

REPORT

on the Results of the Horizontal Inspection of Money Laundering, Terrorism and Proliferation Financing and Sanctions Risk Assessment Process Including Methodology¹

¹ Please, note that originally Latvijas Banka has prepared the Report in Latvian. The English version of the Report has been prepared by a third-party service provider. In case of any discrepancies between the Latvian and English version of the Report, the Latvian version shall prevail.

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I. Summary

The Inspection was performed with an aim to assess one of the elements of the Institutions' AML/CTPF and sanctions risk management ICS, i.e. the process of ML/TPF risk assessment, including, methodology, and to identify good and bad practice examples. The Inspection was carried out in 17 Institutions – in all credit institutions registered in Latvia and all branches of the EU Member States' credit institutions registered in Latvia, as well as four non-bank institutions which have the most significant influence on the non-banking sector both in terms of their mode of operation and size and ML/TPF and sanctions risk. Conclusions of the Inspection were based on the analysis of information provided by the Institutions as effective on 1 August 2022, i.e. the Institutions' answers to previously defined questions about the assessment of ML/TPF and sanctions risk, internal regulations of the Institutions, which define the methodology of ML/TPF and sanctions risk assessment, as well as the latest ML/TPF and sanctions risk assessments of the Institutions were assessed (for more information about the scope of the Inspection refer to the Section II of the Report). As a result of the Inspection examples of good and bad practice that were identified in the practises of Institutions have been determined. Findings of the bad practice examples are based solely on the analysis of the said restricted amount of information, and due to the horizontal character of the Inspection identified findings were not verified with the relevant Institutions where the bad practice examples were found.

Publishing a collection of anonymous examples of good and bad practice was determined as one of the follow-up measures of the Inspection. The aim of publishing the Report is to inform all participants of the financial and capital market about the examples of good and bad practice in terms of ML/TPF and sanctions risk assessment. The participants of the financial and capital market are called to assess whether their practice complies with good and bad practice examples and to take measures to improve their risk assessment process, considering details of the Report.

Overall, during the Inspection it was concluded that the Institutions have a high-level expertise in identifying and assessing ML risk. The key shortcomings observed during the Inspection pertained to the identification and assessment of PF, TF, and sanctions risk. Considering the above, as well as the significant influence of the recently imposed sanctions on Russia and Belarus and interests of the financial and capital market in general, it is important to implement measures that are necessary to increase the Institution's awareness in identifying and assessing the sanctions risk, as well as PF and TF risks. Furthermore, the Inspection revealed that a part of the Institutions was not compliant with the legislative framework that with sufficient clarity lays down basic requirements

for the assessment of ML/TPF or sanctions risk (for example, regularity and requirements for updating risk assessment etc.). The most important examples of the bad practice examples and assessment thereof are included in the table below (for all identified good and bad practice examples refer to the Section III of the Report).

| Report's Section No. | Finding | Impact of a Finding ² |
|----------------------|--|----------------------------------|
| 1. | General Aspects of the Institution's ML/TPF and Sanctions Risk Assessment Methodology and Risk Assessment | |
| 1.1 | The ML/TPF and Sanctions Risk Assessment Methodology | |
| 1.1.1 | An Institution has not prepared such ML/TPF and sanctions risk assessment methodology that would be appropriate for the specific activities of the Institution | Very high |
| 1.1.1 | The risk assessment methodology is too general | High |
| 1.1.2 | The frequency for updating the ML/TPF or sanctions risk assessment methodology does not conform to the statutory requirements | High |
| 1.1.3 | The efficiency of the ML/TPF or sanctions risk assessment methodology has not been assessed | High |
| 1.2 | The ML/TPF and Sanctions Risk Assessment | |
| 1.2.1 | The frequency for updating the sanctions risk assessment does not conform to the statutory requirements | High |
| 1.2.1 | The frequency for updating the ML/TPF or sanctions risk assessment is not appropriate to the Institution's inherent risks | Medium |
| 1.2.1 | Risks throughout the entire risk assessment period are not being assessed | High |
| 1.2.2 | An Institution has not updated the sanctions risk assessment after new sanctions regimes against Russian and Belarus, which directly impact the Institution, were introduced | Very high |
| 1.2.2 | The ML/TPF or sanctions risk assessment has not been updated upon occurrence of such circumstances that require reviewing the ML/TPF or sanctions risk assessment | High |
| 1.3 | Parties Involved in the Development of the ML/TPF and Sanctions Risk Assessment Methodology and Conducting the Risk Assessment | |
| 1.3.1 | Institution's role in the risk assessment conducted by or with | Medium |

²The finding that was identified as an example of bad practice was identified for its potential impact on the Institution's risk management system, risk control and Institution's management. The impact was scored as conforming to one of the following levels – very high, high, average or low. The score was allocated on the basis of the nature of the very finding identified as the bad practice rather than the number of Institutions where that finding was identified.

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| | the assistance of an independent third party is not clear | |
| 1.3.2. | Training directly related to ML/TPF or sanctions risk assessment is not provided | Medium |
| 1.4 | IT Solutions and Quality of the Data Used in the Risk Assessment | |
| 1.4.1 | An Institution does not have the data necessary for conducting ML/TPF or sanctions risk assessment or data format is not appropriate | High |
| 1.4.1 | There are no requirements laid down on how to ensure data quality during the risk assessment process | Low |
| 2. | The Elements of the ML/TPF and Sanctions Risk Assessment Methodology | |
| 2.1 | The Assessment of Inherent ML/TPF and Sanction Risk | |
| 2.1.1 | The inherent sanctions risk is not assessed | Very high |
| 2.1.1 | The inherent ML/TPF or sanctions risk assessment is not based on or is insufficiently based on the analysis of the Institution's quantitative data | High |
| 2.1.1 | The level of the inherent risk is assessed solely based on the exposure of the relevant risk in the Institution, without considering the nature of the risk | High |
| 2.1.2 | The PF risk is not assessed at all or is assessed insufficiently | Very high |
| 2.1.2 | The TF risk is not assessed at all or is assessed insufficiently | Very high |
| 2.1.3 | The Sanctions risk assessment does not cover the sectoral sanctions risk or covers it insufficiently | Very high |
| 2.1.4 | The impact of sanctions imposed by the Member States of the EU and NATO is not assessed | High |
| 2.1.5 | The sanctions risk related to the region where the Institution operates and provides services is not assessed | High |
| 2.1.5.1 | The assessed customers' risk factors are not appropriate to the Institution's customer base | High |
| 2.1.5.1 | The risks posed by the type of customer's business activities are not identified and assessed or are assessed insufficiently | High |
| 2.1.5.2 | The payment flow from and to high risk jurisdictions are not assessed | High |
| 2.1.5.2 | Not all factors linking a customer with a certain jurisdiction are considered | High |
| 2.2 | The Assessment of the Efficiency of Controls for Managing ML/TPF and Sanctions Risk | |
| 2.2 | The operational efficiency of controls is not assessed or is assessed insufficiently | High |

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| 2.2 | Assessment of controls does not provide sufficient insight into whether the controls are able to efficiently mitigate the inherent risk of an Institution | High |
| 2.2 | An Institution assesses the efficiency of controls only for those ML/TPF risk factors which are scored as having high inherent risk | High |
| 2.3 | The Assessment of the Residual ML/TPF and Sanctions Risk | |
| 2.3 | The procedure for the residual ML/TPF or sanctions risk assessment is not determined | Medium |
| 2.3 | The Institution's residual ML/TPF or sanctions risk is not assessed | Medium |
| 3. | The Results of the Institutions' ML/TPF and Sanctions Risk Assessment and the Action Plan for Risk Management or Mitigation | |
| 3.2 | Using the Results of the Risk Assessment in Various Processes of the Institution | |
| 3.2 | The results of the sanctions risk assessment are not used to improve the ICS of sanctions risk management | Very high |
| 3.2 | The Risk assessment results are not used to manage or determine the risk appetite | High |
| 3.3 | Informing the Involved Parties about the Results of the ML/TPF and Sanctions Risk Assessment | |
| 3.3 | The involved parties are not being informed about the results of risk assessment or the procedure of informing the involved parties is not determined | Medium |
| 3.4 | The Action Plan for Risk Management or Mitigation | |
| 3.4 | A requirement to prepare an action plan for risk management or mitigation as a result of the Institutions' ML/TPF and sanctions risk assessment has not been determined | High |
| 3.4 | Risk management or mitigation plan has not been prepared | High |

II. The Aim and Scope of the Inspection

On 8 February 2022, the Commission³ started the off-site horizontal inspection "The Horizontal Inspection of Money Laundering Terrorism and Proliferation Financing and Sanctions Risk Assessment Process Including Methodology". Given the geopolitical situation, the Commission adopted a decision in April 2022 to postpone the Inspection for a certain time, i.e. to Q1 of 2023.

The goal of the Inspection was to assess the supervised Institutions' ML/TPF and sanctions⁴ risks assessment process, including methodology, that is used to identify, assess, understand and manage ML/TPF and sanctions risk inherent in the activities and customers of the Institutions, and to identify examples of good and bad practice. The Inspection was performed in all credit institutions registered in Latvia and all branches of credit institutions of the EU Member States in Latvia. Additionally, the Inspection was performed in certain investment institutions, in certain payment institution and certain electronic money institution which has the most significant influence on the non-bank sector in Latvia both in terms of their type of activity and size, and also ML/TPF and sanctions risk. Altogether, the Inspection was performed in 17 Institutions.

The Inspection results are based on the statutory provisions in force during the period of the Inspection, recommendations of Latvijas Banka as well as internationally recognised recommendation related to the ML/TPF and sanctions risk assessment process and based on the analysis of the following information and documentation submitted by the Institutions as effective on 1 August 2022:

- a) answers provided by the Institutions to certain questions regarding the ML/TPF and sanctions risk assessment;
- b) internal regulations submitted by the Institutions which define the methodology of ML/TPF and sanctions risk assessment;
- c) the latest reports of ML/TPF and sanctions risk assessments performed by the Institutions.

III. Assessment of the Inspection results

This Section of the Report provides the overall results of the Inspection and analysis, which includes the examples of good and bad practice identified in

³ Starting from 1 January 2023, the Commission was integrated into Latvijas Banka, and pursuant to Paragraph 4 of the Transitional Provisions of the Law on Latvijas Banka, Latvijas Banka takes over the property, funds, rights and obligations of the Commission.

⁴ For the purpose of the Report, the sanctions are restrictions imposed on the sanction subjects adopted according to the Sanctions Law, and sanctions determined by a Member State of the EU or NATO identified pursuant to Points 15 and 16 of Regulation No 126.

Institutions' practises for ML/TPF and sanctions risk assessment. As well as this Section of the Report contains requirements determined in the statutory regulations and recommendations. In the following of this Section there will be examples of good practice that were identified in the practises of Institutions and that in the opinion of Latvijas Banka meet the requirements provided for in the statutory regulations and international recommendations regarding an efficient prevention of ML/TPF and sanctions risk. It must be taken into account that the ML/TPF and sanctions risk assessment must correspond to the type and extent of activity of each Institution, and that not all examples of good practice can be attributed equally to all Institutions without individual assessment.

Additionally, this Section of the Report contains examples of bad practice identified in the Institutions during the Inspection which, in the opinion of Latvijas Banka, do not conform to the requirements laid down in the statutory regulations or international recommendations. A collection of the examples of bad practice identified during the Inspection are included in the Annex II "Table of Horizontal Inspection Results" of the Report.

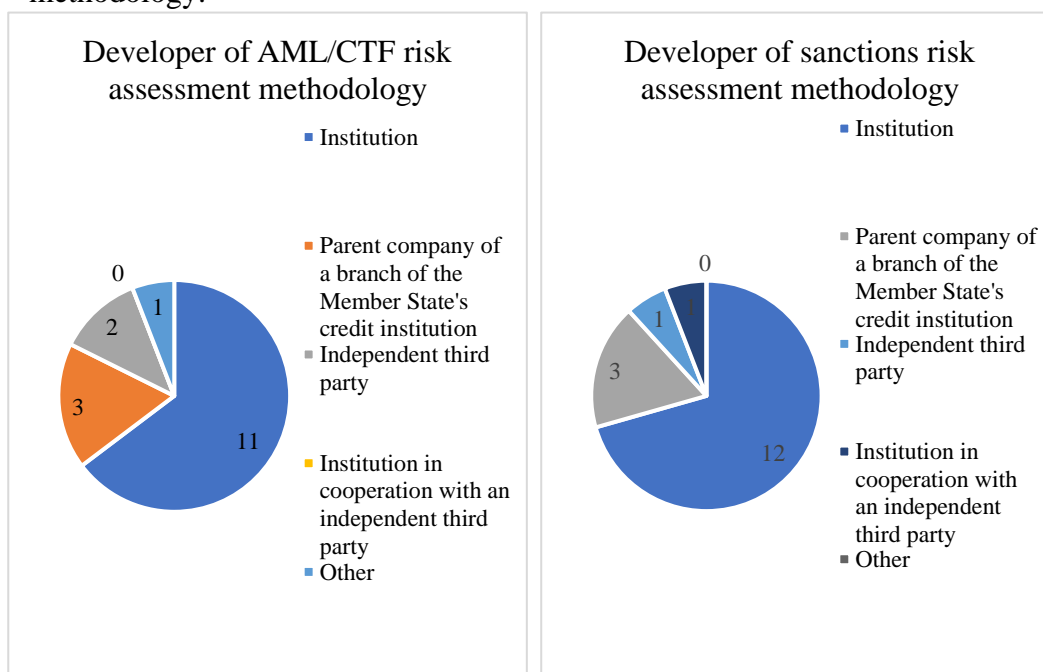
1. General Aspects of the Institution's ML/TPF and Sanctions Risk Assessment Methodology and Risk Assessment

Section 6 of the AML/CTPF Law states that the Institutions, according to the type and extent of operation, must perform and document ML/TPF risk assessment in order to identify, assess, understand and manage the ML/TPF risk inherent in their activities and customers, and, on the basis of that assessment, create the ICS of AML/CTPF, including elaborate and document relevant policies and procedures confirmed by the Institution's management, if applicable, or the highest management body of the Institution. The AML/CTPF Law lays down the minimum requirements for the risk assessment, its frequency and conditions for updating the risk assessment.

Meanwhile, pursuant to Section 13.¹ of the Sanctions Law, the Institutions are obliged to perform and document, according to the type of their activity, an assessment of international and national sanctions risk in order to identify, assess, understand and manage the international and national sanctions risks inherent in their activities or customers. On the basis of that assessment, the Institutions shall create the international and national sanctions risk management ICS, including elaborate and document relevant policies and procedures.

1.1. The ML/TPF and Sanctions Risk Assessment Methodology

The Inspection established that 16 out of 17 Institutions being inspected had the methodology of ML/TPF and sanctions risk assessment in place. One Institution pointed out that it uses a risk assessment tool developed by ACAMS, therefore the Institution does not have a separately documented ML/TPF and sanctions risk assessment methodology. The following charts provide information about the party who developed Institutions' ML/TPF and sanctions assessment methodology.



During the Inspection it was observed that risk assessment methodologies which were developed by an independent third party had significant shortcomings. However, significant shortcomings were identified also in a number of risk assessment methodologies that were developed by the Institutions themselves or their parent company. Therefore, it cannot be certainly concluded that the quality of the methodology depends directly on the fact that it has been developed by the Institution, independent third party or Institution's parent company.

Example of good practice

An Institution has a common ML/TPF risk assessment methodology at the group's level

The Institution has developed a common ML/TPF risk assessment methodology at the group level, which determines the requirements for risk assessment. At the same time the group level methodology stipulates that compliance with the national legislative or other individual circumstances may allow the Institution to

determine a deviation from the group level methodology at the national level. The methodology contains a certain order, according to which the deviations from the group level methodology can be determined.

Example of bad practice

An Institution has not prepared such a ML/TPF and sanctions risk assessment methodology that would be appropriate for the specific activities of the Institution

The Institution uses a standardised tool developed by ACAMS to assess AML/CTF and sanctions risk, which cannot be adjusted to the specifics of the Institution's activity, therefore the Institution is not able to identify and assess the risks in a way that is appropriate for the Institution's type and extent of activity. Additionally, the tool does not cover TF and PF risk.

1.1.1. Documenting the ML/TPF and Sanctions Risk Assessment Methodology

Pursuant to Paragraph one of Section 6 of the AML/CTPF Law and Section 13.¹ of the Sanctions Law, the Institutions must create the ICS of AML/CTPF, including develop and document relevant policies and procedures. Paragraph one of Section 6 of the AML/CTPF Law states that the policies and procedures in the field of AML/CTPF shall be approved by the Institution's board, if applicable, or Institution's highest management body. Additionally, it is explained in Point 26 of the Guidance Manual that the Institutions need to elaborate and document a sanctions risk assessment methodology. It follows from the aforesaid that the Institutions are required to document ML/TPF and sanctions risk assessment methodology. According to the Wolfsberg's Guidelines, the methodology should have a sufficient level of detail and clarity⁵. Therefore, for an Institution to demonstrate compliance of its risk assessment with the requirements laid down in the AML/CTPF Law and the Sanctions Law, the methodology must be documented in such detail that the regulator and other stakeholders would have a clear understanding on how the Institution identifies and assesses ML/TPF and sanctions risk. Likewise, the EBA's Guidelines on ML/TF risk factors⁶ state that the Institutions should record and document their risk assessment, as well as any changes made to this risk assessment in a way that makes it possible for the Institution, and for competent authorities, to understand how it was conducted, and why it was conducted in a particular way.

⁵ Wolfsberg's Guidelines, p. 4. Available here: [- Anti-Money Laundering Risk Assessments FAQs \(2014\) \(wolfsberg-group.org\)](https://www.wolfsberg-group.org/anti-money-laundering-risk-assessments-faqs-2014)

⁶ EBA's Guidelines on ML/TF risk factors, Clause 1.4. Available here: [Guidelines on ML/TF risk factors \(revised\) | European Banking Authority \(europa.eu\)](https://www.eba.europa.eu/en/guidelines-on-ml-tf-risk-factors-revised)

In general, it can be concluded that all Institutions, except for the Institution mentioned in Article 1.1 of the Report, have their ML/CTPF and sanctions risk assessment methodology documented. The Institutions have different approaches in documenting the methodology, namely ML/TPF and sanctions risk assessment methodologies for a number of Institutions are separate documents that cover all terms related to the risk assessment. While for other Institutions different elements of the risk assessment methodology are included in various documents of the Institution (for example, AML/CTPF strategy, ML/TPF risk management policy and documents regulating powers and tasks of certain Institution's structural units). However, other Institutions do not have their methodologies documented separately and instead the risk assessment methodology is included in the risk assessment reports. It has been observed in the Inspection that Institutions who have documented risk assessment methodologies separately have documented the risk assessment process in greater detail and in general such methodologies provide a clearer understanding on how the risk assessment process is organised and conducted.

Example of good practice

An Institution has a clear, detailed ML/TPF risk assessment methodology and it provides a complete and comprehensive understanding of all the phases of assessing ML/TPF risk

The Institution has a clear and detailed ML/TPF risk assessment methodology and it provides a complete and comprehensive understanding of all the phases of assessing this risk, including but not limited on how the Institution identifies ML/TPF risk, the underlying principles and mathematical modules for assessing risk factors, the Institution's approach to identifying and assessing the efficiency of controls, including what internal and external information sources the Institution takes into consideration when assessing the controls and also how the Institution assesses the residual risk. The Institution's ML/TPF methodology is determined in a separate document with attached instructions and guidelines, which explain the applicable requirements in more detail, thereby promoting a consistent and uniform understanding and application of the requirements.

Examples of bad practice

A. The risk assessment methodology is not approved separately by an Institution's management

The risk assessment methodology is not provided in a separate document for several Institutions but is instead included only in the risk assessment report. Thus, the methodology is not approved individually by the management of the Institution before performing the risk assessment. The Institution's board (or other

governing body) approves the risk assessment methodology only together with the risk assessment report after conducting the risk assessment.

B. The risk assessment methodology is too general

Risk assessment methodology of some Institutions contains general requirements regarding ML/TPF or sanctions risk assessment. Therefore, methodology of these Institutions is too general to provide a sufficient understanding on how the assessment is performed by the Institutions. The mentioned finding was identified for all those Institutions, which did not have their methodology documented separately but rather had their methodologies included in the risk assessment reports. The mentioned finding had also been noticed for those Institutions, which had included the risk assessment methodology in various internal regulations of the Institution that generally govern the management of ML/TPF or sanctions risk.

For example, an Institution has determined in its internal regulations only general minimum requirements provided for in the AML/CTPF Law and the Sanctions Law (risk assessment regularity, risk categories to be assessed and other direct statutory requirements) regarding the ML/TPF and sanctions risk assessment. But more detailed requirements on how risks are identified and assessed by the Institution are determined on a general level for all risks that the Institution might be exposed to. Consequently, the requirements that would govern the method for identifying and assessing the ML/TPF and sanctions risk considering the specifics of these risks and their assessment are not provided in greater detail in the Institution.

1.1.2. Requirements for Reviewing and Updating the Risk Assessment Methodology

Pursuant to Point 11 of Paragraph one of Section 7 of the AML/CTPF Law and Point 8.1 of Regulation No 126, the Institutions must outline the requirements and procedures for regular reviewing of the functioning of policies and procedures according to changes in the laws and regulations or the operational processes of the Institutions, services provided thereby, governance structure, customer base or regions of operations thereof. Pursuant to Article 66 of Regulation No 227, the Institutions shall regularly, but not less than once a year, review and update policies and procedures for risk identification and management according to changes in the Institution's activities and external events affecting the Institution's activities. It follows from the mentioned provisions that the Institutions are obliged to define procedures for regular review of the ML/TPF and sanctions risk assessment methodology, which includes also requirements on frequency of review of the risk assessment methodology, circumstances under which the Institution reviews its methodology, a procedure for identifying those

circumstances, and for documenting and approving changes in the methodology, and parties in charge of the mentioned processes.

Generally, it was established in the Inspection that, even though the statutory framework lays down clear requirements on reviewing Institutions' policies and procedures, which include also the methodology of ML/TPF and sanctions risk assessment, large part of Institutions do not have minimum requirements stipulated in their internal regulations that follows from said legal provisions or the Institutions' determined requirements do not correspond the regulatory framework.

The Inspection additionally found that the frequency for reviewing the ML/TPF risk assessment methodology for some Institutions does not conform to the frequency for reviewing the Institution's ML/TPF or sanctions risk assessment. Such non-conformity could be explained with the different regulatory requirements governing the frequency for reviewing policies and procedures and frequency for reviewing ML/TPF and sanctions risk assessment. Meaning, the frequency for reviewing policies and procedures under Article 66 of Regulation No 227 is not less than once a year. Therefore, the majority of Institutions have defined the frequency of methodology review as not less than once a year. Meanwhile, the ML/TPF and sanctions risk assessment is mostly conducted with the frequency as laid down in Point 7 of the Guidance Manual, i.e. every 18 months.

Examples of good practice

A. Requirements for regular review of risk assessment methodology

An Institution's ML/TF risk assessment methodology requires the Institution to review the methodology on a regular basis. According to the rules of the Institution, the instructions and templates that are being used for risk assessment are reviewed constantly. To ascertain and identify that the Institution assesses the risk related directly to the Institution's business, both external and internal information sources are used, including all risk assessments of local level group companies are taken into consideration to assess whether the risks identified in one group's company can be attributed also to other companies of that group.

B. Frequency of risk assessment methodology review corresponds to the regularity of conducting the risk assessment

Frequency of review of an Institution's ML/TPF risk assessment methodology corresponds to the frequency of ML/TPF risk assessment, i.e. said activities are performed at least annually. Thereby, the Institution evaluates before each risk assessment whether the methodology requires for amendments or improvements due to the Institution's internal or external changes.

- C. An Institution identifies and indicates in its risk assessment report how the changes in the methodology affect a possibility to compare risk assessment results

The Institution in its ML/TPF risk assessment report has identified what kind of changes have been made to ML/TPF risk assessment methodology in comparison to previous ML/TPF risk assessment period. If some results of risk assessment cannot be compared to previous risk assessment results, given the changes in the risk assessment methodology, the Institution indicates this in the risk assessment report.

Examples of bad practice

- A. The frequency for reviewing ML/TPF or sanctions risk assessment methodology or circumstances which require reviewing the methodology are not determined

Some Institutions have not indicated in their internal regulations the frequency of review of ML/TPF or sanctions risk methodology or have not indicated some or all circumstances, under which the methodology must be reviewed according to the statutory framework.

Additionally, the Institution which uses ACAMS tool both for assessing ML/TPF and sanctions risk, while using the tool cannot ensure that ML/TPF and sanctions risk assessment methodology is reviewed at the frequency stated in Regulation No 227, as well as under circumstances stated in Point 11 of Paragraph one of Section 7 of the AML/CTPF Law or Point 8.1 of Regulation No 126.

- B. The frequency for reviewing the ML/TPF or sanctions risk assessment does not correspond to the frequency determined in Article 66 of Regulation No 227, i.e. not less than once a year

The frequency of review of ML/TPF or sanctions risk assessment determined in the internal regulations of some Institutions does not correspond the one stated in Article 66 of Regulation No 277, i.e. not less than once a year. Some Institutions have defined the frequency of review of their methodology – once in three years. Meanwhile, other Institutions have defined the frequency of review of their methodology – every 18 months.

Proposal for a follow-up measure

Latvijas Banka believes that it is not useful to determine in the statutory regulations such frequency of review of ML/TPF and sanctions risk assessment methodology that does not conform to the frequency of conducting risk assessment. Therefore, it is recommended to amend the regulatory framework to ensure such frequency of review of Institution's risk assessment methodology that

corresponds to the frequency of conducting a ML/TPF and sanctions risk assessment.

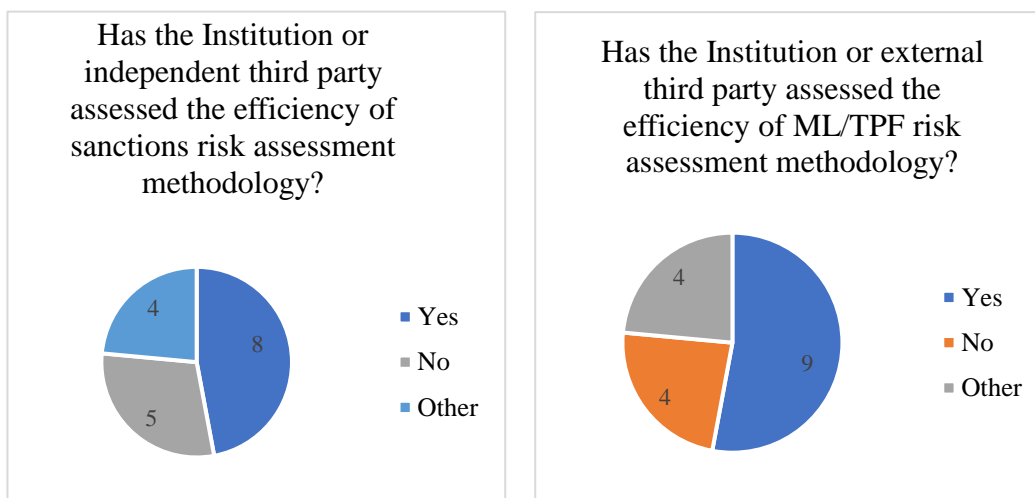
1.1.3. The Assessment of the Efficiency of ML/TPF and Sanctions Risk Assessment Methodology

Pursuant to Point 11 of Paragraph one of Section 7 of the AML/CTPF Law and Point 8.1 of Regulation No 126, the policies and procedures elaborated by the Institution form a part of Institution's ICS of AML/CTPF and sanctions risk management. Pursuant to Paragraph two of Section 8 of the AML/CTPF Law and Point 10 of Regulation No 126, the Institutions must assess the efficiency of ICS of AML/CTPF and sanctions risk management at least every 18 months. It follows from the aforesaid that the Institutions must review the efficiency of Institution's ML/TPF and sanctions risk assessment methodology on a regular basis. According to the EBA's Guidelines on ML/TF risk factors⁷, the risk assessment should help firms understand where they are exposed to ML/TF risk and which areas of their business they should prioritise in the fight against ML/TF. In order to ensure that the risk assessment serves the mentioned goal, the Institutions should ascertain that the method they are applying to identify and assess the risks is efficient and corresponds to the Institution's activities and requirements of regulatory framework.

Overall, the Inspection found that not all Institutions have performed the assessment of efficiency of ML/TPF or sanctions risk assessment methodology (for detailed information refer to the bad practice example in continuation). Institutions which market "other" option when answering to a question on the assessment of methodology's efficiency, stated that, for example, the existing risk assessment methodology has not been assessed for its efficiency, nevertheless it has been performed for previous version of the methodology; meanwhile other Institutions pointed out that they are currently conducting the efficiency assessment. Those Institutions which confirmed having conducted the efficiency assessment informed that the efficiency assessment was performed by the Institution's internal audit function, compliance control function, external auditor,

⁷ EBA's Guidelines on ML/TF risk factors, Clause 1.11. Available here: [Guidelines on ML/TF risk factors \(revised\) | European Banking Authority \(europa.eu\)](https://www.eba.europa.eu/en/guidelines/ml-tf-risk-factors-revised)

or alternatively, some Institutions pointed out that the efficiency assessment was performed only by the Commission.



Example of good practice

Both an Institution and an independent third party have assessed the efficiency of ML/TPF and sanctions risk assessment methodology

The Institution points out that both the Institution's internal audit function and independent third party have assessed the efficiency of ML/TPF and sanctions risk assessment methodology.

Example of bad practice

An Institution has not assessed the efficiency of the ML/TPF or sanctions risk assessment methodology

In some cases, neither the Institution nor an independent third party have assessed the efficiency of ML/TPF or sanctions risk assessment methodology. Some Institutions point out that the assessment of efficiency of ML/TPF and sanctions risk assessment methodology was performed only by the Commission in its on-site inspection. The mentioned Institutions do not indicate that the Institution or an independent third party would have additionally assessed the efficiency of the methodology. Pursuant to the previously mentioned regulatory framework, the Institution is obliged to ensure a regular assessment of efficiency of the methodology. Regulator's on-site inspections are not performed at a frequency demanded in the regulatory framework, and regulator's inspections do not always cover the review of risk assessment or covers only some part of this element. Therefore, it can be considered that these Institutions have not fulfilled the requirements for regular assessment of efficiency of ML/TPF and sanctions risk assessment methodology.

1.2. The ML/TPF and Sanctions Risk Assessment

1.2.1. The Requirements for a Regular Review and Update of the ML/TPF and Sanctions Risk Assessment

Pursuant to Paragraph one of Section 6 of the AML/CTPF Law and Section 13.¹ of the Sanctions Law, the Institutions, according to their type and extent of activity, shall carry out the risk assessment in order to identify, assess, understand and manage the ML/TPF and sanctions risk inherent to its activities and customers. Pursuant to Paragraph one of Section 8 of the AML/CTPF Law, the Institutions must review and update their ML/TPF risk assessment at least every three years. But according to Point 7 of the Guidance Manual, the credit institutions, considering their inherent risks, must update AML/CTPF risk assessment at least every 18 months. Meanwhile, pursuant to Point 9 of Regulation No 126, credit institutions, licensed payment institutions and electronic money institutions and their branches in the Member States and third countries shall review and update their sanctions risk assessment every 18 months, meanwhile other market participants supervised by Latvijas Banka shall carry out the risk assessment every three years.

The statutory regulations require the Institutions to develop such ICS of AML/CTPF and sanctions risk management which is appropriate to the type, extent and inherent risks of Institution's type of activity. Besides, the legislation lays down the minimum requirements regarding the frequency of review and updating the risk assessment. It follows from the mentioned statutory regulations that the Institutions have an obligation to determine such frequency for reviewing and updating the risk assessment that would be appropriate to the type, extent and risks inherent to the Institution's activities.

In addition, it follows from the mentioned statutory obligations that in order for the Institution to identify, assess and understand what risks it is exposed to, the risk assessment performed by the Institution must cover such period that corresponds the frequency of the risk assessment. Namely, the period of quantitative and qualitative data analysed in the risk assessment should match the frequency of the risk assessment. Thereby the Institution can ensure a complete identification and assessment of all the risks inherent in the Institution. For example, if the Institution conducts risk assessment every 18 months, data (for example, customer data, transaction data etc.) used by the Institution to identify and assess the risk factors should cover a period of 18 months. Meanwhile, the assessment of risk mitigation measures or controls should reflect the actual situation on the moment of risk assessment.

Overall, it has been concluded in the Inspection that even though the regulatory framework sets forth clear requirements regarding the frequency of performing

ML/TPF and sanctions risk assessment, some Institutions perform ML/TPF and sanctions risk assessment less frequent than required by the regulatory framework or the Guidance Manual (for detailed information refer to bad practice examples in continuation). Additionally, it has been concluded that certain Institutions in their internal regulations have determined such frequency for conducting ML/TPF and sanctions risk assessment, which does not appropriate to the inherent risks of the Institution, even though it is compliant with the requirements of statutory framework.

Example of good practice

The frequency for a regular review and update of the ML/TPF or sanctions risk assessment determined by an Institution is appropriate to the inherent risks of the Institution

A large part of the inspected Institutions have determined that the ML/TPF or sanctions risk assessment is performed at least annually. Even though the Institutions are not legally obliged to perform the ML/TPF and sanctions risk assessment at such frequency, the determined frequency of risk assessment is considered appropriate to the ML/TPF and sanctions risk inherent to the Institutions. The said good practice has been identified not only in credit institutions or branches of EU credit institutions in Latvia. Additionally, a non-bank institution has determined in its internal regulations that its ML/TPF risk assessment should be reviewed and updated at least every 18 months even though the statutory framework permits the non-bank institution to perform the risk assessment at least every three years.

Examples of bad practice

- A. The frequency for a regular review and update of the sanctions risk assessment does not correspond to the one indicated in Point 9 of Regulation No 126

Some Institutions bound by the obligation to review their sanctions risk assessment at least every 18 months under Point 9 of Regulation No 126, have determined in their internal regulations that the frequency for regular review of the sanctions risk assessment is at least every three years.

- B. The frequency for a regular review and update of the ML/TPF risk assessment does not correspond to the one stated in the Guidance Manual

Some Institutions bound by the provision under Point 7 of the Guidance Manual have determined in their internal regulations that the ML/TPF risk assessment is reviewed and updated at least every three years, although it does not conform to the frequency for updating the risk assessment stated in the Guidance Manual.

- C. The frequency for a regular review and update of the ML/TPF and sanctions risk assessment is not appropriate to the risks inherent to an Institution

Regulation No 126 obliges the investment institutions to review the sanctions risk assessment at least every three years. According to the stated requirement, the inspected investment institutions had determined that the frequency for reviewing the sanctions risk assessment is at least every three years. However, considering the type of activities of these Institutions and the higher risks inherent to the Institutions, the frequency for reviewing the sanctions risk assessment determined by these Institutions does not correspond their inherent risks.

The Guidance Manual does not instruct that the investment firms and payment institutions should update their ML/TPF risk assessment more frequently than laid down in the AML/CTPF Law. According to the requirements of the AML/CTPF Law, the inspected investment institutions and the payment institution have determined that ML/TPF risk assessment must be updated at least every three years. However, considering the type of activities of these Institutions and the higher risks inherent to the Institutions, the frequency for reviewing Institutions' risk assessment is not appropriate to the risks inherent to the Institutions.

- D. An Institution does not assess risks throughout the entire period of the risk assessment

Certain Institutions do not assess risks for the entire ML/TPF or sanctions risk assessment period considering the Institution's determined frequency for reviewing the risk assessment. For example, one Institution conducts ML/TPF risk assessment every three years. In the latest risk assessment performed by the Institution only Institution's data for the period of Q3 of 2021 was analysed, and regarding the transactions data – the Institution had analysed in the risk assessment only transactions performed in Q3 of 2021. Similarly, another inspected Institution that conducts ML/TPF risk assessment every three years, carries out the risk assessment only for a period of 12 calendar months. Meanwhile, other Institutions who perform risk assessment every 18 months analyse data of 12 calendar months' period.

1.2.2. Reviewing and Updating the ML/TPF and Sanctions Risk Assessment under Certain Circumstances

Paragraph three of Section 8 of the AML/CTPF Law and Point 11 of Regulation No 126 list circumstances, under which the Institutions must perform ML/TPF or sanctions risk assessment and take measures to improve the ICS. According to

EBA's Guidelines on ML/TF risk factors⁸, the Institutions should put in place systems and controls to keep their assessments of the ML/TF risk associated with their business under review to ensure that their assessment of ML/TF risk remains up to date and relevant. In this regard, EBA points out that the Institutions must ensure to have systems and controls in place to become aware of emerging ML/TF risks and that they can assess these risks and, where appropriate, incorporate them into their risk assessments. It follows from the mentioned provisions that, in order to ensure fulfilment of the mentioned requirements, the Institutions should determine in their internal regulations a procedure and a responsible person for identifying those circumstances under which the ML/TPF and sanctions risk assessment should be reviewed. The Institutions also should incorporate in their internal regulations a procedure and responsible person for reviewing and updating the risk assessments.

For the Institutions to demonstrate compliance with the aforesaid statutory framework when circumstances listed in Paragraph three of Section 8 of the AML/CTPF Law or Point 11 of Regulation No 126, occur or the Institution plans to carry out the activities indicated in Paragraph three of Section 8 of the AML/CTPF Law or Point 11 of Regulation No 126, the Institution should evaluate how such circumstances will affect the ML/TPF and sanctions risk assessment and update the risk assessment, if needed. Meanwhile, if the Institution considers that there is no need to update ML/TPF or sanctions risk assessment under given circumstances, then the Institution should justify and document such conclusion to demonstrate compliance with the statutory regulations.

Furthermore, Point 11.3 of Regulation No 126 additionally stipulates that the sanctions risk assessment must be reviewed if the Institution has established that significant changes have taken place in the field of sanctions, for example, a new sanctions regime that directly affects the Institution has been introduced. Pursuant to Paragraph two of Section 2 of the Sanctions Law the Institutions shall comply with and implement EU sanctions. Considering the Regulations determined in Points 15 and 17 of Regulation No 126, the Institutions have to comply also with the sanctions imposed by the OFAC. Moreover, the Institutions must comply with sanctions imposed by the OFAC when performing transactions in any currency, not only in U.S. dollars. Additionally, some of the inspected Institutions point out that in their operation they observe also sanctions imposed by the UK and some other countries.

⁸ EBA's Guidelines on ML/TF risk factors, Clauses 1.6–1.10. Available here: [Guidelines on ML/TF risk factors \(revised\) | European Banking Authority \(europa.eu\)](https://www.eba.europa.eu/en/guidelines-on-ml-tf-risk-factors-revised)

In response to the war started by Russia in Ukraine in February 2022, as well as to the actions of Belarus that destroys or threatens the territorial integrity, sovereignty and independence of Ukraine, the EU, the USA, the United Kingdom and other countries have determined broad sanctions directed against Russia and Belarus, which have been extended repeatedly during the Inspection period. Even though individual sanctions against Russia and Belarus were in force since 2014 and even 2006, the sanctions imposed in February 2022 and months to follow are considerably more extensive. Besides, new, previously unseen types of sanctions have been introduced in 2022. The OFAC has additionally determined extensive sanctions against Russia and Belarus, which in many aspects differ from those imposed by the EU in terms of their content, thereby this creates additional challenges for the effective management of the sanctions risk.

In the opinion of Latvijas Banka, the said changes in the sanctions regime against Russia and Belarus are such that should be considered as significant changes that have a direct influence on the Institutions in the meaning of Point 13.1 of Regulation No 126. Therefore, Latvijas Banka is of the opinion that taking into account the requirements of the regulatory framework, the Institutions had an obligation to review and update their sanctions risk assessment as a response to the extensive sanctions imposed against Russia and Belarus in 2022. Furthermore, Latvijas Banka considers that once new sanctions packages against Russia or Belarus are introduced the Institutions should also assess the necessity to update the sanctions risk assessment and improve the ICS of sanctions risk management, depending on the scope of the introduced legislative changes.

However, during the Inspection it was concluded that neither of the inspected Institutions had performed such an update of the sanctions risk assessment until 1 August 2022, i.e. the date by which the Institutions provided the information requested in the Inspection. Though, some Institutions had performed a regular review of the sanctions risk assessment as of the mentioned date, which covered at least some months after 28 February 2022, and at least partially risks posed by the new sanctions' regimes (for detailed information refer to bad practice examples in continuation).

Example of good practice

An Institution had performed an *ad hoc* sanctions risk assessment after new sanctions against Belarus were introduced in 2021

After the EU and the OFAC introduced new sanctions against Belarus in 2021, the Institution performed the *ad hoc* sanctions risk assessment in order to evaluate the impact of the new sanctions on the Institution.

Examples of bad practice

- A. Certain Institutions have not updated their sanctions risk assessment after occurrence of material changes in the field of sanctions, i.e. imposition of the new sanctions' regimes against Russia and Belarus, which have a direct impact on the Institutions

Certain Institutions had not updated the sanctions risk assessment until 1 August 2022, the date by which the Institutions provided the requested information within the framework of the Inspection, on the basis of the fact that a new sanctions regime, which have a direct impact on the Institution, has been introduced. Some Institutions have performed the sanctions risk assessment in 2022, considering the regular frequency of the sanctions risk assessment laid down in the Institution's internal regulations, thus at least partially assessing also the risks related to the sanctions imposed on Russia and Belarus. However, a large part of Institutions have performed neither the routine nor extraordinary sanctions risk assessment covering the period after 28 February 2022 since the adoption of the first sanctions package in the response to the Russia's war. Therefore, these Institutions have not assessed how the broad and significant changes in the sanctions legislation have affected the sanctions risk inherent to the Institution and have not assessed whether the controls introduced by the Institutions ensures efficient management of such new risk.

Additionally, some Institutions indicated that they have adopted a decision to discontinue servicing transactions with the payment flow from and to Russia and Belarus. Even though the said decision considerably reduces the Institution's exposure to the sanctions risk, it does not eliminate the risk completely, especially regarding the risks of sanctions circumvention. Therefore, also for Institutions which had adopted such decisions it was necessary to update the sanctions risk assessment after 28 February 2022 and assess the need to improve the ICS of sanctions risk management pursuant to Point 11 of Regulation No 126.

- B. Internal regulations of the Institution do not list all circumstances stated in the AML/CTPF Law or Regulation No 126, under which the ML/TPF or sanctions risk assessment should be reviewed and updated

Some Institutions have not defined in their internal regulations some or all circumstances listed in Paragraph three of Section 8 of the AML/CTPF Law or Point 11 of Regulation No 126, under which the ML/TPF or sanctions risk assessment should be reviewed and updated. In several cases the Institutions had defined a frequency of risk assessment update (for example not less than every 18 months) but had not defined the circumstances stated in laws and regulations under which the assessment has to be reviewed. Part of the Institutions have determined the same circumstances for the review of ML/TPF as for the sanctions risk assessment. Thereby the Institutions have not taken into consideration that Point 11.3 of Regulation No 126 additionally requires that the sanctions risk

assessment must be reviewed if the Institution has established that significant changes have taken place in the field of sanctions, for example, a new sanctions regime, which have a direct impact on the Institutions, has been introduced. Some Institutions had generally determined in their internal regulations that the risk assessment must be reviewed if "significant circumstances" regarding the Institution's operations change, but at the same time "significant circumstances" have not been defined.

- C. Upon occurrence of the circumstances listed in the AML/CTPF Law or Regulation No 126, which require updating the risk assessment, an Institution had not updated its ML/TPF or sanctions risk assessments

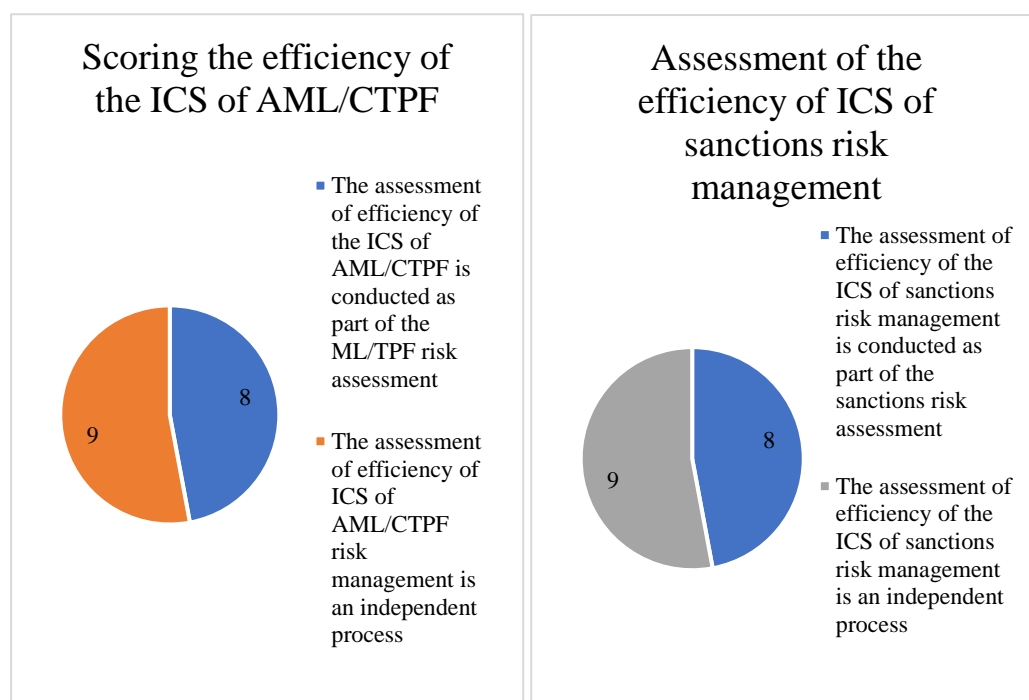
Some Institutions have introduced changes stated in Point 2 of Paragraph three of Section 8 of the AML/CTPF Law or taken actions listed in Point 11.2 of Regulation No 126 but have not updated their risk assessment pursuant to the legislation. Some activities highlighted by the Institutions as performed after the last risk assessment presumably might be considered as minor and such that do not require updating the risk assessment. Nonetheless, in some cases the specified actions *prima facie* can be considered as such that require updating ML/TPF or sanctions risk assessment before performance thereof according to the statutory requirements. For example, the Institutions pointed out that after the last risk assessment they have introduced the following changes – changes in the compliance function operation model and organisational chart, new product delivery channel, material changes in business model and more extensive off-site identification for legal and natural persons have been introduced, and customer database has been reviewed.

1.2.3. Evaluation of the Efficiency of the AML/CTPF and Sanctions Risk Management ICS

Pursuant to Paragraph two of Section 8 of the AML/CTPF Law and Point 10 of Regulation No 126, the Institutions shall assess the efficiency of the ICS of AML/CTPF and sanctions risk management. Eight Institutions point out that the efficiency assessment of ICS of AML/CTPF is performed within the framework of ML/TPF risk assessment process, i.e. the ICS efficiency assessment is performed by assessing the efficiency of risk management measures, i.e. controls. Some of the mentioned Institutions additionally indicated that the efficiency of the ICS is also assessed by the internal audit function and compliance function. The remaining nine Institutions indicated that they assess the efficiency of the ICS of AML/CTPF separately from the risk assessment process, and such assessment is performed by the internal audit function or compliance function, or independent third party.

Meanwhile, regarding the ICS of sanctions risk management, eight Institutions point out that the efficiency assessment of the ICS is conducted as a part of the risk assessment by assessing the controls. However, nine Institutions indicated that the efficiency of ICS of sanctions risk management is assessed separately from the sanctions risk assessment and is performed by the internal audit function or compliance function, or independent third party.

It can be concluded from the provided answers that there are Institutions, which have different approach to assessing the efficiency of ICS of AML/CTPF and the ICS of sanctions risk management. Namely, for certain Institutions the efficiency assessment of the ICS of AML/CTPF is part of the risk assessment, whereas the efficiency assessment of ICS of sanctions risk management is a process that is independent from the sanctions risk assessment or *vice versa*.

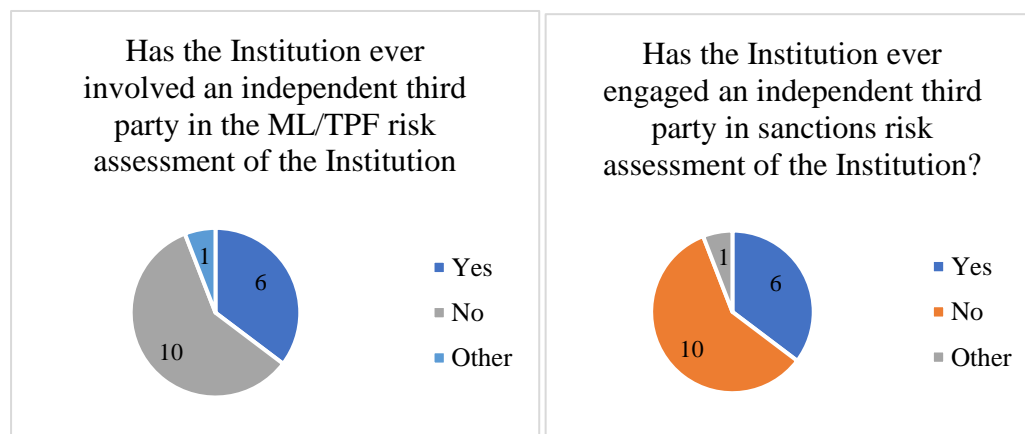


1.3. Parties Involved in the Development of the ML/TPF and Sanctions Risk Assessment Methodology and Conducting the Risk Assessment

The Inspection discovered that six Institutions had involved an independent third party in their ML/TPF risk assessment process. The Institutions have done so for various reasons. In one Institution an independent third party was responsible for entire ML/TPF and sanctions risk assessment, while in another Institution an

independent third party was in charge of performing a risk assessment for a foreign branch of the Institution, and yet in another Institution a third party assisted with introducing a comprehensive ML/TPF and sanctions risk assessment process.

Six Institutions had involved independent third party in the process of sanctions risk assessment. Involvement of external third parties in the risk assessment process was like that stated regarding ML/TPF risk assessment. Additionally, in one Institution an independent third party in cooperation with the Institution prepared a sanctions risk assessment methodology. One Institution answered to this question by picking option "Other", by specifying that it is using a tool developed by an independent third party (ACAMS) for conducting ML/FP sanctions risk assessment.



It follows from the aforesaid that the approach of individual Institutions regarding the engagement of third parties in ML/TPF risk assessment and it the sanctions risk assessment differ, namely, in certain Institutions third parties have been involved in the process of ML/TPF risk assessment, but have not been involved in the sanctions risk assessment process or vice versa.

Additionally, it was established in the Inspection that in regard to all inspected branches of the Member States' credit institutions a joint ML/TPF and sanctions risk assessment is conducted by the parent company of the Latvian branches, and during this joint risk assessment also individual risks inherent to the particular Latvian branch and risk management measures introduced by the branch are being assessed. One branch of the Member State's credit institution pointed out that, in addition to the joint risk assessment carried out by the partner company, the Latvian branch performs also a separate ML/TPF and sanctions risk assessment. All branches indicated that the representatives of Latvian branches are involved in the assessment of risks related to the Branch.

1.3.1. Determining the Responsible Parties in the Internal Regulations

Pursuant to Section 1.1.1 of the Report, the Institutions must document ML/TPF and sanctions risk assessment methodology, as required by the regulatory framework, and it covers also the requirement to determine the responsibility of parties involved in the risk assessment. Accordingly, to ensure that the risk assessment is performed according to the provisions of the applicable statutory regulations and Institution's methodology the Institutions should determine in their internal regulations clear responsibilities over the processes related to risk assessment. This should include, but not be limited to appointing persons that are responsible for the development and updating of ML/TPF and sanctions risk assessment methodology, responsible for identification of circumstances under which the risk assessment should be updated, for approval of risk assessment report, for development, approval and supervision over executing an action plan for managing or mitigating risks that has been developed as a result of the risk assessment, as well as identify individuals or structural units that shall be involved in the risk assessment and the responsibilities of these parties or their tasks over the course of risk assessment. In accordance with the Wolfsberg's Guidelines⁹ it would be advisable to identify in advance those individuals or structural units which shall be involved in the ML/TPF and sanctions risk assessment to ensure a structured and comprehensive risk assessment process.

Engagement of independent, competent third parties in the risk assessment process is permissible and under certain circumstances it could improve quality or efficiency of risk assessment process. Nevertheless, pursuant to Section 6 of the AML/CTPF Law and Section 13.¹ of the Sanctions Law, the Institution itself is responsible for conducting the risk assessment and for ensuring its compliance with the statutory requirements. Pursuant to the EBA's Guidelines on internal governance¹⁰, the Institutions should not rely exclusively on external risk assessment. Therefore, to ensure that the risk assessment is appropriate to the operations of the Institution and that all the risks inherent to the Institution are identified and assessed, the Institution should ensure an appropriate and sufficient involvement of the Institution in the risk assessment process should it choose to engage an external third party in the risk assessment. Meanwhile, in order to demonstrate compliance with the aforesaid, the Institution should document the exact tasks and responsibility of the external third party and of the Institution in the process of each particular risk assessment.

Generally, it can be concluded that a large part of the inspected Institutions in their internal regulations do not specify in detail those individuals or structural

⁹ Wolfsberg's Guidelines, Section 4. Available here: [- Anti-Money Laundering Risk Assessments FAQs \(2014\) \(wolfsberg-group.org\)](https://www.wolfsberg-group.org/anti-money-laundering-risk-assessments-faqs-2014)

¹⁰ EBA's Guidelines on Internal Governance, Clause 142. Available here: [Final Guidelines on Internal Governance \(EBA-GL-2017-11\).pdf \(europa.eu\)](https://www.eba.europa.eu/media/1000000/attachment/1000000/1000000.pdf)

units that shall be involved in the risk assessment process, and also do not determine their responsibility and tasks in performing the risk assessment. However, these Institutions have determined that various structural units or individuals in the Institution are engaged on as-needed basis. Overall, it has been established that the internal regulations of Institutions outline responsibilities for the main risk assessment processes, such as development of methodology, conducting the risk assessment, approval of the risk assessment report etc. The Inspection has also discovered that the Institutions mainly choose to perform ML/TPF and sanctions risk assessment by themselves. Only in limited cases certain Institutions have entrusted a task of performing the entire risk assessment or its phase to an independent third party. In such cases where an independent third party was engaged during the Inspection it was not possible to thoroughly evaluate the Institution's involvement in risk assessment process, because risk assessment reports did not provide information on the scope of involvement of the Institution.

Example of good practice

Risk assessment methodology of an Institution contains a detailed list of involved parties and their responsibilities

The Institution's methodology of ML/TPF and sanctions risk assessment provides a detailed list of parties involved in the risk assessment, their responsibilities and tasks in the process risk assessment, as well as a person or a function, to which the said party reports to regarding the accomplishment of tasks. For example, Institution's methodology provides that the board is responsible for approving the risk assessment methodology and approving risk assessment report, and the board reports about it to the Council. Project (i.e. risk assessment) management function is performed by the compliance function who is the main party in charge of conducting the risk assessment and provision of support in the entire process, including ensures that the necessary resources are allocated necessary for the risk assessment (both human resources and funds) etc.

Examples of bad practice

A. Parties involved in the ML/TPF or sanctions risk assessment and their responsibility have not been determined

Internal regulations of some Institutions do not contain information on individuals or structural units involved in the ML/TPF or sanctions risk assessment and their responsibilities. Several Institutions pointed out that internal regulations generally foresees that any structural units of the Institution can be engaged in the risk assessment process on as-needed basis.

- B. The risk assessment is performed by an independent third party or the independent third party is involved in the risk assessment; however, the involvement of the Institution remains unclear

In certain Institutions conducting of the assessments of ML/TPF or sanctions risks or a certain part of it was in the responsibility of an independent third party. In such cases, which were evaluated during the Inspection, it was not possible to establish the extent of involvement of the respective Institution in the risk assessment process.

- C. When the risk assessment is performed by an independent third party, the risk assessment methodology may differ

Pursuant to an Institution's ML/TPF risk assessment methodology, if the risk assessment is performed by an independent third party, then ML/TPF risk assessment methods, set and scope of data used in ML/TPF risk assessment as well as the scope of information to be included in the final report by the independent third party may differ from the methods described in the Institution's methodology. Latvijas Banka is of the opinion that such major differences should not be permitted in the risk assessment process, because approach like that prevents the Institution from obtaining a complete understanding of its inherent risks over an extended period of time and considerably restricts its possibilities to compare the risk assessment results to those of previous years.

1.3.2. Training of Parties Involved in the Risk Assessment

Pursuant to Wolfsberg's Guidelines¹¹, the Institutions should provide regular and appropriate training or instruction of persons involved in the Institution's ML/TPF and sanctions risk assessment. The training should cover at least information about the risk assessment methodology, tasks of the parties involved as well as any changes in the ML/TPF and sanctions risk assessment methodology (if applicable).

Examples of good practice

- A. A requirement to provide training is determined in the internal regulations

An Institution's internal regulations determines that a training on issues related to the risk assessment methodology and its implementation shall be carried out before conducting each ML/TPF and sanctions risk assessment to ensure the engagement of parties involved in said process and quality of risk assessment's results. The Institution's internal regulations also determine a person in charge of preparing and delivering the training.

¹¹ Wolfsberg's Guidelines, p. 5. Available here: [- Anti-Money Laundering Risk Assessments FAQs \(2014\) \(wolfsberg-group.org\)](#)

- B. An Institution ensures qualification upgrade for the person responsible for conducting risk assessment as well as training is ensured for the involved individuals

The Institution indicates that the person in charge of ML/TPF sanctions risk assessment in the Institution holds a CAMS certificate, and that he/she has additionally received ACAMS certificate in "*Risk Assessment*" and has taken part in other training directly linked to conducting ML/TPF risk assessment. Additionally, the Institution points out that the person in charge, before conducting each ML/TPF and sanctions risk assessment, provides a proper training with the necessary explanations about ML/TPF and sanctions risk assessment for all the employees involved in the risk assessment process, as well as provides relevant support throughout the process of conducting ML/TPF and sanctions risk assessment.

Example of bad practice

Training related to ML/TPF or sanctions risk assessment is not provided

A part of the Institutions do not provide specific training directly linked to conducting ML/TPF or sanctions risk assessment (some of these Institutions provide training related to ML/TPF risk assessment, but do not provide training related to conducting sanctions risk assessment).

1.4. IT Solutions and Quality of the Data Used in the Risk Assessment

1.4.1. Quality of the data used in the ML/TPF and Sanctions Risk Assessment

The Institutions' ML/TPF and sanctions risk assessment should be based on the internal quantitative or statistical data of the Institution regarding their customers and transactions. Therefore, the Institutions should implement certain quality demands for data used for ML/TPF and sanctions risk assessment to ensure proper data quality during data the collection and processing, in which different individuals might be involved and various systems of the Institution could be used, as well as to ensure that any shortcomings in the quality of data are identified, for example, differences in data parameter across various systems, absence of data and other aspects would be identified.

It was concluded in the Inspection that most Institutions have not incorporated specific requirements directly pertaining to data quality in the risk assessment process. The Institutions mainly pointed out that data quality assurance is a process that is constantly supervised and maintained in the Institution. Therefore, in accordance with the answers provided by the Institutions general data quality assurance processes, apply also to risk assessment and to the assurance of data quality used in the risk assessment.

Examples of good practice

- A. An ML/TPF and sanctions risk assessment methodology lays down requirements for data quality assurance

An Institution's risk assessment methodology clearly defines the requirements for data quality assurance in the process of ML/TPF and sanctions risk assessment. Pursuant to the Institution's risk assessment methodology, one of mandatory steps in the risk assessment process is to collect data needed for the risk assessment, verifying data availability and data quality. Individuals who are responsible for data quality assurance are also involved in the risk assessment process. Namely, "data team" participates in the risk assessment process, and it is responsible for collecting and validating quantitative data. The tasks of the "data team" involve also collecting and delivering the required quantitative data about customers and transactions that are necessary for the assessment of inherent risks, testing and validating data models (for example, the weight of risk factors for calculation models), documenting any changes made to the data models.

- B. An Institution identifies and provides information in the risk assessment report on absence or unavailability of data

The Institution identifies and reflects in its ML/TPF and sanctions risk assessment report those data categories, which are unavailable for the Institution to comprehensively assess the risks inherent to the Institution. Pursuant to the Institution's risk assessment methodology, if the Institution lacks data required for the assessment of a particular risk factor, then high level of ML/TPF or sanctions risk shall be assigned to such risk factor. Pursuant to the Institution's methodology, one of steps in the risk assessment process is to identify issues regarding data unavailability and define measures to ensure availability of such data for the next risk assessment of the Institution.

Examples of bad practice

- A. An Institution does not have data necessary for ML/TPF or sanctions risk assessment or data is in non-compliant format

The Institution does not have a partial or full access to certain data that is necessary for the ML/TPF and sanctions risk assessment. Therefore, the Institution cannot fully assess its inherent risks. For example, the Institution points out that for the purpose of the risk assessment it cannot use 100 % of data regarding the source of customers' fund or in 50 % of cases it cannot use data about the country of customers' economic activity. Reasons for such data absence are, for example, it is not possible to extract some data form the due diligence questionnaires of the customers because of their format, and, taking into account non-updated customer due diligence questionnaires, individual data categories

are not indicated at all. A positive aspect is that the Institution assesses, identifies and reflects in the risk assessment report the issues of data absence or unavailability, and the Institution also determines and takes measures to eliminate such shortcomings.

- B. An Institution has not put forth requirements or measures on how to ensure data quality directly in the risk assessment process

A part of the Institutions have not determined specific requirements on how to meet the quality demands for Institution's quantitative or statistical data used in ML/TPF and sanctions risk assessment. Nevertheless, the mentioned Institutions point out that data quality assurance is a routine process, within the framework of which the data quality in risk assessment process is ensured.

1.4.2. Technological Solutions Used for the ML/TPF and Sanctions Risk Assessment

Latvijas Banka is of the opinion that using technological solutions in the ML/TPF and sanctions risk assessment may help the Institutions to enhance the efficiency of that process, as well as minimise human errors, especially considering the extensive volume of data the Institutions should process when assessing their inherent risks. Nevertheless, if the Institution decides to use the technological solutions, the Institution should evaluate and identify the advantages and limitations of such technological solutions, including regarding compatibility of such solutions with other Institution's systems to ensure the quality and integrity of data used in such systems of technological solution.

It was found in the Inspection that the Institutions have different approaches regarding the use of technological solutions in the risk assessment process. Some Institutions indicated that they are using their internal systems that allow generating various reports from various perspectives that can be used for data analysis in the risk assessment. Another Institution mentioned that it uses Excel-based risk driver tool, and another business intelligence tool which ensures automated data acquisition from the internal databases of the Institution in a required format. Several Institutions pointed out that they are using a certain technological solution to process and gather large-scale transaction and customer data. Several Institutions pointed out that they do not use any technological solutions for the risk assessment purposes. Accordingly, it can be concluded that the risk assessment in such cases is done manually.

Example of good practice

An Institution uses a technological solution which evaluates and visually reflects the inherent risk level of the Institution and inherent risk exposure of the Institution

The Institution uses the technological solution for ML/TPF risk assessment for the purpose to assess and visually reflect the inherent risk level of the Institution regarding various risk factors, and Institution's exposure to various inherent risk factors. A solution used by the Institution allows to efficiently collect, analyse and visually reflect large-scale data. However, some shortcomings were observed in usage of such solution (refer to bad practice example below).

Example of bad practice

The technological solution used in the risk assessment restricts Institution's ability to completely assess its inherent risks

Due to a limitation of the technological solution used for the ML/TPF risk assessment, the Institution when determining its risk exposure uses only the number of its customers exposed to the relevant risk factor but does not consider Institution's transaction data. Therefore, from information included in ML/TPF risk assessment it can be concluded that the technological solution used by the Institution restricts the Institution's ability to fully assess the Institution's exposure to ML/TPF risk factors. However, a positive aspect is that the Institution itself identifies the said limitations in the risk assessment report and the Institution analyses transaction data as an additional step to identify and assess "risk pockets".

2. The Elements of the ML/TPF and Sanctions Risk Assessment Methodology

Pursuant to Points 10 and 20 of the Guidance Manual, an Institution, when determining ML/TPF and sanctions risk, to which it is exposed to, should assess the inherent ML/TPF and sanctions risk, to which the Institution is exposed to before applying the risk management measures, i.e. controls, then assesses the efficiency of ML/TPF and sanctions risk management measures and finally determines residual risks by means of the following formula: "inherent risk – efficiency of ML/TPF risk management measures = residual risk".

2.1. The Assessment of the Inherent ML/TPF and Sanctions Risk

2.1.1. The Identification and Assessment of the Inherent ML/TPF and Sanctions Risk

Paragraph 1¹ of Section 6 of the AML/CTPF Law obliges the Institutions to take into account the risks identified by the European Commission in its EU ML/TF risk assessment, risks identified in the national ML/TPF risk assessment report and other risks inherent to the relevant subject of law when performing ML/TPF risk assessment and developing the ICS. Additionally, EBA's Guidelines on

ML/TF risk factors¹² list also certain external and internal information sources of Institutions, which should always be reviewed and which should be considered when identifying and assessing ML and TF risk. Sources mentioned in the specified guidelines should be used also for identifying PF and sanctions risk. In order to ensure and demonstrate that the Institution in its risk assessment takes into consideration at least previously mentioned risks, the Institution should determine in its internal regulations the information sources the Institution uses to identify and assess the Institution's inherent ML/TPF and sanctions risk.

It follows from the mentioned provisions that the inherent risk factor assessment should be based at least on previously listed information sources used by the Institution both to identify the risk factors and assess threats and vulnerability it may be exposed to. The Institution must also take into account and reflect adequately in Institution's risk assessments that the risk factors in EU risk assessment or national risk assessment related to customers, geography, products or delivery channels, have been assessed to have higher ML/TPF or sanctions risk. Whereas, if the Institution in its risk assessment allocates a certain risk level to a risk factor that differs from the one given in the EU or national risk assessment, the Institution should provide a clear explanation to such differences in the assessment of the risk factor.

In order to ascertain that, pursuant to requirements of the AML/CTPF Law and the Sanctions Law, the risk assessment provides to the Institution a proper understanding of risks the Institution is exposed to, the Institution should always analyse both qualitative and quantitative or statistical data of the Institution within the framework of its risk assessment. Data regarding the number of customers should be taken into account in the Institution's risk assessment and one must evaluate the extent to which its customers are exposed to the identified risk factors. The Institution should take into account also its transaction data – data from both the incoming and outgoing transaction flow (volume or number of transactions as required by the relevant risk factor). In certain situations, the Institution may analyse data regarding turnover of funds or volume of assets (for example, in connection with products offered by the Institution or customer's risk factors, considering that a small number of customers may pose major risk exposure if turnover of such customers is relatively large).

Overall, it was concluded in the Inspection that Institutions perform their ML/TPF and sanctions risk assessment in compliance with the method determined in Points 10 and 20 of the Guidance Manual, i.e. they assess the inherent ML/TPF and sanctions risk, assess the efficiency of risk management

¹² EBA's Guidelines on ML/TF risk factors, Clauses 1.29–1.32. Available here: [Guidelines on ML/TF risk factors \(revised\) | European Banking Authority \(europa.eu\)](https://www.eba.europa.eu/en/guidelines/ml-tf-risk-factors-revised)

measures, i.e. control and determine residual risk. The Inspection allowed to observe that the Institutions have different approaches regarding identification and assessment of the inherent ML/TPF and sanctions risk. Different approaches are permissible, taking into account that there is no single method for risk assessment, and that Institutions have different types and extend of operations. However, the Institution should be able to justify and explain why the Institution has chosen to apply a certain method for conducting its risk assessment and the Institution itself should be confident that its methods actually allow to determine and assess all the risks inherent to the Institution. The Inspection concluded that the risk assessment method chosen by the Institution is not clear in all cases, and in certain cases there were doubt about whether the Institution's chosen method in fact allows the Institution to identify and assess its inherent risks. Additionally, regarding the assessment of the inherent risk in general, it can be noted that the Institutions have high expertise in identifying and assessing ML and in most cases also TF risks. However, the Institutions were found to lack understanding regarding the identification and assessment of PF risk and sanctions risk.

Example of good practice

- A. Both the external and internal information sources which must always be taken into consideration in the risk assessment have been identified

An Institution in its ML/TPF risk assessment methodology determines such external and internal information sources that always must be taken into account when performing a risk assessment. In addition to that, the Institution in its ML/TPF risk assessment report has identified all external information sources that were taken into account when assessing the risks, and their list is included in the annex to the risk assessment report.

- B. In its inherent risk assessment, an Institution takes into account both threats and vulnerabilities posed both by the risk factor and Institution's exposure to that particular risk factor

The Institution takes into account both the nature of a relevant risk factor resulting from its threats and vulnerabilities, and Institution's quantitative data – number of customers or volume of transactions subject to that particular risk factor, when performing the inherent risk assessment. Namely, the Institution initially identifies and defines ML/TPF and sanctions risk factors to be assessed. The Institution then assesses these risk factors, taking into account threats and vulnerabilities posed by the relevant risk factor. For example, certain customer business sectors pose higher risk, because, according to external information sources, they are attractive for ML or TF due to large amounts of cash involved. A score (high, average, low or other conforming to the Institution's chosen risk grading matric) for a risk factor is allocated according to the methodology of the

Institution. Afterwards, the Institution determined the Institution's exposure to relevant risk factor by analysing its quantitative data on customers and transactions subject to the risk factors, thereby determining the particular risk exposure.

- C. An Institution identifies and analyses "risk pockets" to identify those combinations of risk factor which pose the largest risk exposure to the Institution

The Institution identifies and assesses high "inherent risk pockets" in order to identify combinations of risks building high risk concentration and assesses their impact on the Institution's risk exposure. The Institution has noted that the reason why such assessment is carried out is that a sperate assessment of risk factors may prevent the Institution from acquiring a sufficient understanding of the risks the Institution is exposed to, as well as Institution notes that the majority of its customers are at low risk (additionally, this is carried out because the particular Institution assesses its inherent risk only on the basis of the number of customers falling into that risk category, but does not take transaction data into account). For example, when assessing the risk factor "incoming transactions from offshore companies" the Institution identifies the total number of customers who have received incoming payments from the offshore countries, and the total amount of such transactions. Then, to assess the "risk pockets", the Institution identifies the proportion of such customers who have received such incoming payments from the offshore countries and whose BO are PEP, and then determine what is the proportion of such incoming transaction, in which the receiver was a customer whose BO are PEP, from all such transactions in the Institution. Also, other "risk pockets" are analysed regarding the said risk factor "incoming transactions from offshore countries" by determining what proportion of the customers involved in such transactions are ones whose ownership structure is related to the offshore jurisdictions and whose BO comes from a high-risk jurisdiction or other "risk pocket".

Examples of bad practice

- A. An Institution does not assess the inherent sanctions risk

The Institution in its risk assessment does not identify and assess those risk factors which are inherent to the Institution's customers, geography, offered products or services and delivery channels. Institution's sanctions risk assessment essentially contains only a general assessment of the efficiency of Institution's controls.

- B. The assessment of inherent ML/TPF or sanctions risk is not based on or is insufficiently based on the analysis of Institution's quantitative data

Some Institutions do not analyse or do not analyse sufficiently their quantitative data regarding their customers and transactions. For example, sanctions and PF risk assessment of a particular Institution contains general analysis of very limited scope of quantitative data. The only data analysed by the Institution within the framework of the risk assessment is data on the number of customers who are related to high risk geographies and the number of customers who are given high risk score, without analysing in greater detail the reason for allocating such high risk score and what are TOP jurisdictions from and to which the largest number of transactions are made over a period of 12 months. Accordingly, the inherent sanctions and PF risk is assessed on the basis of general assumptions.

Meanwhile, sanctions risk assessment of another Institution is not based on the quantitative data of the Institution. The Institution in its sanctions risk assessment does not analyse any data of the Institution regarding the customers or transactions. The risk assessment essentially evaluates the ICS elements of the sanctions risk management and their efficiency (which also is not fully assessed because the Institution only determines whether a particular control element exist rather than assessing its actual efficiency). Therefore, the risk arising from the Institution's customers, geography, products and delivery channels is not assessed. Similarly, risk assessment of another Institution does not contain analysis of any kind of quantitative data of the Institution regarding its customers or transactions.

- C. An Institution, when determining the risk score, relies only on the exposure of the relevant risk in the Institution, but it does not consider the nature of the risk arising from the threats and vulnerabilities of the particular risk

The risk score in some Institutions is determined only on the basis of quantitative data of the Institution regarding the number of Institution's customers exposed to relevant risk factor, or, in some cases, taking into account also data on the value of financial assets of relevant customers and their credit turnover in the Institution.

In the opinion of Latvijas Banka, the inherent risk level score cannot be determined solely on the basis of the quantitative data of the Institution depending on the number of customers or transactions (or other quantitative indicators) exposed to a particular risk factor, without considering the level of threats and vulnerabilities posed by the risk factor. For example, if the Institution assess the inherent ML risk of the risk factor "PEP", the Institution must take into account that according to the external information sources, PEP essentially poses a higher ML risk and its risk level may vary depending also on the PEP's country risk. The number of customers subject to the PEP risk does not essentially change the fact that a PEP has higher inherent ML risk and therefore the Institution needs to

introduce sufficiently efficient controls to manage or reduce the increased inherent ML risk related to the PEP. In the opinion of Latvijas Banka, the exposure of the risk factors of PEP or other risk factor's exposure may help the Institution to determine what level of sophistication or automation in regard to the Institution's controls is necessary to ensure management of such risk.

D. No explanation is provided for allocating a particular score for an inherent risk factor

Some Institutions in their ML/TPF or sanctions risk assessment report do not provide justification for why each particular inherent risk factor has received the relevant score. For example, the Institution in its risk assessment report has allocated "medium-high" risk score to the factor "customers' business activity". The Institution indicates only the numerical value of the score assigned to the risk factor but does not provide a justification for assigning that score. The methodology for ML/TPF risk assessment of the Institution also does not clarify the principle on how risk scores are calculated.

E. When assessing the inherent ML/TPF or sanctions risk, the Institution takes into account the controls introduced by the Institution

Some Institutions, when assessing their inherent risk, take into consideration the controls introduced by the Institution. Namely the score allocated to the risk factor is justified also with the presence of controls. In the opinion of Latvijas Banka, it is important to differentiate between the technical limitations or functionality of products or services that characterise the particular product or service, and between the controls introduced by the Institution to manage the risks. Latvijas Banka is of the opinion that when assessing the inherent risk of a product or a service it is reasonable to take into account the technical restrictions or functionality of the product that characterises the very product and that applies equally to all customers of the Institution. However, controls, including limits, restrictions of a service or a product that are determined for particular customers or groups of customers are considered to be controls applied by the Institution to mitigate or manage sanctions risk. Therefore, such restrictions for product or service may not be taken into account when assessing the inherent risk. Otherwise, there is a risk that Institution's inherent ML/TPF or sanctions risk level may be artificially reduced.

2.1.2. Differences between the ML, TF, PF and sanctions risk

The AML/CTPF Law demands the Institutions to perform assessment of all – ML, TF and PF risk, whereas the Sanctions Law obliges the Institutions to perform the sanctions risk assessment. In order to accomplish it efficiently and to understand the particular risks the Institutions are exposed to, the Institutions

must identify and understand the differences between ML, TF, PF and sanctions risk.

Even though ML, TF, PF risks and the risk of sanctions circumvention or violation have common elements, nevertheless the Institutions must understand and take into account their differences both regarding threats and vulnerability and regarding the risk level in jurisdictions in which the Institutions offer their products or services. Therefore ML, TF, PF, and sanctions risk posed by the Institution's customers, geography, products or services and delivery channels may differ. In order to understand differences of the mentioned risks, the Institutions should assess also various external information sources that provide information about relevant risk factors and different typologies for ML/TFP and sanctions violation and circumvention. For example, EBA's Guidelines on risk factors¹³ list differences to be taken into consideration when assessing ML and TF risk. In order to identify the PF risk, the Institutions may analyse and consider at a national level – risks identified in the national risk assessment, use PF typologies provided in the State Security Service's guidelines¹⁴, PF typologies identified by FATF and guidelines for PF risk assessment¹⁵, as well as, for example, analyse the UN Expert Panel on North Korea reports¹⁶, which analyse actual information on PF risks and methods used by the said country, and other information sources¹⁷.

Besides, bearing in mind the differences in ML, TF, PF and sanctions risk, the Institutions must understand that controls that are being used for the risk management may differ and therefore ensure that the controls introduced by the Institutions can manage or mitigate all mentioned risks. Therefore, when assessing the efficiency of controls within the framework of the risk assessment, the Institutions should be able to evaluate whether the controls introduced by the Institution efficiently mitigate ML, TF, PF and sanctions risk. For example, the Institution may regularly develop and perform staff training in the area of ML and TF, but at the same time the Institution might not have determined that the staff should regularly be trained on a PF risk or, for example, the Institution does not provide sufficient staff training on sanctions risk, because the training does not sufficiently cover issues related to sectoral sanctions risk.

¹³ For example, EBA's Guidelines on ML/TF risk factors, Clauses 2.7, 2.8. Available here: [Guidelines on ML/TF risk factors \(revised\) | European Banking Authority \(europa.eu\)](#)

¹⁴ State Security Service's TF and PF guidelines. Available here: <https://vdd.gov.lv/uploads/materials/6/lv/tfpn-vadlinijas.pdf>

¹⁵ Materials on PF elaborated by FATF. Available here: [Proliferation Financing \(fatf-gafi.org\)](#)

¹⁶ UN reports. Available here: [UN Documents for DPRK \(North Korea\): Sanctions Committee Documents \(securitycouncilreport.org\)](#)

¹⁷ For example, academic research in relation to PF, such as the research conducted by King's College. Available here: [Final report: typologies of proliferation finance \(kcl.ac.uk\)](#)

The Inspection found that some Institutions perform their PF risk assessment together with sanctions risk assessment, while other Institutions perform PF risk assessment together with ML and TF risk assessment, while other Institutions perform a single ML/TPF and sanctions risk assessment. Latvijas Banka holds an opinion that all aforesaid approaches are suitable as long as the Institution is able to take into consideration the differences between ML, TF, PF and sanctions risk both regarding the risk factors assessed by the Institution and regarding the controls introduced by the Institution to manage relevant risks. Furthermore, if a PF risk is being assessed together with a sanctions risk, the Institution must take into account that, considering the PF definition provided in Paragraph five of Section 5 of the AML/CTPF Law¹⁸, a PF risk assessment, in which PF risk is analysed only in the context of sanctions that have been imposed in relation to PF, then such risk assessment would not comply with the AML/CTPF Law.

In general, the Inspection has concluded that the Institutions lack understanding on how to assess risk that are directly related to, therefore within the framework of the risk assessment the PF risk is not considered at all or is not identified and assessed sufficiently. According to the most recent national ML/TPF risk assessment¹⁹ Latvia has medium-low level of PF risk and a low TF risk level. Nevertheless, it is important to enhance the Institutions' understanding about PF and TF risk and management thereof. Within the framework of the Inspection, some institutions indicated a desire to receive explanations and practical examples regarding PF risk assessment.

Example of good practice

An Institution assesses ML and TF risks separately

The Institution in its ML/TPF risk assessment assesses ML and TF risks separately for each risk factor in each risk category, by assessing individually the vulnerabilities and threats a risk factor poses regarding ML and TF separately. For example, regarding the risk factor relating to the type of customers' economic activity "transport and storage industry", the Institution assesses that it has high ML risk and that according to the external information sources this industry is used in ML schemes (for example, trade-based ML), but it is not characteristic to TF, therefore TF risk is evaluated as low. However, taking into account that

¹⁸ Pursuant to Paragraph five of Section 5 of the AML/CTPF Law the PF or financing of manufacture, storage, movement, use, or proliferation of weapons of mass destruction is the direct or indirect collection or transfer of financial resources or other property acquired by any form with a view to use them or by knowing that they will be fully or partly used to finance proliferation.

¹⁹ The national ML/TPF risk assessment report 2017–2019 (summary). Available here: [Nacionālā NILLTPF risku novērtējuma ziņojuma kopsavilkums.pdf \(fid.gov.lv\)](https://nacionala.nilltpf.risku.novertejuma.zinojuma.kopsavilkums.pdf)

pursuant to the Institution's methodology, TF and PF risk is assessed together, this risk assessment method used by the Institution contains also aspects that are considered as bad practice example. For example, the mentioned transport and storage industry should not have a low PF risk, because the transportation industry may be involved as a stage in PF operations. Therefore, the method chosen by the Institution to assess TF risk and PF risk as a single risk without differentiating between them is perceived as an example of bad practice.

Examples of bad practice

A. The PF risk is not assessed at all or is assessed insufficiently

Many Institutions do not separate PF risk and therefore they assess the PF risk together with the TF risk or sanctions risk, or assess all risks – ML, TF, PF risk and sanctions risk together. By analysing the methodologies and risk assessments submitted by the Institutions it can be concluded that the Institutions' assessed risk factors do not cover the PF risk at all or cover it insufficiently.

B. The TF risk is not assessed at all or is assessed insufficiently

The Institutions assess ML and TF risk (or ML and TF, and PF risk in some cases) as a single risk. It has been concluded in the Inspection that a major part of the Institutions do not consider differences between ML and TF in the analysed risk factors, besides some Institutions have been found to not cover TF risk at all in their assessment of risk factors.

2.1.3. Identifying Differences in Risks Posed by Various Types of Sanctions

The Sanctions Law requires the Institutions to perform a sanctions risk assessment. Pursuant to Section 4 of the Sanctions Law, there are different types of sanctions, from which the most significant risks to the Institutions are posed by the financial and civil restrictions indicated in Section 5 of the Sanctions Law, as well as trade restrictions indicated in Section 8 of the Sanctions Law. In addition to the extensive EU sanctions which were imposed as a response to Russia's activities that destroy or threaten the territorial integrity, sovereignty and independence of Ukraine, also new, unprecedented types of sanctions were introduced, for example 100 000 euro deposit restriction as well as extensive scope of products, services and industries were subjected to the restrictions of sectoral sanctions.

Considering various types of sanctions, the Institutions must be aware of the differences that are inherent in the risks posed by various types of sanctions and ensure that they identify and assess not only risks related to the financial sanctions, but also the sectoral sanctions, which have a significant impact on the activities of the Institutions', considering the significant volume of sanctions imposed on Russia and Belarus, geographic location of Latvia as well as

economic ties between Latvia and jurisdictions subject to sanctions. Therefore, the Institutions should analyse and assess also risk factors that directly cover risks posed by sectoral sanctions and ensure that all types of sectoral sanctions are covered and assessed. For example, regarding the assessment of inherent customer sanctions risk, in order to ensure that the sectoral sanctions risk is covered, the Institutions should at least identify and assess the types of customers' economic activities (including ones related to goods and services subject to sectoral sanctions) which have high sectoral sanctions risk. The Institutions should also identify and assess those jurisdictions, which have high sanctions risk (covering all – the countries against which different types of sanctions are imposed, their neighbouring countries, as well as the countries regarding which there is information that they are used to circumvent sanctions). The Institutions should analyse all types of factors that link the Institution's customers to such high risk jurisdictions (covering country of their residence and economic activity, and other factors indicated in Sub-Section 2.1.5.2 of the Report), as well as evaluate the transaction flow from and to such jurisdictions. In addition to that, the Institutions should define and assess other risk factors to ensure that all types of sectoral sanctions, including ones covering the sectoral sanctions regarding the financial instruments and deposit restrictions, are covered.

It is equally important to ensure that in the next steps of risk assessment the Institutions identify and assess the controls introduced by the Institution, which ensure not only mitigation or management of the financial sanctions risk but also directly the sectoral sanctions risk, which includes not only using of sanctions screening tools but also including, but not limited to the following controls – customer due diligence measures, transaction monitoring measures and their efficiency assessment introduced for the management of sectoral sanctions, as well as Institution's procedures to ensure that, in case of changes in the statutory sanctions regulation, the Institution is able to efficiently ensure immediate implementation of such changes in the ICS of sanctions risk management. The Institutions whose risk appetite permits to service customers subject to financial sanctions must define and assess separately the controls that ensure the management of sanctions risk posed directly by such customers of the Institution.

In general, the Inspection led to a conclusion that many Institutions do not assess or insufficiently assess the risk posed by sectoral sanctions. It is essential for all Institutions to assess and be aware of the sectoral sanctions risk the Institution is subject to. It is important to assess this risk also for Institutions, which offer limited scope of services or products and Institutions which have decided to discontinue payments from and to Russia and Belarus. For example, if an Institution offers only loans, it must be aware that the sectoral sanctions restriction includes a prohibition to directly or indirectly provide financial assistance related to certain goods or industries, which apply both to defined

natural or legal persons, and generally to legal and natural persons in Russia or Belarus, or for use in Russia or Belarus. Therefore, even if the Institution does not service persons in Russia, a prohibition to provide financial assistance applies also to indirect funding and funding that can be used in Russia, even though the financial assistance has been provided to residents of other countries. Similarly, Institutions, which offer customers to invest in loans in their platforms must be able to ensure that these loans do not contradict to the sectoral sanctions to ensure that Institutions are not providing indirect financing of loans subject to sectoral sanctions.

Example of good practice

Industries that are subject to the sectoral sanctions have been identified and assessed

For the purpose of assessing sectoral sanction risk an Institution in its sanctions risk assessment has separately identified and assessed also the types of economic activity subject to the sectoral sanctions risk. The Institution evaluates the number of its customers (as a number and per cent from total number) who are subject to the industry's sectoral sanctions risk in question, as well as assesses the value of total turnover of funds subject to such risk factor in the Institution.

Example of bad practice

Sanctions risk assessment does not cover the sectoral sanctions risk or covers it insufficiently

Several Institutions insufficiently assess risks related to sectoral sanctions risk. For instance, an Institution assesses only the following three risk factors related to its customers – citizens of or legal persons operating in the countries subject to sanctions, customers with a BO from countries subject to sanctions, customers subject to sanctions or whose BO is subject to sanctions. Such risk factors do not comprehensively embrace the risk of sectoral sanctions. Besides, the Institution points out that it also services and does not limit the risk appetite regarding high-risk customers like financial institution from high-risk jurisdictions or virtual currency service and payment service providers that are related to high sanctions risk. Consequently, considering the Institution's customer base and risk appetite the Institution's sanctions risk assessment which analyses only the listed risk factors regarding its customers, cannot identify and provide a clear understanding to the Institution on what sanctions risk the Institution is exposed to.

For example, another Institution, regarding the customers' sanctions risk and PF risk assesses only the customers' country of residence (by determining the number of residences from the particular high-risk jurisdictions) and the risk category allocated individually to customers (a number of low, average and high risk

customers). Considering the two factors, the Institution concludes that it has a low customers' sanctions and PF risk. Therefore, it can be concluded that regarding the customers' association with high risk jurisdictions, the Institution assesses only the criteria of residence and accordingly does not assess other factors which may link its customer to high risk jurisdiction, for example, the place of business operations or customer's business partner is from a high risk jurisdiction, which is essential for the sectoral sanctions risk assessment. The Institution generally indicates that within the framework of sanctions risk management activities it assesses various factors that may increase the customer's sanctions risk, including individual industries with heightened sanctions risk, which are also related to trade of certain high-risk goods. However, the Institution within the framework of the risk assessment does not analyse and assess the number of Institution's customers that are exposed to such sectoral sanctions risk. Furthermore, the list of factors that increases sanctions risk indicated by the Institution does not cover all industries or product categories which are currently subject to the restrictions of sectoral sanctions against Russia and Belarus.

2.1.4. Evaluation of the Impact of Sanctions Imposed by the Member States of the EU and the NATO within the Framework of Sanctions Risk Assessment

Point 17 of Regulation No 126 stipulates that if, according to the provisions of Points 15 and 16 of Regulation No 126 the Institution determines in the sanctions risk assessment a significant impact of sanctions imposed by a Member State of the EU or NATO on the interests of the Institution or financial and capital market, then the Institution must ensure proper sanctions risk management also regarding the sanctions imposed by the respective Member State of the EU or the NATO. Accordingly, it follows from Points 3.1 and 4 of Regulation No 126 that the Institutions according to their type of activity in order to identify, assess, understand and manage the sanctions risk inherent in its operations, must perform and document a risk assessment of sanctions, i.e. regarding the restrictions imposed on sanctions subjects adopted according to the provisions of the Sanctions Law, as well as the sanctions imposed by the respective Member State of the EU or NATO, which the Institution has identified pursuant to Points 15 and 16 of Regulation No 126.

Pursuant to Point 15 of Regulation No 126, it is considered that sanctions with significant impact on the interests of the financial and capital market are such sanctions that are imposed by a Member State of the EU or NATO, in the official currency of which (except for euro) settlement of transactions are mainly made in the international trade and financial markets, and that the failure to comply with would hinder the ability of the financial and capital market participants to access the international financial settlement system. Considering the aforesaid, sanctions imposed by the OFAC are deemed to have a significant influence on

the financial and capital market's interests. Therefore, when assessing the sanctions risk, the Institutions must always assess the sanctions risk regarding the sanctions imposed by the EU, the UN and the OFAC.

In addition to the mentioned, pursuant to Point 16 of Regulation No 126, when assessing the sanctions risk and assessing those sanctions imposed by the Member States of the EU or NATO, which could have significant influence on the Institution's interests, the Institutions shall assess and take into account at least the following conditions mentioned in Point 16 of the said Regulation No 126: (1) currencies, in which the Institution provides services and products, (2) Institution's contractual relations with other financial institutions or correspondent banks, (3) region, including a country where the Institution's units – a subsidiary, a branch, a representative office – operates and provides services, (4) countries of operation of the Institution's customers. Pursuant to Point 17 of Regulation No 126, the said assessment, which shall be performed within the framework of sanctions risk assessment, forms a basis for adopting a decision on whether the Institution is required to ensure proper sanctions risk management also regarding those sanctions imposed by that particular EU or NATO Member State, regarding which the Institution has established to have a significant impact on the Institution or interests of the financial and capital market. Latvijas Banka believes that it is important to perform such evaluation regularly within the framework of sanctions risk assessment in order to ensure that the Institution puts in place such sanctions risk management measures that correspond to the actual situation in the Institution.

It follows from the aforesaid that within the framework sanctions risk assessment the Institutions, when analysing the factors mentioned in Point 16 of Regulation No 126, shall assess and determine whether in addition to sanctions imposed by the EU, the UN, the OFAC there are any another sanctions imposed by a particular Member State of the EU or NATO, that have significant impact on the interests of the Institution. If the Institution identifies a significant impact of sanctions of a particular Member State of the EU or NATO and adopts a decision to manage such sanction risk, then the Institution shall perform the sanctions risk assessment regarding all the sanctions imposed by the EU, the UN and the OFAC and by that particular Member State of the EU or NATO.

Generally, the Inspection led to a conclusion that even though the regulatory framework clearly obliges the Institutions to perform such sanctions risk assessment regarding the impact of sanctions imposed by the Member States of the EU and NATO on the Institution and lists also the criteria to be analysed, the majority of Institutions does not perform such assessment (see detailed information in the bad practice example in the continuation).

Example of good practice

The impact of sanctions imposed by the EU and NATO Member States is assessed

An Institution indicates that to determine those sanctions imposed by the Member States of the EU and NATO, which have a significant influence on the interests of the Institution or the financial and capital market, the Institution takes into account the criteria stated in Chapter III of Regulation No 126. The institution also considers that the obligation stated in its internal sanctions compliance policy complies with statutory regulations and considers the risk which may arise if sanctions are not observed. The Institution in its sanctions compliance policy has listed those countries whose issued sanctions the Institution shall observe. If it was determined that, taking into account the risks, the Institution has to comply with the national sanctions issued by other Member States of the NATO or the EU, then the sanctions compliance policy of the Institution would be updated accordingly. Pursuant to the Institution's sanction compliance policy, on the basis of the Institution's sanction risk assessment and considering the contracts in which the Institution has entered (for example, regarding establishing and maintaining correspondent relationships), the Institution may comply with the sanctions issued also by other EU or NATO Member States to an extent it does not contradict regulations that are binding to the Institution, if a significant impact is identified on its interests, even if these sanctions are not legally binding for the Institution. Thereby, the Institution ensures the sanctions risk management in relation to the restrictions determined by such EU or NATO Member State.

Example of bad practice

Within the framework of the sanctions risk assessment, an Institution does not assess the impact of the sanctions imposed by the Member States of the EU and NATO

A large part of the Institutions does not regularly evaluate the impact of sanctions imposed by the EU and NATO Member States on the interests of the Institution and the financial and capital market within the framework of the sanctions risk assessment pursuant to Point 16 of Regulation No 126, including does not assess the factors mentioned in Point 16. The Institutions have determined in their internal legislation those Member States of the EU or NATO whose issued sanctions they comply with. However, it follows from the answers of the Institutions that they do not regularly evaluate whether, taking into account the changes in Institution's activities, including the conditions mentioned in Point 16 of Regulation No 126, it is necessary to supplement or change the list of those countries whose sanctions the Institution complies with.

2.1.5. Assessment of Various Categories of ML/TPF and Sanctions Risk

Pursuant to Paragraph 1² of Section 6 of the AML/CTPF Law, when determining the inherent ML/TPF risks of the Institution, the Institution evaluates at least the following categories – customer risk, country and geographical risk, risk of services and products used by the customer and risk of delivery channels of services and products. Pursuant to Point 4 of Regulation No 126, when determining the sanctions risk inherent in the Institution regarding its customer, the Institution takes into consideration the risk categories mentioned in the AML/CTPF Law, as well as regarding the Institution's operation, it takes into consideration the following factors: (1) region of the Institution's operation and service provision, including a country where the Institution's unit – a subsidiary, branch, representative office – operates and provides its services; (2) countries and territories where third parties, which on behalf of the Institution attract, identify customers or acquire information necessary for their due diligence (i.e. agents) operate, and (3) the services and products offered by the Institution. In order to determine the risk factors that should be assessed regarding the mentioned risk categories, the Institution may take into consideration the risk factors determined in EBA's Guidelines on ML/TF risk factors²⁰. However, it should be noted that in addition to the provisions of EBA's Guidelines on ML/TPF risk factors, the Institutions consider also the PF risk and sanctions risk factors, which are not directly covered in EBA's Guidelines on ML/TF risk factors. Even though many risk factors will be suitable also in context of PF and sanctions risk, they do not fully cover these risk factors.

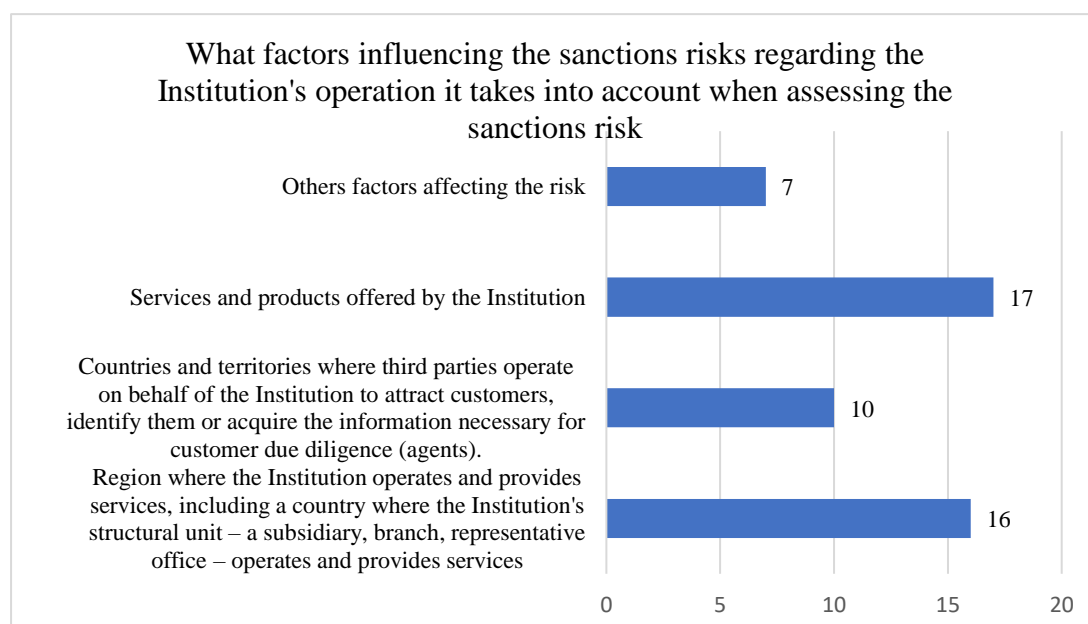
If the Institution in its ML/TPF or sanctions risk assessments, in addition to what was stated previously, opts to assess other risk categories, the Institution in its risk assessment methodology should clearly define what the relevant risk category includes and how it is assessed. The Institution should provide a clear explanation for the assessment of additional risk categories, especially if such risk category is not supported by internationally recognised recommendations. For example, according to different recommendations, the Institution, in addition to said risk categories, can assess qualitative and emerging ML/TPF and sanctions risks.

Pursuant to the answers given by the Institutions within the Inspection, all the inspected Institutions pointed out that they assess all four risk categories mentioned in the AML/CTPF Law when assessing the ML/TPF risk. Additionally, some Institutions pointed out that regarding ML/TPF they evaluate

²⁰ EBA's Guidelines on ML/TF risk factors, Chapter 2 Available here: [Guidelines on ML/TF risk factors \(revised\) | European Banking Authority \(europa.eu\)](#)

also the following risk categories – a transaction risk, industry risk, qualitative risk, emerging risk, risk of resource adequacy.

Furthermore, within the framework of assessing the sanctions risk, the Institutions assess all four risk categories mentioned in the ML/TPF Law regarding the Institution's customer (see the next Chart). One Institution pointed out that it does not assess a risk that is related to a region where the Institution operates or provides services. Meanwhile, some Institutions pointed out that they do not assess countries and territories where third parties operate on behalf of the Institution to attract customers, identify them or acquire the information necessary for customer due diligence (i.e. agents). One of such Institutions explained that it does not assess this risk factor, because the Institution does not use such agents in the mentioned process, meanwhile other Institutions had not any explanations regarding this factor. The Institutions pointed out that, in addition to the mentioned risk categories, they also assess the following risk categories – credit institution's relations with other providers of financial services or correspondent banks; technologies used by the Institution; currencies in which the Institution provides services; Institution's service providers and employees.



Example of good practice

Assessing the emerging risks

An Institution has determined a requirement in its methodology to assess the emerging risks and has defined clear criteria, which shall be assessed under this risk category. The Institution has determined that, when assessing the emerging risk category it assesses, for example, the following aspects – increase in the

planned number of customers or turnover, introduction of new products or services, or delivery channels, planned mergers of companies, planned changes in strategy, planned changes in external legislation. Latvijas Banka holds a view that additional good practice would involve assessing emerging risks posed to the Institution not only by the internal changes of the Institution but also changes in external environment, for example, future risks identified in the national risk assessment²¹ or risk identified by EBA²² etc.

Examples of bad practice

A. An Institution assesses additional risk categories with no clear explanation for their individual assessment

Individual Institutions additionally assess other risk categories with no clear explanation for their individual assessment. For example, one Institution assesses individually a category "Industry risk" where it assesses only one risk factor – industry where the Institution's customer performs economic activities. In the ML/TPF risk assessment performed by the Institution, it was established that regarding the majority of Institution's business segments (the Institution individually assesses the risks in various business segments) in most cases the inherent "Industry's ML/TPF risk" was scored as "high", however the inherent "customer's ML/TPF risk" was scored as low or medium. Since the Institution's methodology does not contain a clear justification for separating the "industry risk" from the "customer risk" category, *prima facie*, it can be concluded that separating such risk category can reduce the inherent ML/TPF risk of Institution's customers without objective justification. This can result in insufficient or biased understanding of the risks inherent in the Institution, especially taking into account the fact that the Institution's risk assessment lacks analysis of interactions between various risk categories, for example, analysis of interactions between customer and industry risk categories.

Meanwhile, another Institution assesses transaction risk as a separate risk category within the framework of the sanctions and PF risk assessment. The only factor the Institution assesses in the transaction risk category, is the number of transactions that are local and remaining TOP 10 countries in terms of the number of transactions (it is not clear from the risk assessment and methodology whether the value in euro of transactions is evaluated or the number of transactions).

²¹ For example, the National ML/TPF Risk Assessment Report 2016–2019 (summary), Section 2.7. Available here: [Nacionālā NILLTPF risku novērtējuma ziņojuma kopsavilkums.pdf \(fid.gov.lv\)](https://nilltpf.gov.lv/files/default/documents/files/document_library/Publications/Opinions/2021/963685/Opinion%20on%20MLTF%20risks.pdf)

²² For example, EBA's opinion on ML/TPF risks influencing the EU financial system. Available here: https://www.eba.europa.eu/sites/default/documents/files/document_library/Publications/Opinions/2021/963685/Opinion%20on%20MLTF%20risks.pdf

Considering this specific factor, the Institution concludes that the transaction risk of sanctions and PF is low. In addition to that, the Institution concludes from the mentioned analysis that the OFAC's sanctions risk is "higher", but this statement is not backed up by any considerations.

B. An Institution does not assess the sanctions risk related to the region of Institution's operation and service provision

The Institution points out that it does not assess the risk related to the region of Institution's activities and service provision, which the Institution should be assessing in line with Point 4 of Regulation No 126.

C. Separating elements of qualitative risk from the controls

Some Institutions, when assessing the inherent ML/TPF or sanctions risk, assesses a risk category "Qualitative risk", which is a risk category the assessment of which is recommended, for example, in Wolfsberg's Guidelines. The Inspection found that the Institution when assessing factors of the qualitative risk also assesses such factors that essentially apply to the efficiency of Institution's controls. For example, the following factors were assessed – identified significant or material deficiencies regarding the ICS of AML/CTPF or managing sanctions risk that concerns management, strategy or general framework of the ICS; deficiencies identified in the regulator's inspections.

2.1.5.1. Assessment of the Inherent Customers' ML/TPF and Sanctions Risk

Pursuant to Paragraph 1² of Section 6 of the AML/CTPF Law and Point 4.2 of Regulation No 126, the Institutions shall assess the customer risk inherent in the customer's legal form, ownership structure, the economic or personal activities of a customer or customer's BO. The Institution should identify and assess those customers' risk factors, which correspond to the Institution's customer profile, and which provide sufficiently detailed understanding of all risks posed to the Institution by its customer base.

Example of good practice

When assessing the customers' ML/TPF risk, all customers are covered and the risk posed thereof

An Institution, when assessing the customers' ML/TPF risk, covers all the Institution's customers. Namely, when assessing the risk factors the Institution is subject to in relation to its customers, the Institution includes each client in one of the risk segments. For example, all customers of the Institution – natural persons – are included in one of the assessed risk segments (including but not limited to the following segments – adults, minors, seniors, persons which are residents of high-risk tax jurisdictions, PEPs, high net worth persons etc.). If a

customer corresponds to the features of several segments, then the customer is included only in one segment with the higher risk. Afterwards, the Institution identifies and assesses ML/TPF threats and vulnerabilities that the relevant segment poses, by allocating to each segment a risk score and assessing exposure of each risk segment in the Institution.

Examples of bad practice

A. Customers' risk factors do not correspond to the Institution's customer base

It has been established that for some Institutions the risk factors evaluated in relations to the Institutions' customers do not correspond to the Institutions' customer base. For example, one Institution assesses customers' ML/TPF risk category by assessing only the following three risk factors: customers subject to enhanced due diligence in the Institution; shell companies and PEPs. At the same time, the Institution indicates in its risk assessment that according to its risk appetite, the Institution does not restrict cooperation with high-risk customers, including institutions which provide financial services (also payment services and services related to virtual currency), as well as with such high-risk customers that operate in high-risk jurisdictions. Considering such risk appetite of the Institution and its customer base, the three mentioned risk factors assessed by the Institution are not considered as sufficient to identify and assess all risks posed to the Institution by its customers. Meanwhile, other Institution points out that its customer base mainly consists of the customers who are natural persons. But in the risk assessment regarding the customer risk, mainly risks to which legal persons may be subject, are analysed.

B. Risks posed by the type of economic activities of customers are not identified and assessed or are assessed insufficiently

Some Institutions, when assessing the customers' ML/TPF or sanctions risk, do not assess the risks posed by the type of economic activity of its customers or assess such risks insufficiently. For example, an Institution in its ML/TPF risk assessment regarding the type of the economic activity type, analyses only two factors – high risk industries in which use of cash is common, and high risk industries where the use of cash is not common. In the opinion of Latvijas Banka, taking into account the size and extent of operations of the particular Institution, the analysis of the said two risk factors cannot provide sufficient understanding on how exactly the Institution's customers, taking into account the types of their economic activities, influence the Institution's risks. Therefore, it would be necessary to assess the types of customers' economic activity in more detail, including to take into account that the exposure of different types of the economic activity to ML and TF risk may differ.

2.1.5.2. Assessment of the Inherent Geographical ML/TPF and Sanctions Risk

Pursuant to Paragraph 1² of Section 6 of the AML/CTPF Law and Point 4.2 of Regulation No 126, the Institution shall assess the country and geographical risk, namely risk that the customer or customer's BO is related to a country or territory where the economic, social, legal or political circumstances may indicate high ML or TF and PF as well as sanctions risk inherent to the country. The Institutions should take into account that different jurisdictions may be subject to different risks, for example, a jurisdiction may be subject to high ML risk, whereas in the same jurisdiction PF risk might be of minor importance. Therefore, in order to ensure that the Institution's risk assessment completely covers all risks to be analysed, the Institutions should take into account such differences in risk to which the jurisdictions are subject. The Institutions should provide a clear justification on how they assess the risk level of jurisdictions, including what external information sources are used for assigning a particular risk level.

According to the Wolfsberg's Guidelines²³ it is essential for the Institutions, when assessing the geographical risk, to take into account various factors, linking the Institution's clients and transactions to relevant jurisdictions. Such factors are at least the following – the country of registration of a legal person, citizenship and actual residency of a natural person, citizenship and actual residence of the legal person's BO, country of economic activity of a customer and customer's BO, other liabilities which the customer or its BO has with the jurisdiction, for example, a business partner, financial or legal interests in relevant jurisdiction. The Institutions should analyse also the transaction flow (incoming and outgoing) regarding various jurisdictions. The Institutions may choose how to combine and in which risk category to assess geography-related risks. For example, customer's connection with high-risk jurisdictions may be assessed by the Institution by assessing the customer's inherent risk, meanwhile the Institution can analyse a transaction flow by assessing the inherent risk of Institution's products, or the Institution may assess these risk factors under the geography risk category. No matter which approach is chosen by the Institution, it should be clearly reflected in the Institution's risk assessment methodology.

Additionally, the Institutions should adequately assess also ML/TPF and sanctions risk of Latvia, including, taking into account the ML/TPF risk assessment provided in the national risk assessments, and taking into account the location of Latvia and its economic and other connections with countries subject to sanctions in context of the sanctions risk. It has been established within the framework of the Inspection that the majority of Institutions, regarding the

²³ Wolfsberg's Guidelines, p. 9. Available here: [- Anti-Money Laundering Risk Assessments FAQs \(2014\) \(wolfsberg-group.org\)](https://www.wolfsberg-group.org/aml/anti-money-laundering-risk-assessments-faqs)

geographic risk category, perceive Latvia as a country with low ML/TPF and sanctions risk.

Example of good practice

An Institution, when assessing the geographical risk category, takes into account jurisdictions related to the Institution, customers and payment flow

When assessing the geographical risk, the Institution analyses and assesses risks posed by the jurisdictions where the Institution operates, jurisdictions to which the customers are connected to and jurisdictions from which and to which payment flow goes. The Institution has evaluated and determined a separate ML risk level and TF level for each country. The Institution has scored Latvia as a country with average ML risk and low TF risk, considering the score provided also in the national risk assessment.

Examples of bad practice

- A. An Institution does not assess the payment flow from and to high-risk jurisdictions

Some Institutions do not analyse the payment flow data. Meanwhile, some Institutions assess restricted payment flow data. For example, an Institution, when assessing the geographical risk factor for ML risk, assesses the incoming payment flow from high risk countries, but does not assess the outgoing payment flow. Meanwhile, the Institution, when assessing the PF for ML risk, assesses the incoming payment flow from high risk countries, but does not assess the outgoing payment flow.

- B. Not all factors linking a customer with a certain jurisdiction are considered

Some Institutions, when assessing the customers' connection with high risk jurisdictions, take into account only limited factors that connect a customer to certain jurisdiction. For example, certain Institutions do not analyse the jurisdiction in which the customer carries out its business activities.

2.1.5.3. Assessment of the Inherent Products' ML/TPF and Sanctions Risk

Pursuant to Paragraph 1² of Section 6 of the AML/CTPF Law and Point 4.2 of Regulation No 126, the Institutions shall assess the risk of services and products used by the customer, namely, a risk that the customer can use a particular service or product, due to its functionality and features, for ML, TF, PF or to circumvent or violate sanctions. The Institutions, when assessing their products' risk, should determine clear risk factors that shall be assessed to determine the risk posed by each product or service offered by the Institution.

Examples of good practice

A. Detailed analysis of products' ML/TPF risk factors

An Institution analyses a broad range of risk factors regarding the products' risk category. An explanation is provided about each product or service offered by the Institution in the risk assessment report – why the product is scored at certain risk level, explaining what are the functionalities and features of the product that pose ML/TPF risk. The Institution assesses regarding each product how many customers of the Institution use the product in question. The Institution scores ML and TF risk level of the product separately. For example, the Institution analyses the following risk factors – possibility for anonymity, an opportunity for persons who are not customers of the Institution to use the product, high or absent limits, opportunity for customers to use the product remotely, potential options on how to use the product and an existence of cross-border element (i.e. a possibility to use products in other countries or to perform cross-border transactions). In addition to the mentioned risk factors, other Institutions assess the following factors – access to cash, a possibility to make overpayment or drawback.

B. Product's ML/TF risk score conforms to the one determined in information sources

An Institution's ML/TF risk assessment methodology provides that the ML/TF risk level assigned by the Institution to a product offered by the Institution shall correspond to the risk score of such product determined in the external information sources (for example, EU risk assessment, national risk assessment etc.). The methodology demands the Institution to provide clear justification on why the product offered by the Institution has higher or lower ML/TF risk score than the one provided in the external information sources, if the Institution scores ML/TF risk level differently.

Example of bad practice

An Institution assesses the risks posed by various products separately, but does not analyse risks posed by the product combination

It was found in the Inspection that some Institutions analyse the offered products or services separately, by assessing the ML/TF and sanctions risk inherent in them, but does not adequately account for a condition that the product is mostly used together with other products of the Institution. For example, the Institution, when assessing the product risk for the payment cards and accounts, indicate that a product that was assessed separately cannot be used for ML/TF alone, because it can be used for ML/TF only in conjunction with other products. The Institution

does not take into account the risks to which the product combination would be subject to when determining the risk level individually for each product.

2.1.5.4. Assessment of the Inherent Delivery Channels' ML/TPF and Sanctions Risk

Pursuant to Paragraph 1² of Section 6 of the AML/CTPF Law and Point 4.2 of Regulation No 126, the Institutions shall assess the risk of delivery channel of services and products that is linked to a way (channel) in which the customer obtains and uses the service or product. When assessing the delivery channel risks, it would be important for the Institutions to identify and assess all delivery channels through which the customer obtains and uses a service or a product.

Example of good practice

Delivery channels through which the products or services are obtained and used are assessed

An Institution assesses both delivery channels related to obtaining a product or service and channels related to their use. For example, the following delivery channels and related risks are assessed: online banking and mobile bank, reception of services in the Institution's branches in person, ATMs, contact centres, remote establishment of business relations, services provided over phone or via mail. When assessing a risk of various delivery channels, the Institution provides an assessment of vulnerabilities related to the delivery channel, thus determining what the risk level of a particular delivery channel is, as well as assesses how many customers of the Institution uses the delivery channel and how the dynamics of its use has changed in comparison to previous risk assessment results.

Example of bad practice

Delivery channels through which the products or services are used are not assessed

It was found in the Inspection that some Institutions do not assess all risks related to the delivery channels. For example, an Institution, within a framework of assessing delivery channels risk category, assesses only risk factors that are related to channels, through which the product or service is obtained. Namely the Institution assesses the following factors – whether an account was opened in person, remotely by using proper technological solutions, remotely by using remote technology solutions that are not safe enough, whether an account was opened by means of agents or that there is no information about the way the account was opened. Latvijas Banka believes that the indicated risk factors are adequate for assessing the risk related to channels through which the product or service is acquired. However, additionally it is necessary to assess the delivery

channels risks that are related to the channels, through which the products are being used.

2.2. The Assessment of the Efficiency of the Controls for Managing ML/TPF and Sanctions Risk

Pursuant to Points 10 and 20 of the Guidance Manual, the second phase in the process of assessing ML/TPF and sanctions risk is the assessment of efficiency of ML/TPF and sanctions risk management measures, i.e. the controls. The goal of assessment of risk management measures, i.e. the controls of ML/TPF and sanctions risk is to assess whether the controls introduced by the Institution can sufficiently manage and mitigate the ML/TPF and sanctions risk inherent in the Institution and to identify shortcomings in the controls introduced by the Institution.

In order to ensure that the Institutions conduct ML/TPF and sanctions risk assessment that corresponds to their operation and statutory requirements, the Institutions in their ML/TPF and sanctions risk assessment methodologies should clearly determine a method how the controls are assessed, including to determine the responsible parties and the internal and external information sources, which shall be taken into account when assessing the controls. The Institution's ML/TPF and sanctions risk assessment methodology should also contain an explanation on how the controls are assessed, i.e. what factors should be identified to assess the control as "non-conforming", "improvement are necessary" or "conforming" (there can be categories for assessing controls determined by the Institution). In order to demonstrate that the control assessment performed by the Institution conforms to the Institution's methodology, and to demonstrate that the Institution in accordance with the results of the risk assessment has assessed the necessity to improve the Institution's ICS as required by the statutory requirements, then the Institution's ML/TPF and sanctions risk assessment report should contain information also about reasons why a particular score has been allocated to the control in question, by providing a justification for the particular score. If the Institution in ML/TPF or sanctions risk assessment identifies shortcomings in the efficiency of controls, the Institution should assess a necessity to improve the efficiency of a particular control or note that the elimination of shortcomings is ongoing.

According to the Wolfsberg's Guidelines, the Institutions may choose to carry out a general assessment of the efficiency of controls in regard to the Institutions' ML/TPF and sanctions risk management, by assessing the efficiency of categories of controls, for example, conduct customer due diligence measures, transaction

monitoring, reporting suspicious transactions etc.²⁴. In this case the Institutions should map the respective controls by identifying specific control measures and grouping them into categories that are assessed separately.

Meanwhile to ensure that the risk assessment corresponds to the type and extent of the Institution's operations, the Institution with a broader type and extent of activity should consider assessing the controls for each risk factor individually. Because a general assessment of the efficiency of controls might not necessarily provide sufficient and objective understanding of the efficiency of controls applied by the Institution for managing various inherent risk factors. In order to do so the Institution may perform controls mapping in order to identify specific types of controls that are required to manage the inherent ML/TPF and sanctions risk that are specifically inherent to the Institution and assess whether the Institution has introduced such controls that are necessary to manage the respective inherent risks and whether the introduced controls are applied efficiently.

The Wolfsberg's Guidelines²⁵ stipulate that the Institutions should allocate different weighing for various controls, which are assessed within the framework of ML/TPF and sanctions risk assessment. In the opinion of Latvijas Banka, the allocation of weighing allows to assess the efficiency of ML/TPF and sanctions risk management controls more accurately and, therefore, to determine the Institution's residual ML/TPF and sanctions risk with more precision. The method of determining the weighing will depend on the chosen overall ML/TPF and sanctions risk assessment methodology, for example, whether the Institution identifies and assesses controls that mitigate certain risk factors individually or whether the Institution performs a general assessment of the controls. Individual control elements have a more significant role in mitigation or management of ML/TPF and sanctions risk than others. For example, in general such control elements as transactions' monitoring and customer due diligence measures are more significant in terms of managing or mitigating ML/TPF and sanctions risk than, for example, staff training. The Institutions can take into consideration the example provided in the Wolfsberg's Guidelines²⁶ in relation to the weighting of controls. If the Institution chooses to allocate different weighing to different control elements, then this should be determined in the Institution's ML/TPF and

²⁴ The Institutions may view the breakdown of controls categories in Wolfsberg's Guidelines on p. 7. Available here: - [Anti-Money Laundering Risk Assessments FAQs \(2014\) \(basel.institute\)](#)

²⁵ Wolfsberg's Guidelines, p. 12. Available here: - [Anti-Money Laundering Risk Assessments FAQs \(2014\) \(wolfsberg-group.org\)](#)

²⁶ Wolfsberg's Guidelines, Annex I. Available here: - [Anti-Money Laundering Risk Assessments FAQs \(2014\) \(wolfsberg-group.org\)](#)

sanctions risk assessment methodology, and a justification or explanation for allocating various weighing should be provided.

Wolfsberg's Guidelines²⁷ stipulate that in order to assess the efficiency of controls of ML/TPF and sanctions risk management, both design and operating efficiency of controls should be assessed. The said guidelines stipulate also that the assessment of efficiency of controls should reflect the actual situation on the moment of carrying out the risk assessment. Improvements or changes in controls, which the Institution plans to introduce in future, or which are being introduced but not completed yet, should not be taken into account when assessing the efficiency of controls.

Generally, it was observed during the Inspection that the Institutions chose to assess the efficiency of controls generally by assessing the categories of controls regarding the management of the Institution's ML/TPF and sanctions risk. In the opinion of Latvijas Banka, such approach to assessing controls does not always provide a sufficient understanding of the efficiency of the assessed controls of the Institutions regarding various risk factors, especially for the Institutions which have a broad range of services and products and extensive customer base, as well as in the risk assessments of the Institutions where the Institutions perform a joint assessment of ML/TPF and sanctions risk.

Examples of good practice

A. Institution's ML/TPF risk assessment methodology provides a clear procedure for control assessment

Institution's ML/TPF risk assessment methodology provides a clear procedure for assessing the controls, including, but not limited to:

- a procedure has been determined as well as steps that shall be taken to assess the efficiency of controls, as well as persons in charge for each step;
- the Institution assesses controls by analysing whether the control can efficiently manage the inherent ML/TPF risk factors identified by the Institution by assessing the efficiency of controls for each risk factor separately. In addition to the individual elements of controls, which directly reduce or manage particular ML, TF or PF risk factors, the general controls that apply to ML/TPF risk management are assessed;
- controls are assessed taking into account their design (functional) and operating efficiency. Within the framework of assessing the efficiency of controls' design, the Institution assesses whether the determined control has been introduced in the Institution, including whether it has been determined in the procedures and policies, and whether the control

²⁷ Wolfsberg's Guidelines, p. 11. Available here: [- Anti-Money Laundering Risk Assessments FAQs \(2014\) \(wolfsberg-group.org\)](#)

- considering its design, is suitable for managing ML/TPF or sanctions risk or whether it is suitable for managing a certain ML or TF risk. Meanwhile, when assessing the operating efficiency of the controls, the Institution assesses whether the relevant control has been actually applied and performed, and if it is done according to the design and aim of the relevant control. The Institution assesses the operating efficiency on the basis of certain proof of control's operation, for example, assessment of the whether the key performance indicators are met, internal or external audit reports, reports of compliance function, regulator's inspection reports, information on quality of submitted reports provided by the Financial Intelligence Unit, quality control inspections, management reports etc.;
- specific Institution's internal and external information sources that must be taken into when assessing the operating efficiency of controls have been determined;
 - the methodology explains how exactly the efficiency level of controls is determined by explaining what factors must be identified to allocate a particular score;
 - the methodology explains the mathematical model by which the general efficiency level of each risk category (for example, customer risk category) is calculated. For example, the Institution has determined that the assessment of general controls that apply to entire management of ML/TPF risks influences 10 % of that particular control efficiency assessment, whereas the remaining 90 % consist of individual control elements which directly mitigate or manage certain risk factors that apply to the risk factor in question;
 - assessment of control requirements should include information about certain shortcomings that were identified regarding the control elements (if identified) and certain actions to take to prevent the identified shortcomings.
- B. When assessing the efficiency of controls, the Institution takes into account the number of customers or transactions the relevant control is being applied to

In relation to the Institution's ML/TF risk assessment methodology, the Institution takes into account the number of customers and transactions subject to the particular control. Namely, if many customers or transactions are subject to the particular control element, then, when assessing the efficiency of control, the Institution must take into account that such control must have higher automation level and must be more sophisticated to assess the control as efficient (for example, controls for risk factor covering thousands of customers should be more sophisticated and more automated, in comparison to the controls of the risk factor covering only few customers).

C. Institution's ML/TPF and sanctions risk assessment methodology determines various weighing for different controls

Institution's ML/TPF and sanctions risk assessment methodology contains predefined categories of risk management or mitigation controls and their subcategories. The Institution has determined a weighting for each sub-category of controls that shall be considered when calculating the overall score for the particular category of controls. As well as the Institution has determined the weighting for each category of controls that shall be considered when calculating the overall level of efficiency of all controls. In addition to that, the Institution's methodology explains the following logics of allocating weighing – the Institution points out that weighing has been allocated on the basis of internationally recognised recommendations, external consultant recommendations and professional experience of persons in charge of group's AML/CTPF and sanctions risk management.

D. Differences in control elements are taken into account in the management or mitigation of various types of risks

The Institution in its sanctions' and PF risk assessment has individually identified and assessed the control elements that were introduced directly to manage or mitigate PF risk, and it individually assesses the control elements for the management of sanctions risk. Meanwhile, other Institution which performs a common ML/TPF and sanctions risk assessment individually assesses controls for ML/TPF risk mitigation and controls for sanctions risk mitigation, which are evaluated by answering pre-defined questions.

Examples of bad practice

A. The operating efficiency of controls is not assessed or is assessed insufficiently

Individual Institutions assess controls by assessing only whether the control exists. For example, the Institution provides a general description on what controls have been introduced in the Institution, and then provides its efficiency score, without assessing if the control is suitable for ML/TPF or sanctions risk management or mitigation, or if the control actually is applied and works efficiently. Meanwhile, other Institutions provide general description of control and general evaluation of the efficiency of control's design and operational efficiency, however they do not provide sufficient substantiation of such evaluation. For example, an Institution in its sanctions and PF risk assessment assesses the control design and operational efficiency as "efficient", but in some cases it does not provide any substantiation or explanation for allocating the particular score. Meanwhile, other Institution has not determined clearly enough what factors must be met to assess the controls at certain level, therefore it is not

clear why certain score is allocated to controls. For example, in cases when the Institution identifies shortcomings in control efficiency, which, *prima facie*, are not minor, the control is scored as "conforming" (i.e. it receives the highest score).

- B. The controls are assessed in general, without providing a sufficient insight into how they are able to efficiently mitigate the inherent risk of the Institution

Some Institutions assess the controls generally, scoring them by categories (customer due diligence measures, transaction monitoring etc.). One cannot ascertain from the controls assessment performed by the Institution that the Institutions have assessed and gained certainty on whether the existing controls can manage or mitigate the ML/TPF or sanctions risk inherent to the specific Institution.

- C. There is no weighting determined to different ML/TPF or sanction risk management controls

Some Institutions do not determine different weighing for control measures and, when determining the total efficiency level of controls for a certain risk category (for example, customer risk category) or general level of efficiency of the Institution's controls, equal value or weighing is allocated to all control elements.

- D. The Institution assesses the efficiency of controls only for those inherent ML/TPF risk factors which the Institution has scored as high

It was established in the Inspection that the ML/TPF risk assessment methodology of a certain Institution determines that in order to assess the controls for ML/TPF management the Institution identifies those aspects of the Institution's activity, which has a high inherent ML/TPF risk, and assesses what will be the residual risk level after the controls have been applied. It can be concluded from the aforesaid that the Institution does not assess the efficiency of controls for those inherent risk factors, which are scored to have low or medium inherent ML/TPF risk.

2.3. Assessment of the Residual ML/TPF and Sanctions Risk

According to Articles 10 and 20 of the Guidance Manual, once the Institution's inherent ML/TPF and sanctions risk assessment and assessment of the efficiency of controls for management of the said risks has been conducted, the third phase in the assessment of ML/TPF and sanctions risk is determining the residual risk. The residual risk is a risk which remains after the inherent risk is subject to controls. Accordingly, the goal of determining the residual risk, is to find out if the controls applied by the Institution are sufficient for the Institution to efficiently manage its ML/FP and sanctions risk.

When conducting the ML/TPF and sanctions risk assessment, it is possible to use different risk assessment matrices, with various levels of detailing, for example, as determined in Point 15 of the Guidance Manual. According to Point 16 of the Guidance Manual, the risk score matrix applied by the Institution shall depend on the type of activity, size and customer base of the Institution. Regardless of the chosen residual risk assessment matrix, the Institutions in their ML/TPF and sanctions risk assessment methodology, should include the residual risk assessment matrix chosen by the Institution and determine a procedure for assessing the residual risk, as well as the procedure for determining the total residual risk for each risk category or the total residual risk level of the Institution's ML/TPF and sanctions risk.

Pursuant to Article 14 of the Guidance Manual, when calculating the residual risk according to the formula given in Point 10 of the Guidance Manual, more weight must be allocated to the inherent risk, because no matter how efficient the ICS is, the existing or the inherent risk cannot be mitigated to zero. Therefore, in the opinion of Latvijas Banka, if, for example, the Institution uses three-level residual risk scoring matrix (low, average, high), the Institution, when scoring the residual risk, should determine only such principles for scoring the residual risk that do not permit that high inherent risk can be mitigated to low residual risk regardless of the efficiency level of controls implemented by the Institution.

In general, it was concluded in the Inspection that the Institutions with some exceptions have a clear procedure determined for scoring the residual ML/TPF and sanctions risk, and that the Institutions assess the residual risk according to a procedure stated by them. Generally, the Institutions determine the residual risk according to the formula stated in Points 10 and 20 of the Guidance Manual, but a different approach was detected regarding the mathematic models or principles according to which the Institutions determine residual risk and what gradation of the residual risk the Institutions apply. Institutions' approaches differ in regard to whether they score only the total residual ML/TPF or sanctions risk or determine the residual risk for various risk factor categories. Overall, no such shortcomings were found that would apply to majority of the inspected Institutions.

Example of good practice

Risk-based approach is used for assessing the residual risk

According to an Institution's ML/TPF risk assessment methodology, the principles for assessing the residual risk include a risk-based approach. Namely, the higher the inherent risk factor, the higher the control efficiency relevant for the particular risk factor must be scored (in per cent), in order to affect the residual risk level positively. For example, if the inherent risk level of a certain risk factor has been scored as "medium", then in order to score the residual risk level as

"love" the controls of that particular risk factor should have at least 60 % efficiency. Meanwhile, if the inherent risk level of a certain risk factor is scored as "high", then the controls must have at least 70 % efficiency so that the residual risk level could be scored as "medium".

Examples of bad practice

- A. An Institution's methodology provides that a high inherent risk can be reduced to low risk

In some Institutions ML/TPF or sanctions risk assessment methodologies provide that a high inherent risk can be reduced by means of certain efficiency level of controls to low residual risk. Besides, one Institution has such methodology which contains a mathematical residual risk assessment model, permitting that the residual ML/TPF and sanctions risk may be scored as zero.

- B. An Institution's methodology does not provide a clear procedure for assessment of the residual ML/TPF and sanctions risk

A ML/TPF and sanctions risk assessment methodology of one Institution does not contain information about the procedure for assessment of the residual risk. The methodology includes only general information and therefore the principles according to which the Institution assesses the residual ML/TPF and sanctions risk is not clear.

Meanwhile, the internal regulations of another Institution stipulates that the residual risk of the Institution is determined taking into account the likelihood of a relevant risk and its impact on the Institution. A single matrix is used to determine the inherent risk and residual risk of the Institution. It can be concluded from the Institution's methodology that the residual risk of the Institution does not depend on the efficiency score of Institution's controls. For that reason, it is not clear how the Institution arrives at the residual risk results.

- C. The Institution determines only the total residual risk inherent in the Institution

The Institution determines only the total residual ML/TPF and sanctions risk inherent in the Institution, but does not determine the residual risk for various risk factor categories in more detail. Therefore, it is not clear from the Institution's risk assessment which risk factors or categories of risk factors or efficiency of which controls directly influence the residual risk level of the Institution.

- D. The institution does not assess the Institution's residual ML/TPF or sanctions risk

The Inspection concluded that certain Institutions do not assess the residual risk in their ML/TPF or sanctions risk assessment.

3. The Results of the Institutions' ML/TPF and Sanctions Risk Assessment and the Action Plan for Risk Management or Mitigation

3.1. Analysis of the Results of the ML/TPF and Sanctions Risk Assessment and Conclusions

The Wolfsberg's Guidelines²⁸ stipulate that the Institutions should assess whether the residual risk level in ML/TPF and sanctions risk assessment corresponds to the ML/TPF and sanctions risk appetite determined by the Institution. Thereby, the Institutions can ensure that its risk appetite corresponds to the actual risks of the Institution and the Institutions can make decisions on taking necessary measures to eliminate any discrepancies. The mentioned Guidelines²⁹ also recommend the Institutions to make a comparison to Institution's risk assessment results from previous periods. In that way, the Institutions may form an understanding on changes in risks they are exposed to, and on changes in the efficiency of their risk management measures in a longer run.

In order to demonstrate that the Institution's risk assessment has ensured that the Institution has identified and understood their inherent risks, the Institutions are advised to make conclusions on the main inherent ML/TPF and sanctions risks to ensure that, according to a risk-based approach, they may ensure that more attention is paid to mitigating or managing risks which are material for that particular Institution.

Generally, it was concluded within the framework of the Inspection, that many Institutions in their assessment reports do not draw general conclusions on the risk assessment results. It was observed that each risk assessment phase (inherent risk score, assessment of controls and residual risk score) in the Institution is conducted according to the methodology by arriving at the total residual risk assessment or assessment across various risk categories. But such results, which most often is reflected as a brief table, is not followed by a qualitative analysis on the obtained data, including on whether the determined risk level corresponds the Institution's risk appetite, and Institution's trends regarding their risk assessment results in a long-term are not compared.

Examples of good practice

²⁸ Wolfsberg's Guidelines, p. 15. Available here: [- Anti-Money Laundering Risk Assessments FAQs \(2014\) \(wolfsberg-group.org\)](#)

²⁹ Wolfsberg's Guidelines, p. 4. Available here: [- Anti-Money Laundering Risk Assessments FAQs \(2014\) \(wolfsberg-group.org\)](#)

A. Results of ML/TPF risk assessment are compared to the Institution's risk appetite

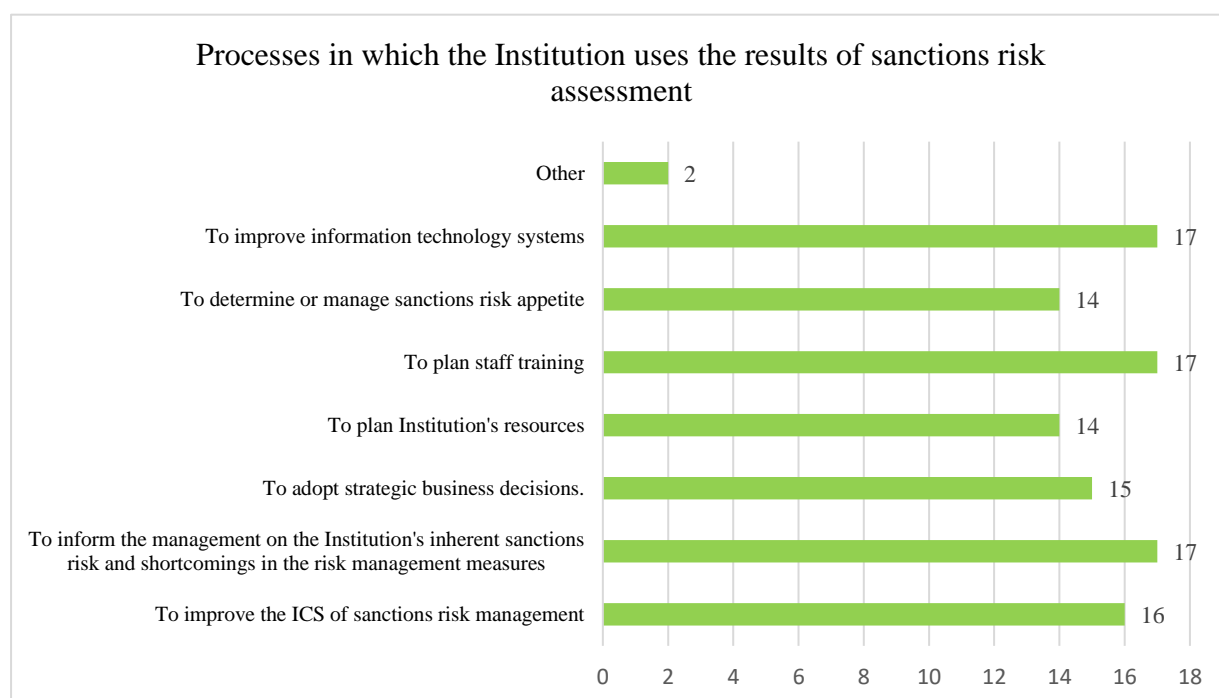
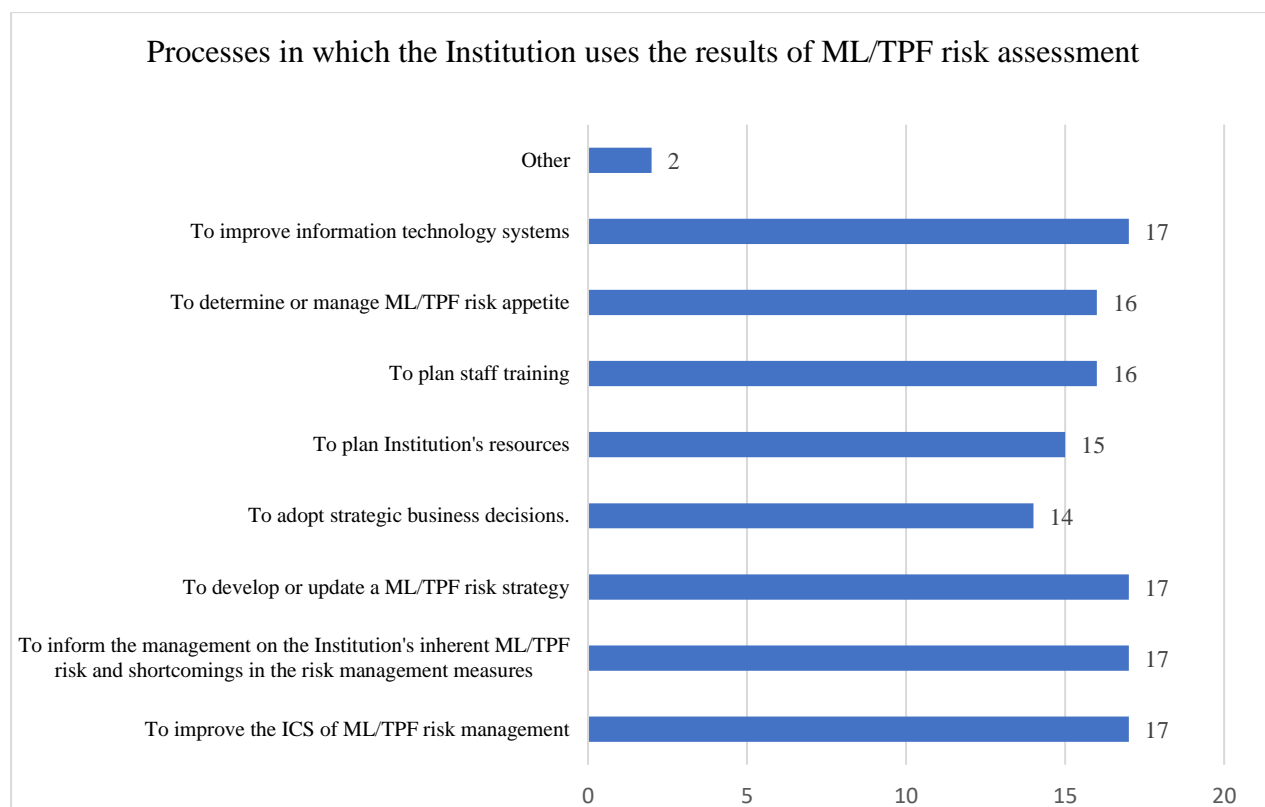
An Institution, within the framework of risk assessment, compares the residual ML/TPF risk with the Institution's ML/TPF risk appetite. According to the Institution's risk assessment methodology, the goal of such analysis is to conclude if the actual ML/TPF risk of the Institution matches the Institution's determined risk appetite, and if the risk does not match the risk appetite, then to determine measures that shall be taken to eliminate such discrepancy. In addition to that, the Institution's methodology lays down the priority for different measures, taking into account the conclusions drawn from comparing the ML/TPF residual risk results to Institution's risk appetite. For example, if it is concluded that the residual risk does not fall within the limits of Institution's risk appetite, the methodology in such case stipulates certain order for addressing such situation and it has been determined that such measures that have to be taken to address this issue must be with high priority.

B. Comparison of the ML/TPF or sanctions risk assessment results with the results of previous years

An Institution in its ML/TPF risk assessment report compares certain inherent risk factor score, as well as the efficiency score for controls against the results of previous risk assessment results. Additionally, if the score of a risk factor or control element differs from the results of previous risk scores, the Institution identifies the main reasons for such change. If the resulting risk factor score cannot be compared to the previous risk score, because the risk assessment methodology has changed, the Institution identifies it and indicates in risk assessment report.

3.2. Using the Results of the Risk Assessment in Various Processes of the Institution

Pursuant to the AML/CTPF Law and Regulation No 126, the Institutions shall create the ICS for AML/CTPF and sanctions risk management, on the basis of ML/TPF and sanctions risk assessment and take into account the results of the risk assessment regarding the improvement of the ICS. Further Charts show the purposes for which the Institutions use the results of ML/TPF and sanctions risk assessment.



In addition to the indicated processes, two Institutions pointed out that they use the results of both ML/TPF and sanctions risk assessment for "other" processes, i.e. the Institution uses the results to inform the group's companies on the risk

inherent to the Institution and another Institution uses the results to develop new products or services or improve and modify the existing ones.

Generally, it can be concluded that the Institutions use the results of ML/TPF and sanctions risk assessment for various processes which are necessary for efficient management of the Institution's risk and improvement of the ICS. Latvijas Banka holds a view that it would be important to take into account the risk assessment results in all of the processes indicated in previous two Charts, which are part of the Institution's ICS of AML/CTPF and sanctions risk. It can be concluded from the Inspection's results that not all Institutions use their risk assessment results for all of the aforesaid processes.

Example of good practice

ML/TPF and sanctions risk assessment methodology clearly states the purposes for which the risk assessment results must be used

An Institutions ML/TPF and sanctions risk assessment methodology clearly states the purposes for which the risk assessment results shall be used. Namely, the results of the Institution's risk assessment must be used to ensure that its resources and priorities comply with the risks to which the Institution is exposed to. The risk assessment results must be used to assess whether the Institution's residual risk matches or exceeds the determined risk appetite of the Institution, to make improvements in the internal regulations, processes and risk management measures or controls, and the results must also be used to identify a need to carry out activities for to improve the awareness of risks within the Institution's, and for preparing training plans. The Institution's methodology contains a requirement that such measures must be defined in the risk management action plan, which has to be elaborated within the framework of ML/TPF and sanctions risk assessment.

Examples of bad practice

- A. The results of sanctions risk assessment are not used to improve Institution's ICS of sanctions risk management

One Institution does not use the results of the sanctions risk assessment to improve the Institution's ICS for sanctions risk management.

- B. The results of ML/TPF or sanctions risk assessment are not used for the planning of Institution's resources

Some Institutions do not use the results of ML/TPF or sanctions risk assessment to plan Institution's resources.

- C. The results of ML/TPF or sanctions risk assessment are not used to manage or determine the institutions risk appetite

Several Institutions do not use the results of ML/TPF or sanctions risk assessment to manage or determine the ML/TPF or sanctions risk appetite.

- D. The results of ML/TPF risk assessment are not used for the planning of staff training

The Institution points out that it does not use the results of ML/TPF risk assessment to plan the staff training.

- E. The results of ML/TPF or sanctions risk assessment are not used for making strategic business decisions

Part of the Institutions stated that they do not use the results of ML/TPF or sanctions risk assessment to adopt strategic business decisions.

3.3. Informing the Involved Parties about the Results of the ML/TPF and Sanctions Risk Assessment

Since the Institution's management is primarily responsible for the management of ML/TPF and sanctions risk, the Institutions should use the risk assessment results also to inform the Institution's management about the risks inherent in the Institution and shortcomings in the risk management. In addition to the above, other parties involved, including those who are directly impacted by the ML/TPF and sanctions risk or which are responsible on daily basis for implementing certain controls, must be informed about the results of ML/TPF and sanctions risk assessment. The Institutions should provide clear procedures for identifying and informing the parties involved as well as those in charge of these processes.

Example of good practice

Relevant employees are informed about the risk assessment results

The Institution provides information about the results of ML/TPF and sanctions risk assessment to Institution's staff which need to know the ML/TPF and sanctions risk inherent in the Institution due to their job responsibilities, by reporting about current efficiency of Institution's ML/TPF and sanctions risk management system, on the residual ML/TPF and sanctions risk of the Institution, and the main identified ML/TPF and sanctions risks. Training is provided by the Institution's Know Your Customer competence centre in cooperation with the AML/CTPF Department of the Institution's group. The responsible structural units of the Institution, on the basis of the results of ML/TPF and sanctions risk assessment, prepare a proper presentation, determine employees of the Institution that need to undergo training, and ensure that relevant employees are acquainted with the training materials and pass a specific test.

Example of bad practice

The involved parties are not being informed about the results of ML/TPF or sanctions risk assessment or the procedure of informing the involved parties is not determined

Some Institutions inform about the risk assessment results only its management, but not other units or employees of the Institution which are affected by the identified risks or their management measures. Additionally, it was identified for some Institutions that the internal regulations do not provide for a procedure on how to inform the involved parties on the results of risk assessment or do not determine a person in charge of that process. For example, one of the mentioned Institutions does not have a separate requirement to inform its management on the results of ML/TPF and sanctions risk assessment. The Institution has only general requirements which intend to inform the management on the Institution's risks (all risks rather than just ML/TPF and sanctions risk) on a quarterly basis.

3.4. The Action Plan for Risk Management or Mitigation

Since, on the basis of the risk assessment results, the Institutions must create and improve the ICS for AML/CTPF and sanctions risk management, the Institutions, according to the results of ML/TPF and sanctions risk assessment, should elaborate an action plan for the risk management or mitigation. In order to fulfil this requirement, the Institutions in their internal regulations should determine a requirement on preparation and confirmation of the action plan as well as a requirement to supervise the implementation of the action plan.

In order to demonstrate compliance with the regulatory framework requirements which state that, according to the risk assessment results, the ICS should be improved if needed, the Institutions must always assess the need to elaborate an action plan, including, if the Institution has identified shortcomings in a design or efficiency of risk management measures or controls, as well as if according to the Institution's risk assessment results the risks do not match the risk appetite determined for the Institution. Institution's internal regulations should determine a requirement on preparation and confirmation of the action plan as well as a requirement to supervise the implementation of the action plan.

Generally, it was concluded in the Inspection that majority Institutions in their internal regulations have determined a requirement to elaborate a risk management or mitigation action plan according to the results of their ML/TPF and sanctions risk assessment and supervise its implementation. However, some bad practice examples have been identified, which are specified in continuation. Overall, regarding a risk mitigation action plan no shortcomings characteristic to the majority of the inspected Institutions were found. Note, the Inspection did not assess how efficiently the Institutions actually implement and supervise the implementation of their action plans.

Examples of good practice

- A. An Institution's ML/TPF and sanctions risk assessment methodology provides a procedure for implementation and supervision of the action plan and on informing the management

The Institution's ML/TPF and sanctions risk assessment methodology states that the supervision of action plan implementation is carried out by the compliance function on a quarterly basis. It evaluates the progress of action plan and prepares a report on the performance status of the action plan which is presented to the management on a quarterly basis.

- B. The Institution ensures the resources necessary for the risk management action plan

The Institution points out that not only it supervises the implementation of an action plan, but the Institution's management ensures sufficient allocation of resources (including human resources) for risk mitigation or management that are necessary to implement the action plan measures.

Examples of bad practice

- A. The Institution's internal regulatory enactments do not include a requirement to elaborate an action plan for the risk management or mitigation according to the results of ML/TPF and sanctions risk assessment

Separate Institutions in their internal regulations have not included a requirement to elaborate an action plan for the risk mitigation or management according to ML/TPF risk assessment results.

- B. A risk owner is the only one responsible for elaboration of ML/TPF or sanctions risk management or mitigation action plan

In some Institutions the relevant risk owner is the only person responsible for elaboration of the risk management or mitigation plan. Hence, there is no coordination of single action plan in the Institution at the level of management or other responsible function, as well as it was not possible to confidentially conclude from the submitted documents that Institutions' management confirm the action plans developed by the risk owners, besides such requirement is not determined also in the internal regulations of the Institutions.

- C. A person in charge of fulfilment of the risk management or mitigation action plan and procedure of relevant supervision are not determined in the Institution's internal regulatory enactments

A part of the Institutions in their internal regulations do not have a predefined procedure or person in charge for supervision of the action plan implementation,

as well as of informing the management about the status of the action plan's implementation.

- D. Institution's internal legislation requires to elaborate the action plan only regarding an identified high residual ML/TPF risk

Institution's AML/CTPF methodology provides that an action plan and risk mitigation measures must be determined only regarding mitigation of such ML/TPF risk which is scored in the risk assessment as having high residual risk. In the Institution's methodology other situations when the action plan could be elaborated are indicated as examples, but it is not stated as a mandatory requirement to elaborate the action plan. Accordingly, for example, if the Institution has identified shortcomings in the risk management measures or efficiency of controls, the Institution's methodology does not oblige it to elaborate an action plan.

- E. According to the results of ML/TPF or sanctions risk assessment, an action plan for the risk management or mitigation has not been elaborated even though the report has identified shortcomings of controls

Certain Institutions which have identified shortcomings in ML/TPF or sanctions risk assessment regarding risk management controls design or efficiency have not assessed a need for elaboration of risk management or mitigation action plan and also have not elaborated the action plan.

3.5. Storage of ML/TPF and Sanctions Risk Assessment's Documentation

In the opinion of Latvijas Banka, the Institutions must ensure that all documentation related to ML/TPF and sanctions risk assessment is stored. The Institution's internal regulatory enactments should provide a procedure and person in charge of storing the documentation related to risk assessment.

Example of good practice

Internal legislation includes requirements for document retention

Institution's ML/TF risk assessment methodology provides a procedure for retention of documentation of ML/TF risk assessment and persons in charge by determining a retention term, document classification regarding confidentiality as well as format in which the document must be stored. Additionally, responsibility and demand to document and store the minutes of management meetings which have ML/TF risk assessment results presented, together with the ML/TF risk assessment documentation, are outlined.

Report | 28.06.2023.

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Annex I Abbreviations Used in the Report

| Term | Abbreviation Used |
|---|--------------------------|
| Financial and Capital Market Commission | Commission |
| The horizontal off-site inspection "The Horizontal Inspection of Money Laundering, Terrorism and Proliferation Financing and Sanctions Risk Assessment Process Including Methodology" | Inspection |
| Report on the Inspection's results | Report |
| Institutions assessed within the framework of the Inspection, mentioned in the Section II of the Report | Institutions |
| Money laundering and financing of terrorism and proliferation | ML/TPF |
| Anti-money laundering and combating of financing of terrorism and proliferation | AML/CTPF |
| Money laundering and terrorist financing | ML/TF |
| Money laundering | ML |
| Terrorism financing | TF |
| Proliferation financing | PF |
| The Law on the Prevention of Money Laundering and Terrorism and Proliferation Financing (revision of 01.01.2023–31.01.2024) | AML/CTPF Law |
| The Law on International Sanctions and National Sanctions of the Republic of Latvia | Sanctions Law |
| Commission's Regulation No 227 of 01.12.2020 "Regulation on Establishment of Internal Control System" (revision of 01.05.2023) | Regulation No 227 |
| Commission's Regulation No 126 of 11.08.2020 "Regulation on Sanctions Risk Management" (revision of 19.08.2020) | Regulation No 126 |
| Commission's Recommendations No 169 of 21.12.2021 "Recommendations for the Establishment of the Internal Control System for Anti-Money Laundering and Countering Terrorism and | Guidance Manual |

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| Proliferation Financing and Sanctions Risk Management, and for Customer Due Diligence". | |
| Wolfsberg "Frequently Asked Questions on Risk Assessments for Money Laundering, Sanctions and Bribery & Corruption", available here: - Anti-Money Laundering Risk Assessments FAQs (2014) (wolfsberg-group.org) | Wolfsberg's Guidelines |
| United Nations | UN |
| Financial Action Task Force | FATF |
| European Banking Authority | EBA |
| European Union | EU |
| North Atlantic Treaty Organisation | NATO |
| United States of America | USA |
| Office of Foreign Assets Control of the United States of America | OFAC |
| Politically exposed person, his/her family members and persons closely related to the politically exposed person | PEP |
| Beneficial owner | BO |
| Internal control system | ICS |
| Association of Certified Anti-Money Laundering Specialists | ACAMS |
| Certified Anti-Money Laundering Specialist | CAMS |

Annex II Table of Inspection's Results

| Report's Section No | Finding | Description of the Finding | Impact of the Finding ³⁰ |
|---------------------|--|--|-------------------------------------|
| 1. | General Aspects of the Institution's ML/TPF and Sanctions Risk Assessment Methodology and Risk Assessment | | |
| 1.1 | The ML/TPF and Sanctions Risk Assessment Methodology | | |
| 1.1.1 | An Institution has not prepared such ML/TPF and sanctions risk assessment methodology that would be appropriate for the specific activities of the Institution | The Institution uses a standardised ACAMS risk assessment tool which cannot be adjusted to the Institution's specific activities. | Very high |
| 1.1.1 | The risk assessment methodology is not approved separately by the Institution's management | The ML/TPF or sanctions risk assessment methodology of an Institution was not confirmed by the Institution's management before conducting the risk assessment. This is because the risk assessment methodology is not documented separately, and instead is only included in the risk assessment report. | Medium |
| 1.1.1 | The risk assessment methodology is too general | The risk assessment methodology is too general and does not provide sufficient information on how an Institution conducts the risk assessment. | High |
| 1.1.2 | Requirements to review the ML/TPF or sanctions risk assessment methodology are not defined or are defined incompletely | An Institution has not indicated in its internal regulations the frequency for reviewing the ML/TPF or sanctions risk methodology or has not indicated certain or all of those circumstances under which the methodology must be reviewed according to the statutory regulations. | Low |
| 1.1.2 | The frequency for updating the ML/TPF or sanctions risk assessment methodology does not conform to the statutory requirements | The frequency for reviewing the ML/TPF or sanctions risk assessment methodology stipulated in the Institution's internal regulations is every three years or every 18 months, which does not correspond to the frequency stipulated in the statutory regulations – not less than once a year. | High |

³⁰ The finding that was identified as an example of bad practice was identified for its potential impact on the Institution's risk management system, risk control and Institution's management. The impact was scored as conforming to one of the following levels – very high, high, average or low. The score was allocated on the basis of the nature of the very finding identified as the bad practice rather than the number of Institutions where that finding was identified.

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| 1.1.3 | The efficiency of the ML/TPF or sanctions risk assessment methodology has not been assessed | An Institution has not carried out a regularly assessed the efficiency of the ML/TPF or sanctions risk assessment methodology. | High |
| 1.2 | The ML/TPF and Sanctions Risk Assessment | | |
| 1.2.1 | The frequency for updating the sanctions risk assessment does not conform to the statutory requirements | An Institution reviews and updates the sanctions risk assessment every three years, even though the statutory regulations determined that it shall be updated once every 18 months. | High |
| 1.2.1 | The frequency for updating the ML/TPF risk assessment does not conform to the Guidance Manual | An Institution reviews and updates the ML/TPF risk assessment every three years, even though the Guidance Manual determined that it shall be updated once every 18 months. | Medium |
| 1.2.1 | The frequency for updating the ML/TPF or sanctions risk assessment is not appropriate to the Institution's inherent risks | An Institution reviews and updates ML/TPF or sanctions risk assessment every three years, but such frequency is not appropriate to the Institution's inherent risks, even though such frequency corresponds to the statutory regulations and requirements of the Guidance Manual. | Medium |
| 1.2.1 | Risks throughout the entire risk assessment period are not being assessed | An Institution does not assess risk for the entire ML/TPF or sanctions risk assessment period, taking into account the Institution's defined frequency for reviewing the risk assessment, for example, risk assessment is carried out every three years, but in the risk assessment only data for a period of 12 months is analysed. | High |
| 1.2.2 | An Institution has not updated the sanctions risk assessment after new sanctions regimes against Russian and Belarus, which directly impact the Institution, were introduced | Sanctions of significant and unprecedented scale and type were imposed against Russia and Belarus in February 2022. However, neither of the inspected Institutions had updated their sanctions risk assessment until 1 August 2022, based on the fact that a new sanctions regime has been introduced which influences the Institution's activity, even though the mentioned is a factor which requires to update the sanctions risk assessment in accordance with the statutory regulations. But four Institutions conducted a regular sanctions risk assessment in 2022 which at least partially covered the risks posed by the mentioned sanctions. | Very high |

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| 1.2.2 | All circumstances under which ML/TPF or sanctions risk assessment must be reviewed and updated have not been determined | An Institution has not defined in its internal regulations a part or all circumstances laid down in the statutory regulations under which ML/TPF or sanctions risk assessment must be reviewed and updated. | Low |
| 1.2.2 | The ML/TPF or sanctions risk assessment has not been updated upon occurrence of such circumstances that require reviewing the ML/TPF or sanctions risk assessment | An Institution has not reviewed and updated ML/TPF or sanctions risk assessment before taking such actions which requiring updating the risk assessment, for example, changes in the compliance function's operation model and organisational structure, a new delivery channel for a product has been introduced, material changes in business model have been made etc. | High |
| 1.3 | Parties Involved in the Development of the ML/TPF and Sanctions Risk Assessment Methodology and Conducting the Risk Assessment | | |
| 1.3.1. | Parties that are involved in conducting the ML/TPF or sanctions risk assessment and their responsibilities have not been determined. | Certain Institutions have not determined those parties, which shall be involved in conducting the ML/TPF or sanctions risk assessment or their responsibility in their internal regulations. | Low |
| 1.3.1. | Institution's role in the risk assessment conducted by or with the assistance of an independent third party is not clear | Institution's role in the ML/TPF or sanctions risk assessment conducted by or with the assistance of an independent third party is not clear. | Medium |
| 1.3.1. | If an Institution's risk assessment is performed by an independent third party, the risk assessment methodology may differ from the one defined by the Institution | If the Institution's risk assessment is performed by an independent third party, ML/TPF risk assessment methods may differ from the methods stipulated in the Institution's methodology, and the data set and scope used in ML/TPF risk assessment as well as the content of information to be included in the final report may differ. | Medium |
| 1.3.2. | Training directly related to the ML/TPF or sanctions risk assessment is not provided | An Institution does not provide individual training that would be directly linked to conducting ML/TPF or sanctions risk assessment (it was found that some Institutions provide training related to ML/TPF risk assessment, but do not provide training related to conducting sanctions risk assessment). | Medium |

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| 1.4 | IT Solutions and Quality of the Data Used in the Risk Assessment | | |
| 1.4.1 | An Institution does not have the data necessary for conducting ML/TPF or sanctions risk assessment or data format is not appropriate | The Institution does not have a partial or full access to data necessary for ML/TPF and sanctions risk assessment. Therefore, the Institution cannot fully assess its inherent risks. | High |
| 1.4.1 | There are no requirements laid down on how to ensure data quality during the risk assessment process | An Institution has not determined individual requirements or measures on how to ensure the quality of Institution's quantitative or statistical data used in ML/TPF and sanctions risk assessment. However, the Institution has indicated that ensuring data quality is a routine process. | Low |
| 1.4.2 | The technological solution used in the risk assessment restricts the Institution's ability to completely evaluate its inherent risks | Considering the limitations of the technological solution used for determining a risk exposure, only the number of the Institution's customers exposed to the risk factor in question are taken into account, but it does not consider the Institution's transaction data. Therefore, the technological solution used by the Institution restricts the Institution's ability to fully assess the Institution's exposure regarding ML/TPF risk factors. However, the Institution in its risk assessment includes additional transaction data to compensate for the said shortcomings. | Low |
| 2. | The Elements of the ML/TPF and Sanctions Risk Assessment Methodology | | |
| 2.1 | The Assessment of Inherent ML/TPF and Sanction Risk | | |
| 2.1.1 | The inherent sanctions risk is not assessed | The Institution does not identify and assess the inherent sanctions risk it is exposed to. | Very high |
| 2.1.1 | No information is provided on the reasons for assessing an inherent risk factor in a certain level | An Institution in its ML/TPF or sanctions risk assessment report does not justify why a particular inherent risk factor has been assessed in a certain level. | Medium |
| 2.1.1 | The inherent risk assessment is not based on or is insufficiently based on the analysis of the Institution's quantitative data | The Institution in their ML/TPF or sanctions risk assessment does not analyse at all or does not analyse sufficiently the Institution's quantitative data regarding the customers and their transactions. | High |

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| 2.1.1 | The level of the inherent risk is assessed solely based on the exposure of the relevant risk in the Institution, without considering the nature of the risk | Institution's inherent risk level is determined only on the basis of the Institution's quantitative data regarding how many customers of the Institution (may be other quantitative data) exposed to relevant risk factor, but not taking into account the nature of the risk factor (threats and vulnerabilities). | High |
| 2.1.1 | When considering the inherent ML/TPF or sanctions risk, the controls are taken into account | An Institution, when assessing the inherent risk, takes into consideration the controls introduced by the Institution, namely the score allocated to the risk factor is justified also with the presence of controls. | Medium |
| 2.1.2 | The PF risk is not assessed at all or is assessed insufficiently | The risk factors assessed by the Institution do not cover PF risk or covers it insufficiently. | Very high |
| 2.1.2 | The TF risk is not assessed at all or is assessed insufficiently | The Inspection has not considered differences between ML and TF in the analysed risk factors, besides some Institutions have been found to not cover TF risk at all in their assessment of the risk factors. | Very high |
| 2.1.3 | The Sanctions risk assessment does not cover the sectoral sanctions risk or covers it insufficiently | The Institution does not assess or assesses the risks related to sectoral sanctions risk insufficiently. | Very high |
| 2.1.4 | The impact of sanctions imposed by the Member States of the EU and NATO is not assessed | Within the framework of sanctions risk assessment, an Institution does not regularly assess the impact of sanctions imposed by the Member States of the EU and NATO on the interests of the Institution and the financial and capital market as required by the statutory regulations. | High |
| 2.1.5 | The Institution assesses additional risk categories with no clear explanation for their individual assessment | In addition to the risk categories of customer, geography, service or product and delivery channel risks, an Institution assesses other risk categories. However, there is no clear explanation on the reason for their individual assessment, for example, certain Institutions additionally assess industry and transaction risk. | Medium |
| 2.1.5 | The sanctions risk related to the region where the Institution operates and | An Institution does not assess the risk related to region in which the Institution operates and provided services, which the | High |

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| | provides services is not assessed | Institution should be assessing in accordance with the statutory regulations. | |
| 2.1.5 | An Institution does not differ between risk management control elements and qualitative risk factors | The Institution assesses under the qualitative risks also such factors which essentially apply to the efficiency of Institution's controls. | Low |
| 2.1.5.1 | The assessed customer's risk factors are not appropriate to the Institution's customer base | The customers' risk factors assessed by the Institution are not appropriate to the Institution's customer base. | High |
| 2.1.5.1 | The risks posed by the type of customers' business activities are not identified and assessed or are assessed insufficiently | When assessing the customers' ML/TPF or sanctions risk, the Institution does not assess or does not sufficiently assess the risks posed by the customers' type of business activities. | High |
| 2.1.5.2 | The payment flow from and to high-risk jurisdictions are not assessed | An Institution does not analyse the payment flow data or analyses limited date of payment flow. | High |
| 2.1.5.2 | Not all factors linking a customer with a certain jurisdiction are considered | The Institution, when assessing the customers' link to high-risk jurisdiction, considers only restricted factors that link the customer to a certain jurisdiction, for example, does not analyse a country where the customer operates its business. | High |
| 2.1.5.3 | An Institution does not analyse risks posed by using their offered products in combination | The Institution analyses its offered products or services separately, by assessing the products' ML/TPF and sanctions inherent risk, but does not adequately account for a condition that a product is mostly used together with other products offered by the Institution. | Medium |
| 2.1.5.4 | An Institution does not assess delivery channels through which the products or services are used | The Institution assesses within the framework only the risk factors that are related to the channels of acquiring of a product or service but does not assess the channels intended for using the products. | Medium |
| 2.2 | The Assessment of the Efficiency of Controls for Managing ML/TPF and Sanctions Risk | | |
| 2.2 | The operational efficiency of controls is | An Institution assesses the controls by only evaluating whether the control exists in the | High |

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| | not assessed or is assessed insufficiently | Institution but does not assess the efficiency of that control. | |
| 2.2 | Assessment of controls does not provide sufficient insight into whether the controls are able to efficiently mitigate the inherent risk of an Institution | An Institution carries out general assessment of the controls, scoring them by categories (e.g. customer due diligence measures, transaction monitoring etc.). The controls assessment performed by the Institution does not provide sufficient insight in whether the Institution has assessed and gained certainty that the existing controls are capable to manage or mitigate the Institution's inherent ML/TPF or sanctions risk. | High |
| 2.2 | There are no weights assigned to different ML/TPF or sanctions risk controls | An Institution has not determined different weighing for control measures and, when assessing the overall efficiency of controls, it allocates equal score or weighing to all control elements. | Medium |
| 2.2 | An Institution assesses the efficiency of controls only for those ML/TPF risk factors which are scored as having high inherent risk | The Institution assesses the efficiency of controls only for those inherent risk factors which have high inherent risk, but does not assess the efficiency of controls for those inherent risk factors which are scored with low or average inherent ML/TPF risk. | High |
| 2.3 | The Assessment of the Residual ML/TPF and Sanctions Risk | | |
| 2.3 | A high inherent risk level can be reduced to a low risk level | The ML/TPF or sanctions risk assessment methodology in an Institution provides that a high inherent risk can by means of certain efficiency level of controls can be reduced to low residual risk level. | Medium |
| 2.3 | The procedure for the residual ML/TPF or sanctions risk assessment is not determined | An Institution's methodology does not contain information about the procedure on how the residual risk is being assessed, therefore the principles by which the Institution assesses the residual risk are not clear. | Medium |
| 2.3 | An Institution assesses only the total residual risk inherent to the Institution | The Institution determines only the total residual ML/TPF and sanctions risk that is inherent to the Institution. It is not clear which risk factors or categories of risk factors or efficiency of which controls directly influence the residual risk level of the Institution. | Medium |

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| 2.3 | The Institution's residual ML/TPF or sanctions risk is not assessed | The Institution does not assess the residual ML/TPF risk. | Medium |
| 3. | The Results of the Institutions' ML/TPF and Sanctions Risk Assessment and the Action Plan for Risk Management or Mitigation | | |
| 3.2 | Using the Results of the Risk Assessment in Various Processes of the Institution | | |
| 3.2 | The results of the sanctions risk assessment are not used to improve the ICS of sanctions risk management | An Institution does not use the results of sanctions risk assessment to improve the Institution's ICS for sanctions risk management. | Very high |
| 3.2 | The Institution does not use the risk assessment results for resource planning | The Institution does not use the results of ML/TPF or sanctions risk assessment to plan Institution's resources. | Medium |
| 3.2 | The Risk assessment results are not used to manage or determine the risk appetite | The Institution does not use the results of ML/TPF or sanctions risk assessment to manage or determine ML/TPF or sanctions risk appetite. | High |
| 3.2 | An Institution does not use the results of ML/TPF risk assessment for planning the staff's training | The Institution does not use the results of ML/TPF risk assessment for planning the staff's training. | Medium |
| 3.2 | The Institution does not use the risk assessment results for adopting strategic business decisions | The Institution does not use the results of ML/TPF or sanctions risk assessment to adopt strategic business decisions. | Medium |
| 3.3 | Informing the Involved Parties about the Results of the ML/TPF and Sanctions Risk Assessment | | |
| 3.3 | The involved parties are not being informed about the results of risk assessment or the procedure of informing the involved parties is not determined | The Institution informs only the management about the risk assessment results but does not inform other structural units or employees of the Institution that are affected by the identified risks or their management measures, or the Institution has not defined a procedure according to which the management or other stakeholders shall be informed about the | Medium |

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| | | assessment's results and employees in charge of that. | |
| 3.4 | The Action Plan for Risk Management or Mitigation | | |
| 3.4 | A requirement to prepare an action plan for risk management or mitigation as a result of the Institutions' ML/TPF and sanctions risk assessment has not been determined | An Institution in its internal regulations have not included a requirement to prepare an action plan for risk mitigation or management in result of the ML/TPF risk assessment. | High |
| 3.4 | The risk owner is the only one responsible for determining risk management or mitigation action plan | Only the owner of relevant risk is responsible for preparing the risk management or mitigation action plan in the Institution, therefore at the level of Institution's management or other senior function a single action plan is not determined and coordinated. | Medium |
| 3.4 | An institution has not defined in its internal regulations a procedure or person in charge of supervision of the action plan implementation | An institution has not defined in its internal regulations a procedure or person in charge of supervision of the action plan implementation, as well as of informing the management about the status of action plan implementation. | Low |
| 3.4 | The action plan must be prepared only in regard to such identified ML/TPF risk factors that have been assessed with high residual risk | Action plan and risk mitigation measures in the Institution must be determined only regarding mitigating of such ML/TPF risk factors which according to the risk assessment have been scored as having high residual risk. | Medium |
| 3.4 | Risk management or mitigation plan has not been prepared | An Institution that had identified shortcomings in its ML/TPF or sanctions risk assessment regarding risk management controls design or efficiency has not assessed a need to prepare a risk management or mitigation action plan and has not prepared an action plan. | High |