

MAJOR ENHANCEMENTS IN AML/CTF COMPLIANCE
AND OTHER RELEVANT DEVELOPMENTS

AS PrivatBank



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PROFILE OF THE BANK

Brief description of the bank

AS "PrivatBank" is a Latvian credit institution which was established in 1992 and currently is the 14th largest Latvian bank (by assets, on March 31, 2017). It is represented in the country via 13 branches located both in the capital and in the major regions.

Credit rating, if obtained on bank itself or financial instruments issued and/or enlisted

Not rated.

Major business lines

Corporate banking, retail business.

Turnover (% of total turnover) with shell companies

In 2016 the turnover of the companies classified as shell companies was approximately 20% (compared with 2015). In 2017 the turnover continued to decline reaching 15% of the total turnover.

Structure and profile of shareholders

Shareholders structure on 30.06.2017.

Shareholder	Shares, EUR	Capital shares, %
PAS "PrivatBank"	40,190,855	46.54%
Concorde (Bermuda) Limited	7,967,355	9.23%
Wadless Holdings Limited	4,894,085	5.67%
Unimain Holdings Limited	4,566,475	5.29%
Danig Limited	3,000,000	3.47%
Chastely Investments Limited	2,338,098	2.71%
Minority shareholders	23,392,688	27.09%
Total	86,349,556	100.00%

RESHAPING OF THE BUSINESS MODEL IF AML/CTF COMPLIANCE DETERMINED (noteworthy, visible and impactful)

Reduction of dependency of transactional (payments) business line

Compared to 2015, the number of USD payments in 2016 decreased by 25% while the EUR payment number remained stable. In 2017 the number of USD payments

continued to decline, and comparing the second half of 2016 to the first half of 2017, the number of USD payments has declined by more than 50% in total. In turn, the number of EUR payments has slightly increased over the same period (by about 5%).

Diversification of lines of business/business lines to be developed in reshaped business model

Further development of corporate and retail services for the domestic market as well as selected international customers.

Reduction of turnover with shell companies

Turnover of companies classified as shell companies in 2016 decreased by 80% (compared to 2015). In the first half of 2017, the turnover continued to decrease (by 5%, reaching an 85% decrease compared to 2015).

Remediation actions subject to regulatory enforcement measures by FCMC, if applicable

In 2016 the Bank developed an action plan (which was coordinated with the FCMC) to improve the effectiveness of internal control system and AML Policy. The Action plan has been completed in full extent.

Projections, figures proving sustainability of the business model in upcoming 3 years if turnover with shell companies reduced significantly

The Bank will continue developing the domestic corporate and retail services further and continue servicing selected international customers that fit the set criteria.

CORPORATE GOVERNANCE

Development of new policies and procedures

The Bank has implemented high business ethics standards throughout the banks policies and procedures and the attitude of employees. Additionally, the Bank fully reviewed and updated internal policies and procedures in 2016.

Financial sanctions (UN, EU, national) compliance policy

A dedicated sanctions compliance program was created by the Bank in 2016. The relevant processes have been put under one umbrella (a single and comprehensive policy) in order to manage the sanctions risks. The area is managed by a certified Sanctions Officer. Additionally, the Financial Crime Risk Management tool provided by Fiserv Inc. was implemented to strengthen the capacity of the Bank to mitigate sanctions risks (online and offline screening of customers and payments).

OFAC adherence policy

The Bank fully adheres to OFAC sanctions regimes that are an inseparable part of financial sanctions risks management.

Increased transparency (improved quality of information provided in payments, publicly available reports on compliance etc.)

The Bank is making sure that the payments

made are transparent and the economic reason of the underlying transaction raises no doubt (the relevant documents are requested from customers). Additionally, the Bank has set transaction limits that allow the Bank to have control over the payment flow. Several improvements have been made to ensure that the information provided with the payment is accurate and sufficient.

Strengthened management and/or supervisory function (new employees, reporting lines etc.)

Regardless of the Bank customer number decrease the AML unit had a 35% increase in the staff number in 2016 compared to 2015. A strong AML management team structure was created by hiring experienced employees. The Head of AML is supported by experienced team leaders each of whom is in charge of defined AML areas (including a dedicated Sanctions Compliance Officer).

Additionally, AML staff adequacy calculation methodology has been implemented at the Bank that allows the Bank to manage flexibly the resource adequacy (should the capacity thresholds be exceeded adequate resources will be allocated).

Designated Sanctions officer (function)

A Sanctions Compliance Officer position was created in 2016.

INTERNAL CONTROLS

Structural changes

The Bank has implemented the three lines of defence principle, where the first line is business and support units, the second one is the AML unit, Risk Director, Risk Control unit and Compliance unit, and the third one is the internal audit.

Changes in KYC/CDD/EDD/PEP/Financial Sanctions monitoring

The due diligence and enhanced due diligence requirements have been strengthened by implementing more rigorous scrutiny and documentation requirements as well as automated solutions for monitoring and online screening purposes – Financial Crime Risk Management tool provided by Fiserv Inc. Automated PEP screening has been fully implemented (at on boarding and during relationship).

Changes in on-boarding policies and procedures, including, on-barding via agents

The Bank has implemented stricter on boarding procedures, especially in respect of international customers who must correspond to the transparency requirements set by the Bank.

TRAINING OF THE STAFF

Focused training provided in 2016

The internal AML training is done at least once annually for all employees. Tailored trainings are provided to the management board as well as business and support units on an ad hoc basis. Moreover, international sanctions trainings are organized (in addition to the general AML trainings).

External/internal training

All employees have been trained by completing internal AML training. External AML training has been completed by 62% of Bank's employees pursuant to the training plan of the Bank (all lines of defence represented, including customer service managers and employees of internal audit).

On-going testing and certification

The Bank has approved a training plan which clearly defines which employee categories need to be trained. Mandatory external trainings are also included in the plan focusing primarily on the AML staff.

INDEPENDENT TESTING

US consultants independent testing outcome

In 2016 an outsourced independent US consultant, NAVIGANT, carried out the audit of the AML area. Based on Navigant's report, the Bank prepared an action plan to eliminate the identified shortcomings.

Level of implementation of independent testing recommended elements

Currently, the Bank is going to fulfil the NAVIGANT's recommendations till the end of 2017 / beginning of 2018.

Further plans for validation of implementation of remediation plans

In 2017 external consultant will carry out AML audit (focusing on the testing of the correctness of the operation of the Bank's AML systems). Moreover, NAVIGANT is going to carry out a repeated audit in the beginning of 2018.

Internal audit function ability to carry on independent testing in the field of AML/CFT

Internal Audit has planned regular audits in 2017 which include AML area audits (a part of which is AML IT system testing). A dedicated AML auditor is now a part of the audit team.

Any other external audits, outcomes

In 2016 several external audits were carried out in the AML area (including testing of the AML IT area). The audit was carried out by PricewaterhouseCoopers and the outcome of the testing was satisfactory.

AUTOMATED SYSTEMS AND TOOLS

Concise description of IT systems, changes (upgrades) in 2016

Financial Crime Risk Management tool provided by the external provider Fiserv Inc., Siron KYC and Siron AML – scoring tools provided by the company FICO TonBeller.

Core banking system: name/ supplier

PROMIN, Technical development of PrivatBank. The Bank started the implementation of a new core banking system, Temenos 24, the first stage of implementation is to be finished by the end of 2018.

AML/CFT monitoring system: name/ supplier

Financial Crime Risk Management tool provided by the external provider Fiserv Inc.

Sanctions screening system: name/ supplier / online 24/7 or T+1/2/3

Financial Crime Risk Management tool provided by the external provider Fiserv Inc. (both online real-time payment screening and offline overnight batch screening).

Other databases

Dow Jones Risk & Compliance database provided by Dow Jones Inc. and data provided by Accuity Inc.

Closed gaps, improved effectiveness, particularly in management of international financial sanctions

Sanctions screening has been improved in 2016 by implementing the Financial Crime Risk Management tool provided by the external provider Fiserv Inc. Furthermore, additional processes have also been implemented to enhance the controls regarding dual use/military goods.

DE-RISKING OF CUSTOMERS AND BUSINESS LINES

Business lines exited

No lines exited.

De-risked customers

Systematic de-risking was started in 2016 and led to a drastic decrease of international customers (see the shift in customer base below).

Shift in customer base by jurisdiction

The decrease on the international customers side has been 88% and on the domestic resident customers side – 1%.

Changes in number of PEP customers

Compared to 2015 and 2016, the number of politically significant persons in 2017 has increased slightly (approximately about 5%). Despite the fact that the concept of a local politically significant person was introduced in Latvia, in 2016 the number of customers which are politically significant persons did not increase considerably as the business relations were terminated with a significant number of foreign politically significant persons, however no increase in the number of local politically significant people was observed.

Reduction of AML/CFT risk level (scoring) among customers

The number of customers subject to enhanced due diligence has decreased and fallen from 9,706 in 2015 to 6,856 at the end of 2016. There have been no crucial changes in 2017, since the Bank does not collaborate with customers that pose overly high AML risk.

Target markets

Latvia, EU and CIS countries.

Trends in customers' structuring of their assets (for example shift from short term assets to longer term assets, move from transactions to placement of longer term assets for management etc.)

Most of the Bank's customers invest their funds in long-term deposits (the Bank offers competitive services) in 2016, a significant activity of local depositors was observed (increased by 28%). In 2017 the situation remained at the same level.