all purposes. For example, there is no different participation for CRS and FATCA. If regulation demands or allows different handling, a 5% participation might be used for AML purposes and ignored for FATCA.

Whereto should clients be reported if domiciled in Crimea? Whatever might be determined today or in future, the drop down for the data field „domicile country“ must not only contain real states but also special jurisdictions. This hopefully already exists for Hong Kong or Jersey but should now also include Crimea or Northern Cyprus. Data Usage might be different for CRS, MiFID or AML. Each bank may be affected, if a client informs the relationship manager that he moved from London to Yalta last week.

2.5 Forms

Authorities may define mandatory information to be captured, but the forms used are mainly designed by the bank. This is a chance for each bank to synchronize the demands of marketing and several regulatory directives into one useful form. No client likes to complete forms, especially with redundant information. This applies accordingly for online forms or questionnaires completed by relationship managers. The only way to ease the life of clients and staff on this is to ensure that the manager responsible for the forms has a fundamental

understanding of all related aspects and interdependencies. And as forms follow the structure of data, both need review and update with each regulatory change.

3 Processes & Lifecycle

3.1 Integrity

A person in the master system, representing an individual which moved from Zurich to Vienna, is moved to Vienna in the master system too – latest after receiving the registration confirmation in the bank. And of course this information is replicated into all systems which know this person with the overnight processing at the latest. National rules and guidelines may require additional formalities for special roles, but an individual with one domicile only will never live simultaneously in different countries. Naturally this applies for all other attributes of the person as well, like for example name, marital status, nationality etc.

3.2 Primary Data and Derived Data

If the client from the previous example, who moved to Vienna wants his correspondence still to be sent to his old address in Zurich, this is not necessarily a breach of integrity; maybe he has a relative remaining there who is taking care of his financial matters. But still it is preferable that the address is changed only once with replication for example to the mailing instructions. This simply means that additional rules shall be implemented for the replication.

It gets even more complex for a relationship with 2 account holders. After their divorce Mr. and Mrs. Meier live one in Hamburg and one in Berlin, but the relationship or mailing instructions remain keyed to New York. In this case neither marketing nor FATCA can operate correctly. Ideally algorithms are able to solve this, but at least an alert should happen to trigger a manual check by the relationship manager.

4 Plausibility

The BVI offshore company¹ is not „active“ according to FATCA. The savings club as simple partnership of two individuals domiciled in Italy and in Austria is not domiciled as a club in Panama.

Such peculiarities must never go undetected. Today's compliance and reputational risks are so big that an instant closing of the relationship is preferable over a time-consuming investigation to hopefully find exotic justifications. Exceptions for UHNWI clients shall be subject to thorough investigations.

A client born in 1940 is most likely not interested in a savings plan, and also not in an occupational disablement insurance. Having a date of birth in 18xx means the definitive end of US tax liability, the presents for loyal customers should be sent to the heirs - and if they are unknown, the accounts are dormant. And both Biafra and the Soviet Union might be the country of birth, but they may never be part of a valid address nor nationality.

Plausibility checks should run in an automated way whenever possible. Smaller banks may do it in a (semi-) manual way, based on extracted data – as long as compliance ensures that it is really done regularly.

¹ For Swiss readers „domiciliary company“ according to CDB

5 Clean-up of Legacy Issues

Banks with a proven concept for managing their client master data, a correct IT implementation and strong enforcement of processes and rules may enjoy the luxury of “self improving” data, while new errors will be rare. Data clean-up is still required, but will be quite easy to sustain good quality and correct data.

5.1 Adjustments without Contacting Clients

If all relevant data has been received but not yet captured in a system, a redo of OCR scanning should be sufficient. If the last formalities have been collected in the last century, correctness can be assumed

- hopefully for the date of birth and first name
- sometimes for last name and address
- rarely for **private and commercial situation**.

And a change of the business purpose of a legal entity might have a tremendous impact on the FATCA and CRS status. When in doubt, it is advisable to simply reach out to the clients.

5.2 Adjustments with Contacting Clients

Getting new documents from clients might cause new implausibility's with already existing formalities. Whenever a client is contacted in such cases, ideally a full repapering is done. This should obviously be done based on the new forms, with a short and understandable explanation on how and why to complete the forms. For clients without dedicated relationship manager an inbound support center can be useful. All this is not for free of course, but in the end much cheaper than the invisible costs of lost chances and a bad reputation.

--

Banking Concepts knows the full importance of high-quality and up-to date client master data, both for marketing purposes and regulatory compliance. In addition, we are familiar with the challenges of capturing and maintaining this data and its structure. Furthermore, we know about the importance of processes related to the life cycle of clients and we have experience with reach outs. And we are familiar with many banking systems.

Please do not hesitate to contact us:

Banking Concepts AG
Gartenstrasse 59
CH-4052 Basel
Tel.: +41 61 284 9080
<http://www.bankingconcepts.com>

André Schwarz
Managing Partner
Mobile: +41.79.600 85 74
andre.schwarz@bankingconcepts.com

Benedikt Jaeger
Senior Consultant
Mobile: +41.79.316 71 61
benedikt.jaeger@bankingconcepts.com