

Know Your Customer Screening
for
Negative News:

There is Now a Better Way

David Caruso

Chief Operating Officer

TransparINT, LLC

david@transparint.com

November, 2015

Executive Summary

Knowing Your Customer (KYC) is, “the cornerstone of a strong BSA/AML compliance program.”¹

The purpose of KYC is to identify customers, counterparties, beneficial owners and others doing business with a financial institution who pose greater money laundering, financial crime, or terrorist financing risk.

Identifying what is known as “negative news” is an essential way to determine who among this group poses risk.

Negative news, also known as “adverse media” is discovered by searching the public information domain, where news items, publications, and other print or electronic records exist. Negative news research is an indoctrinated core of KYC compliance.

Anti-Money Laundering (AML) and financial crime compliance professionals rely on just a handful of applications to discover the misdeeds of those they are researching. Nearly every financial institution uses these applications, or tools, and has done so for the past decade. The tools include risk intelligence databases, archived news libraries, and internet search engines such as Google.

Many believe these tools are an effective way to discover past risky activity. Most in the industry accept that if there is a record of wrongdoing to be found, it will be found by using these applications.

That belief is wrong.

Applications financial institutions use to discover negative news fail to identify significant amounts of publicly available risk information.

This poses substantial compliance, operational, legal and reputation risks.

¹ Federal Financial Institutions Examination Council, “Bank Secrecy Act/Anti-Money Laundering Examination Manual” 2014.

Introduction

Knowing Your Customer: Then and Now

Customer Due Diligence hatched in the 1990's as "Know Your Customer" initiatives from the Federal Reserve, OCC and FDIC. During that time, Congress easily defeated what was seen by many as intrusions into the American public's privacy.

That changed on September 11, 2001.

In the months following the attacks on the United States, Congress overwhelmingly approved the USA PATRIOT Act, provisions of which enshrined into law financial institution obligations to know their customers.

The past 15 years have seen regulation of financial institutions grow substantially. The instability of our country's banking system brought on by loose credit, poor mortgage underwriting, and the recession in 2008, added more regulation. At no point in our history have financial institutions, of all kinds, been subjected to more regulation and oversight than right now. This isn't going to change.

There are thousands of rules and regulations to which financial institutions must adhere. Some are more important than others. Among these more important requirements are those that are collectively known as "Know Your Customer" mandates which have several elements including Customer Due Diligence (CDD) and Enhanced Due Diligence (EDD).

Why KYC Is So Important

The purpose of AML laws is clear:

Institutions are obligated to identify, investigate and report suspicious activity.

Do this correctly and financial institutions avoid government investigation and enforcement.

Fail to report suspicious activity and the consequences are severe: Billions in fines, lost careers, and skyrocketing legal, compliance and operating expenses.

Two elements are needed for institutions to properly report suspicious activity.

1. Institutions must know *what* customers and counterparties are doing.
2. Institutions must know the true nature and pasts of those *with whom* they are doing business.

This paper addresses how current industry practices for complying with the second element, KYC regulations, fall well short of fulfilling regulatory requirements and how TransparINT enables institutions to fully comply with AML laws, properly identify risk, and protect themselves and their employees from penalties.

The Problem of KYC and Due Diligence

As you read this, thousands of AML due diligence analysts and suspicious activity investigators are using risk intelligence databases, news libraries and Google to research customers, counterparties, and beneficial owners.

The analysts, and their management likely have a sense of comfort that by using these tools they are fully complying with regulations and identifying potential money laundering, terrorist financing and financial crime risk.

That sense of comfort is misplaced.

Traditional negative news applications and search engines do not perform as AML users imagine.

Where do these applications fall short? In the following areas:

1. **Missing information:** Today’s negative news products look at only a small fraction of publicly available information. Most providers look at a few thousand sources. Commercial search engines, while scanning many more sources, are not built with AML compliance in mind. Closely guarded algorithms (these companies are worth billions for a reason) incorporate many nuances that actually hinder efforts of AML analysts to discover information that identifies risk.
2. **Flood of unrelated information:** Combing through pages and pages of results from news libraries and search engines is time consuming and monotonous. Case workloads pile up as analysts spend too much time reading through piles of results to determine what, if anything, is actually related to the people and entities under investigation.
3. **Inconsistency:** To use negative news and search engine applications, analysts either adhere to highly structured methods and approaches (think elaborate search strings) or as more experienced analysts will attest, devise their own methods and “tricks of the trade.” There is little likelihood that each analyst in any due diligence or investigation group undertakes their work consistently from case to case. *This is risky.*



Are compliance officers, executives, and regulators as nervous as they should be that every day thousands of pieces of meaningful and available information needed to make good risk management decisions goes undiscovered?

Today's Approach to KYC and Due Diligence

As part of KYC, every AML compliance department uses some application to identify adverse media, PEPs, and sanction information. These applications fall into the following categories.

“Risk Intelligence” Databases – Risk Intelligence databases enable users to search a set of structured data (imagine a spreadsheet of names) for individuals, businesses, and government entities. The Risk Intelligence database provides what is called a “profile” which is a brief summary explaining the reason a database vendor believes the person or entity poses AML risk. The risk may be posed because a major news media outlet reported a bribery investigation involving your customer, or because the beneficiary of a wire payment is an official of an unseemly government.

Information in these databases must be pulled together, sifted through and selected for inclusion by people who read piles of news publications and government bulletins and pick out names they believe may be of interest to AML professionals. These employees then go through a manual process of typing information, creating URL links, and categorizing the reported offenses.

Archived News Databases – Archived news databases are large collections of media

articles that may go back more than a decade. News databases contain much more information than risk intelligence databases.

Archived news databases accumulate articles and are used not just by the financial service industry, but also law firms, academic researchers, and media outlets.

Business Reporting Services – Business reporting services gather commercial record data. Corporate registration files, ownership records, and financial reports provide subscribers background information.

Watch-List Screening – These applications compile anywhere from a few dozen to many hundreds of lists from governments and non-government organizations where individuals, entities and governments that are sanctioned, barred, or prohibited in some way from using domestic or international financial, trade, communication, or travel services are listed.

Search Engines – Google, Bing, Yahoo; everyone uses them for all aspects of their life, including work.

Public Record Libraries - These applications include information such as property records, car registrations, boat licenses, marriage records, liens and judgments.

Where Today's Applications Fall Short

Each current approach to due diligence has weaknesses, and because of this, institutions use a combination, or all of the available choices described on the prior page. A bigger concern however is the fact that even with using all these applications users are regularly missing vital information needed for sound AML compliance.

Risk Intelligence databases are constrained by human effort and attention. Database vendors must selectively choose which information to review and they must rely on humans to read, record, input and create records. Such reliance on employees scattered around the world means error and omission occur every day.

Moreover, the leading risk intelligence databases may market that they have more than 2,500,000 “profiles” (i.e. list of names) but this is a claim with little meaning. Sure, 2,500,000 is better than 1,000,000, but what if the public information domain contains enough data where there should be 10 million or 20 million or 50 million such profiles?

Archived news databases contain large collections of media articles. One leading archived news databases promotes that it stores stories from nearly 35,000 sources. There are two problems with this.

First, 35,000 may seem like a large number but in fact it is only a small number of the sources of information that are useful to AML analysts.

Second, the ability provided by these archived news databases to quickly and accurately search for relevant articles is poor.

Analysts who search for records using a person or company name know the sense of frustration when they are faced with paging through dozens of articles, hoping to find any that relate to their current investigation.

Attempting to address the problem of having to scroll through too many articles, KYC analysts use key-word search strings hoping to reduce non-relevant results. In some instances, the key word search strings are useful, in others the search strings limit the number of returned articles, and perhaps eliminate the responses that are actually important.

Key word searches strings are not used among every analyst, in every search, every time. This means work from analyst to analyst is inconsistent. Inconsistency leads to non-compliance.

Business reporting services are useful to understand a company's operations, markets and financial status, but are unlikely to uncover negative information. Much of the data these products publish is provided by the businesses themselves. Visit the websites of the leading business reporting services and you will see for yourself the simplicity of establishing a record with them. Once you pay the nominal fee, you can provide them anything you'd like about your business, accurate or not.

Public record databases can validate addresses, let users know marital status and on occasion will note that the person under review hasn't paid taxes. These are good systems to confirm demographic and personal data but rarely identify real AML risk.

EFFECTIVE SCREENING FOR NEGATIVE NEWS

Search engines like Google have transformed how people get information.

Google uses complex algorithms that find information. These algorithms use hundreds of factors including those about the sites Google indexes and information Google knows about *you* the user. Where your computer is located, your past search history and popularity of the web pages Google catalogues, are just a few of the more than 200 elements the algorithms consider.

Google is not however the best way for AML analysts to find negative news information.

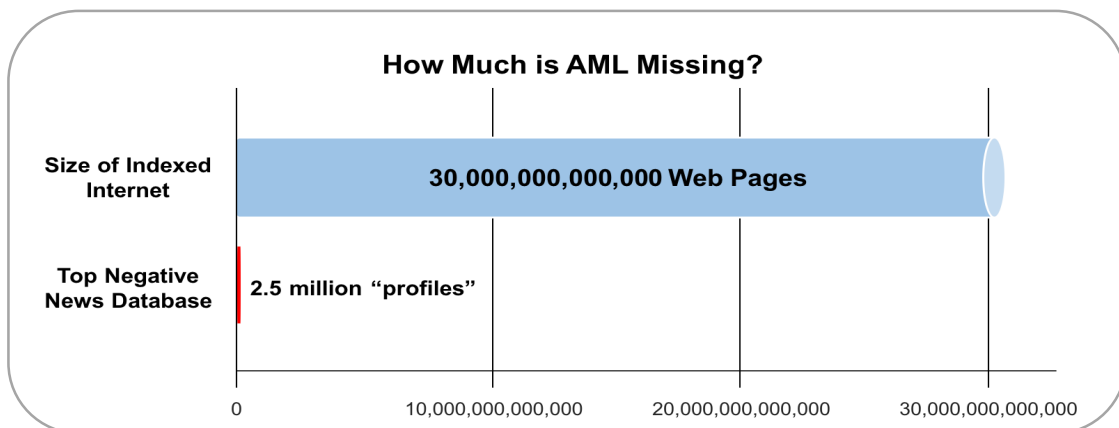
We do not know the logic and computations behind Google’s algorithms. Those are Google’s property and their corporate secret.

Many of the elements Google’s algorithms use to find the best restaurant in town or a list of the best movies from 1987 (Top Gun) can impede an AML analyst’s efforts to find negative news.

Factors like your location, search history and page rank, while great for finding good restaurants, may bury - pages down the list of search results - the information needed by an AML analyst.

Consider this – there is an entire marketing industry devoted to helping companies ascend higher on Google search results. If there are ways, by capitalizing on Google’s methods, to improve the likelihood of a more visible result, are there not also ways to use Google’s methods to bury results someone wants to hide? Of course there are. Use Google to read about “reputation management” and see how anyone can take a few simple steps to bury negative news information about themselves on page 4, 5, or 10 of Google results, thus effectively hiding it from an AML investigator.

Security of information – Web sites, whether run by the New York Times or a jihad fundraising group, know who is searching their sites (in this case a financial institution), what the institution is looking for and the search terms that found it.

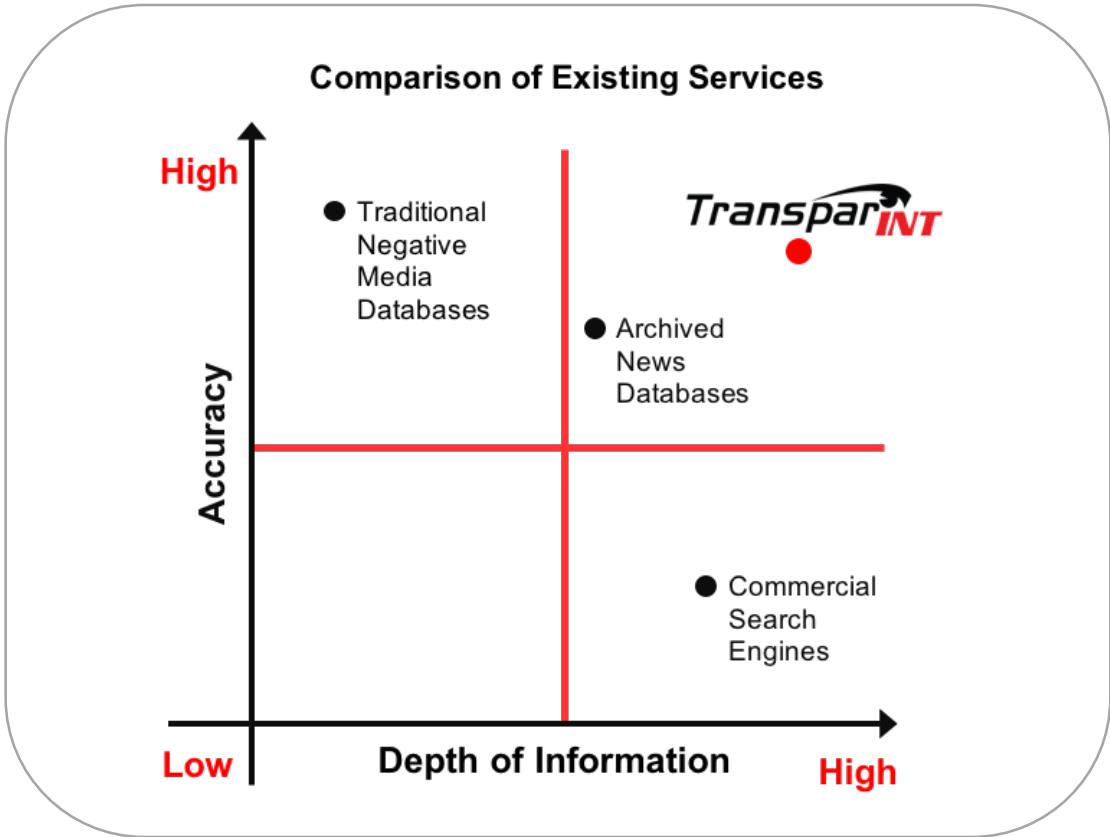


Better Approach to Discovering AML Risk Information

Existing risk intelligence databases, archived media collections, and search engines fail to fully identify information needed to make informed and supported AML risk management decisions.

TransparINT overcomes those shortcomings, enabling AML compliance programs to properly fulfill their legal and regulatory obligations. Regulators expect financial institutions to find information available in the public domain.

TransparINT uses computer science technology known as Natural Language Processing and Machine Learning that enable us to scour vastly more information than any other present day AML or financial crimes application *and* to return that information to our users with an unmatched degree of accuracy.



TransparINT provides greater accuracy and depth of information than traditional sources

What TransparINT Does and Its Value to Our Users

1. More Coverage: TransparINT provides immediate access to the largest collection of media information available to AML and financial crime compliance operators.

No other system, whether a risk intelligence database, an archived news database, or commercial search engine provides as much direct relevant information to AML analysts. Instead of using a defined number of information sources, like risk intelligence and archived media databases do, TransparINT uses a patent pending identification and relevancy scoring process powered by leading edge Natural Language Processing and Machine Learning programming to scour the entire contents of the world wide web, at the moment our users initiate a search.

Risk intelligence database providers use people cloistered in cubicles to read articles and pick out names of potential interest to AML analysts. Enough people cannot be hired and trained to read the vast amount of information produced globally each day.

As for search engines, we discussed the implications secret, well-guarded algorithms have on finding information someone wants to hide. That information cannot be hidden from TransparINT. If negative news is buried on page 10, 20 or 100 of the search engine results, TransparINT finds it and puts it on page 1 of what our users see.

2. TransparINT provides Real Time up-to-the second results to its users.

Contrast that with risk intelligence databases where there are delays of days, weeks, and even months between when negative news information first becomes public and when it is entered onto a list. Needing people to find the information, read it, analyze it, draft a written summary, type that into a database and have a supervisor approve the content takes time. TransparINT doesn't need this time to make the source information available to our users. It is available the moment it enters the public domain. And we trust that our users, AML and compliance professionals, can decide what is important to them.

3. Greater Accuracy and Relevance: TransparINT returns only results related to AML and financial crime risk and presents the most relevant right at the top.

Using KYC due diligence search techniques honed over 20 years of operations, TransparINT's team of developers has programmed the industry's best practices into every search.

Each result has posted with it a relevancy score denoting the likelihood of its relation to the search. Those results with the highest relevancy score are displayed right at the top. Intuitive user interface design enables the analyst to see instantly why the result matters.

EFFECTIVE SCREENING FOR NEGATIVE NEWS

4. Confidence: That when nothing is found, there really is nothing to find.

The most common result of negative news research is that no results are found.

Unfortunately however, analysts are left wondering if that is really the case. “Did I miss something somewhere?” is their thought. So they keep re-doing the search, going to more applications or more search engines. This takes time and slows down work. With TransparINT the absence of results doesn’t mean absence of confidence.

5. Consistency: TransparINT raises the performance of all analysts to the level of the best.

There are always a small handful of KYC analysts who are able to find things others miss. They have figured out how to get more from the applications they use. These analysts are the best. Now imagine if every KYC analyst performed at that same level? That is what TransparINT enables.

No longer do AML managers have to wonder why one analyst can find information that others cannot. No longer are there “tricks of the trade” that must be discovered and passed around among analysts as they chat over lunch. No longer do AML officers need to worry about what happens when that best analyst is recruited away by another bank.

6. Easy to Use: Anyone who knows how to use the internet can use TransparINT after just a few minutes of familiarization.

There is no need to integrate a database with a client’s technology architecture. User name, password and access to the internet is all that is needed for users to begin performing searches.

There is no new work-flow or processes that must be added to the KYC procedure.

Find a result that needs to be included in the file? Tick a box selecting the items to include, and a report is generated that can be exported to a file or integrated into an existing case management system. The best way for our users to capture what is needed, is the way *they* want it captured. TransparINT makes capturing results easy.

7. Speed and Cost: With greater accuracy, consistency with every search, and confidence that each search has scoured the most up-to-the minute public information, analysts can move faster. Speed reduces time and this reduces cost.

Claims of better compliance at less cost are questionable. We invite you to see if ours is valid.

8. Proof: TransparINT provides a complete record of every search, when it was conducted, who conducted it, and all the results.

Here is a situation many AML officers and analysts find themselves in: An auditor or regulator is reviewing due diligence files. They begin to question how the adverse media and public record searching was done.

EFFECTIVE SCREENING FOR NEGATIVE NEWS

“Which system was used?” “What was found?” “Why isn’t this article that I just found included?” “Can we speak with the analyst who did this work?”

Anxiety grows, heart beats faster: “Are we going to get criticized?” “Is this a finding?” “Will it be in the written report?” “Will they want to keep looking at more files now?” “What will they find in those files?”

With TransparINT there is no longer the need for lengthy conversation with an auditor or regulator about what “search terms” or “search strings” were used, why one analyst found something and another did not.

TransparINT also provides a valuable feature which allows the auditor or regulator to recreate the search as if it were being done on the exact day the analyst performed the original search. They will be able to confirm that the information in the file was the information presented that original day months earlier.

9. Management and Tracking:

TransparINT lets managers keep track of all the searches and search results of every member of their team.

No more wondering which databases and search engines were used. No more wondering if one of those 80 articles returned had useful information and if the analyst found it. No more wondering if every analyst, on every search used the right key words or search strings. No more hitting “print screen,”

copying and pasting to prove there were “no results found.”

See how many searches were completed, by whom, when, and track work trends among the AML team. Print reports for management, auditors, and the regulators.

Know more about your customers and also know more about your own team’s work.

10. Security: TransparINT provides greater security to its users than do search engines.

When an AML analyst uses a search engine to find information and then clicks on links, they have just transmitted a lot of information about their institution to that end site. That end site now knows that your institution is looking at them and knows what specifically you are looking at. It records this information and makes use of it.

Search engines also make use of it. Some search engines and the end sites have the ability to sell this information (legally) to all sorts of places like marketing firms, business intelligence services and data analytics companies. That doesn’t sound very secure.

TransparINT doesn’t do any of that. When using TransparINT’s Results Analysis Tool, the platform actually builds a wall between our users and the site from which they are getting information, so these sites do not know which institution is looking at their content

Negative News Approaches: A Comparison

Features	<i>TransparINT</i>	Risk Intelligence Database	Archived News Database	Search Engine	Business Reporting Service	Watch List Screening
Web Search Results	✓	X	X	✓	X	X
Real Time Results	✓	X	X	✓	X	X
Archived News	✓	X	✓	✓	X	X
Ranking Results for AML Risk Specifically	✓	✓	X	X	X	✓
Watchlist & Sanction Searches	✓	✓	X	X	X	✓
Built specifically for AML	✓	✓	X	X	X	✓
Audit Control	✓	X	X	X	X	✓
Management Reporting Features	✓	X	X	X	✓	X
Current Politically Exposed Persons (PEPs)	✓	✓	X	X	X	X
Past PEP and Related Parties	✓	✓	X	X	X	X
3 rd Party Implementation Needed	NO	YES	NO	NO	NO	YES
Privacy Protection	✓	X	X	X	X	n/a
Integrate with Case Management System	✓	✓	✓	X	✓	✓
Management Dashboards	✓	X	X	X	✓	✓

Improve Negative News Searching and Strengthen AML Compliance

Traditional risk intelligence databases and watch list screening applications fail to identify and retrieve all relevant information needed to properly understand risk posed by customers, prospects, counterparties, and vendors. Existing providers search only a tiny amount of available data, rely on outdated manual human review processes, and are unable to keep pace with the constant flow of new information entering the public domain.

Conventional KYC applications have not changed for nearly 15 years. Why has innovation changed every aspect of our lives, but barely touched AML, and in particular barely touched how negative news risk is found?

During these past 15 years, AML practitioners have had a false sense of comfort that they were using tools that would uncover KYC risk. Everyone was using the same tools, learning tricks of the trade, hoping it all worked out. It hasn't. TransparINT has now changed that.

TransparINT provides what other applications do not. TransparINT provides confidence that important adverse media information will be found. AML officers and senior management can be confident they are adhering to the letter and spirit of AML law and regulation.

Learn more about TransparINT at www.transparint.com.