NATIONAL BANK OF SERBIA

AML SUPERVISION CENTRE

ANALYSIS OF BANKS' RESPONSES TO THE QUESTIONNAIRE ON ACTIVITIES REGARDING ML/TF RISK MANAGEMENT FOR 2019

April 2020

Introductory note

Within bank supervision, the National Bank of Serbia carries out off-site monitoring and analysis of the ML/TF risk management activities of banks. The analysis of data from the Questionnaire on Banks' Activities regarding ML/TF Risk Management (hereinafter: Questionnaire) is carried out at least once a year. In accordance with the Law on the Prevention of Money Laundering and Terrorism Financing (RS Official Gazette, No 113/2017 – hereinafter: the Law), the NBS Decision on the Guidelines for Assessing the Risk of Money Laundering and Terrorism Financing (RS Official Gazette, Nos 13/2018 and 103/2018), and the National Money Laundering and Terrorism Financing Risk Assessment carried out in 2018, a new Questionnaire was created for the purposes of adequate updating of this analysis, as well as for the regular supervisory assessment of the ML/TF risk in banks. The updating of the Questionnaire was aimed at further improving the risk-based approach to supervising banks' activities relating to the ML/TF risk management.

Questions in the Questionnaire are sorted into eleven groups:

Part I: General bank data
Part II: Clients
Part III: Client composition by the assessed risk level
Part IV: Client composition by CDD actions and measures
Part V: Transactions and products
Part VI: Outsourcing CDD actions and measures to third parties
Part VII: Correspondent relationship
Part VIII: Employee training
Part IX: Organisational structure
Part X: Reporting to the AML/CFT compliance officer
Part XI: Internal audit and internal control

The key objectives of the analysis of data from the Questionnaire:

- analysing the state-of-play in terms of identifying, measuring and managing ML/TF risk in the entire banking system at annual level for the purposes of timely identification of areas that may indicate increased exposure to the ML/TF risk;

- off-site monitoring of the efficiency and adequacy of the established ML/TF risk management system in the entire banking system and identification of possible deficiencies in the risk management system;
- timely alerting banks to potential exposure to the ML/TF risk.

This analysis was carried out based on data for January–December 2019, submitted by banks to the NBS on a quarterly basis.

In the period covered by the analysis, 26 banks operated in Serbia's banking sector, but relative to end-December 2018, this number decreased by one amid a merger by acquisition of one bank.

CONTENTS:

I Key findings

Based on the analysis of primarily the inherent risk of exposure to the ML/TF risk, i.e. quantitative and qualitative data and information from the Questionnaire, as well as data and information related to the management and control of this risk, the overall conclusion is that banks have medium exposure to the ML/TF risk, as in the previously analysed periods.

Banks are exposed to the ML/TF risk due to the size of the sector and the branched out network, the number and type of clients, as well as the number of performed transactions. Namely, as at 31 December 2019, 26 banks established business relations with clients at a total of 2,498 locations, while cash transactions could be executed at a total of 3,319 locations in Serbia. Compared to the data from the past year, the total number of banks decreased by one, with a simultaneous increase in the number of locations at which a bank could establish business relations with clients, and a decrease in the number of locations at which cash transactions could be executed.

The total number of clients in the banking sector declined relative to the previously analysed year, measuring over 11.9 million at end-2019, of which around 11.14 million were natural persons (82,859 non-residents), 394,606 legal persons (5,542 non-resident legal persons) and 401,822 entrepreneurs. According to the data provided, in the observed period, somewhat fewer than 574 million non-cash and over 165 million cash transactions were executed. Compared to the previously analysed year, an increase was recorded in the number of cash transactions and a decrease in the number of non-cash transactions.

The key findings based on the analysis of the data provided in the Questionnaire, regarding the indicators of the factors of exposure to the inherent ML/TF risk in the observed period are the following:

- Compared to the previously analysed year (as at 31 December 2018), the total number of banks decreased by one, and the total number of clients in the banking sector by 0.5 million;
- The total number of employees in the banking sector rose by 238, while the number of employees directly engaged in client- and transaction-related operations went up by 301;
- In 2019, there were no significant changes in the composition of clients by risk level, residence and CDD actions and measures applied;
- The number of high-risk clients was negligibly above the average for the previously analysed periods. It came at slightly more than 75.5 thousand;
- Compared to the previously analysed year (as at 31 December 2018), the number of executed cash transactions increased by over 3.9 million, and the number of non-cash transactions decreased by almost 82 million;

- At the same time, the number of executed inflows/outflows with high-risk countries decreased, while that number increased for off-shore countries;
- In 2019, ten banks introduced a total of 103 new products into their business offer, i.e. 49 products more relative to 2018;
- Compared to the previously analysed year, the total value of loans secured by a 100% deposit rose considerably, by EUR 53,763,666.83 mn and stood at EUR 123,328,409.70 mn at 31 December 2019;
- All banks declared that they did not establish loro correspondent relationship with a bank or another similar institution with a head office in a foreign country that is on the list of countries with strategic deficiencies in the AML/CFT system;
- In the analysed period, nineteen banks established a total of 195 loro correspondent relationships (an increase of 17 from 31 December 2018).
- Six banks responded positively, stating they closed a total of 20 loro accounts and citing as the main reason a small volume of turnover, i.e. inactivity.

Based on the presented indicators of the factors of exposure to the inherent ML/TF risk, banks, which play the most important role in the financial system, represent the most sensitive part of the financial sector in terms of exposure to the ML/TF risk. However, the observations obtained from the analysis of data and information regarding the measures taken by banks to adequately manage and control the ML/TF risk in the observed period, indicate that this risk was significantly reduced, inter alia, in the following ways:

- All banks set up their own ML/TF risk management systems applying an ML/TF risk assessment approach and taking into account the findings of the National Money Laundering Risk Assessment;
- 25 out of 26 banks use some of the software for tracking transactions and clients to detect suspicious transactions and individuals, while one bank is in the process of final testing, before introducing the software;
- All banks use some of the commercial databases for filtering clients and transactions against embargo lists and the so-called blacklists (OFAC, UN, EU, etc.);
- 23 out of 26 banks have a special organisational unit which deals exclusively with implementing the Law, whereas in three banks these tasks are performed by other organisational units;
- Two banks had a client who is a designated person (a person who tried to establish a business relation or any other person with whom it has or had a business or other similar relationship);
- Fourteen banks declared that in the observed period there were no changes regarding the function of the compliance officer and his deputy, whereas the

remaining twelve banks declared positively (eight banks reported changes regarding the compliance officer);

- All banks stated that they prescribed procedures for internal reporting of violations of the provisions of the law through a special and anonymous communication channel;
- In 21 out of 26 banks, the AML/CFT area is covered by the report of the external auditor;
- In 2019, all banks carried out internal control (the control identified irregularities in 22 banks and set deadlines for their removal, while four banks did not identify irregularities);
- Of the 22 banks which identified irregularities in the course of internal control, 13 banks took and implemented measures to remove such irregularities within the set deadline, while in nine banks the deadline has not yet expired;
- In 2019, nineteen banks performed an AML/CFT-related internal audit. The audit identified deficiencies in 16 banks and set deadlines for their removal, there were no deficiencies in one bank, while two banks have not concluded/sent a report on the internal audit;
- Of the 16 banks which identified irregularities in the course of internal audit, 6 banks took and implemented measures to remove such irregularities within the set deadline, while in ten banks the deadline has not yet expired in the moment this analysis was made;
- Eighteen banks terminated the business relations with 133,456 clients (of which 1 bank with 90,999 clients) because it was impossible to carry out CDD actions and measures, an increase of 68,737 from 31 December 2018;
- Sixteen banks refused the offer to establish a business relation and/or execute a transaction in 15,368 cases, due to the impossibility to take CDD actions and measures, an increase of 10,437 clients from 31 December 2018;
- In the period since the implementation of the Law on the Prevention of Money Laundering and Terrorism Financing (1 April 2018) until 31 December 2019, 27,130 banking sector employees successfully completed the training.
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II General bank data

As at 31 December 2019, there were 26 banks licensed by the NBS in the Republic of Serbia. According to the submitted responses, banks established business relations with clients at 2,498 locations. Six banks can establish business relations at up to 10 locations, six banks at 11–50 locations, six banks at 51–100 locations, five banks at 101–200 locations, and three banks at over 200 locations.

At banking sector level, cash transactions can be made at a total of 3,319 locations. Seven banks have up to 10 such locations, five banks between 11 and 50 locations, nine banks between 51 and 100, two banks between 101 and 200, and three banks over 200 such locations.

Total banking sector employment as at 31 December 2019 was 23,084 persons, while the number of employees directly engaged in client- and transaction-related operations was 13,707 (59.38% of the total number of employees). Based on the analysis, there was an increase in the total employment by 238 relative to 31 December 2018, while the number of employees directly engaged in client- and transaction-related operations went up by 301.

At banking sector level, the average number of clients per employee directly engaged in client- and transaction-related operations was 871. The average number of transactions per employee in the period January–December 2019 fell by 1,501 to 32,039 compared to the same period in 2018. In relation to this, the average number of clients per bank employee fell by 59 relative to end-December 2018. This means that the upward trend of increased employee workload, observed in the previous years, was reversed in the period under review.

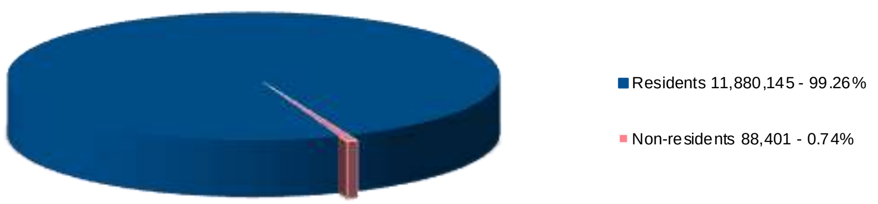
III Clients

As at 31 December 2019, the total number of clients at the banking sector level came at 11,938,546, down by 532,362 clients (4.26%), in absolute amount relative to 31 December 2018.

Based on the data obtained from the Questionnaire, Charts 1–6 show the composition of clients by residence, the legal form of organising resident legal persons, as well as the composition of non-residents in the banking sector by their country risk profile.

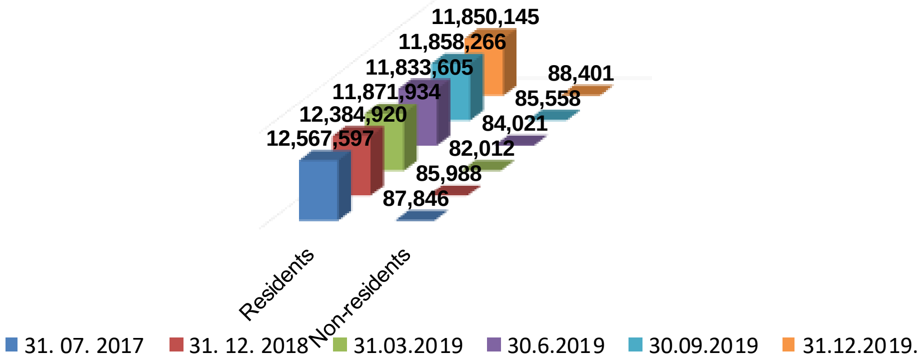
Chart 1 shows the absolute and relative share of resident and non-resident clients in the overall banking sector as at 31 December 2019, whereas Chart 1a shows the composition of the number of clients by residence from 31 July 2017 until the period under review.

Chart 1 **Composition of clients by residence as at 31 December 2019**



Relative to the previously analysed period, there were no changes in the composition of clients by residence in the banking sector.

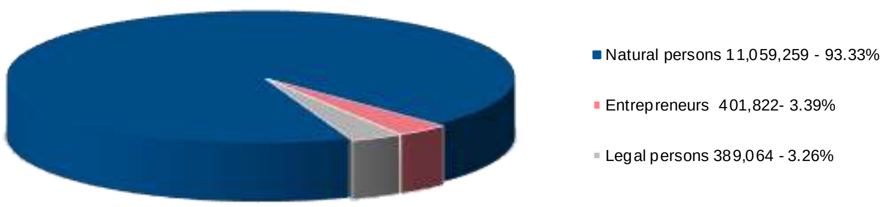
Chart 1a **Composition of clients by residence in analysed periods**



However, a downward trend was observed in the total number of clients.

Of the total number of resident clients, natural persons were dominant (93.33%), while resident legal persons and entrepreneurs accounted for 3.28% and 3.39%, respectively (Chart 2).

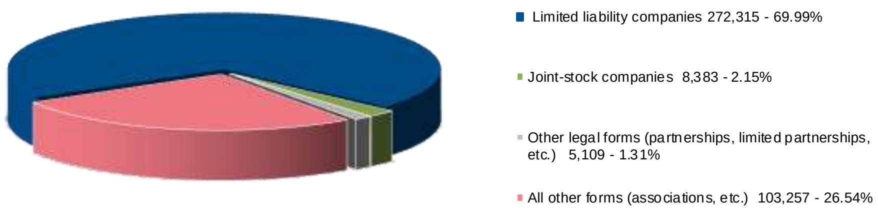
Chart 2 **Composition of resident clients as at 31 December 2019**



Relative to 31 December 2018, the composition of resident clients remained almost unchanged.

Chart 3 shows the composition of resident legal persons by legal form of organising, while Chart 3a shows this composition in different periods from 31 December 2018 until 31 December 2019.

Chart 3 **Composition of resident legal persons by legal form of organisation as at 31 December 2019**



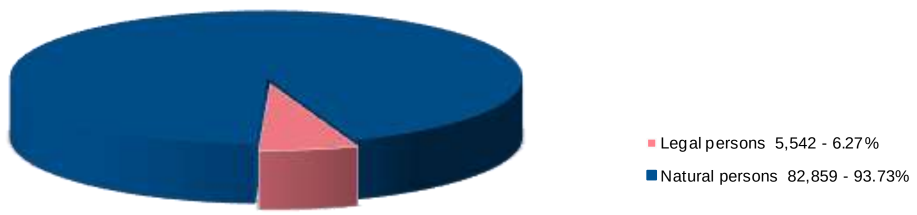
It should be noted that in the total number of resident legal persons, the dominant share belongs to limited liability companies (DOO), with the National Risk Assessment estimating this legal form to be at an elevated ML/TF risk, while the share of legal persons that are organised as joint-stock companies (AD) amounts to 2.15%.

The share of legal persons organised in other legal forms (limited partnership, partnership company) was only 1.31%, and all other forms (associations, foundations, sport associations, etc.) accounted for the remaining 26.54% or 103,257 clients.

Relative to 31 December 2018, the number of clients organised as limited liability companies declined by 11,855 and joint-stock companies by 2,512, but the number of legal persons organised as associations rose by 20,658. However, in 2019 the total number of legal persons regardless of their form of organising increased by 4,786.

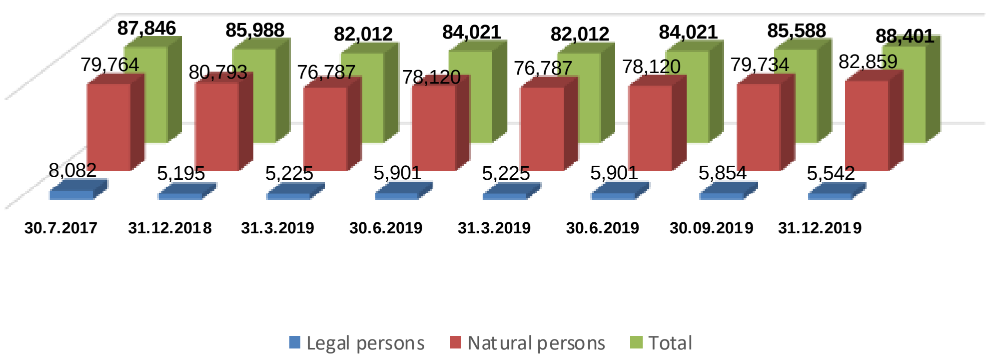
Chart 4 shows the composition of non-resident banking sector clients as at 31 December 2019, while Chart 4a shows an overview of these clients in different periods from 30 July 2017 until 31 December 2019.

Chart 4 **Composition of non-resident clients as at 31 December 2019**



The total number of non-resident clients as at 31 December 2019 was 88,401. Compared to the previously analysed period (as at 31 December 2018), the total number of these clients increased by 2,413. The number of non-resident natural persons edged up by 2,066 with the 93.73% share, and the number of non-resident legal persons by 347.

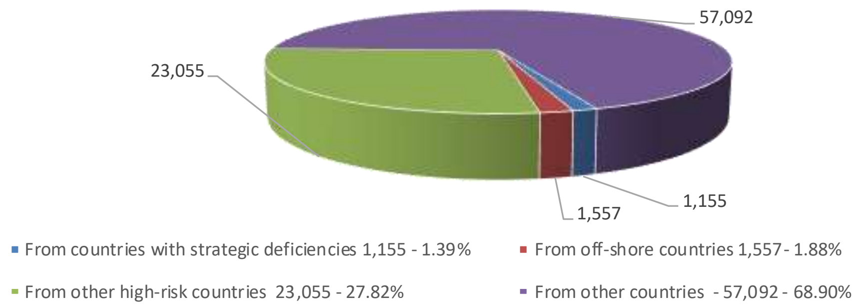
Chart 4a **Composition of non-resident clients in analysed periods**



Based on these data, it can be concluded that at the end of this period the total number of non-resident clients (natural and legal persons) was above the average for the previously analysed periods, shown in Chart 4a. It came at slightly more than 85 thousand or 79.9 thousand for non-resident natural persons. As for non-resident legal persons, their number is somewhat lower than the average for the periods shown in Chart 4a. It came at slightly more than 6.4 thousand.

Charts 5 and 6 show the composition of non-resident natural and legal persons by the country risk profile, client's permanent and temporary residence, i.e. of the beneficial owner of the client.

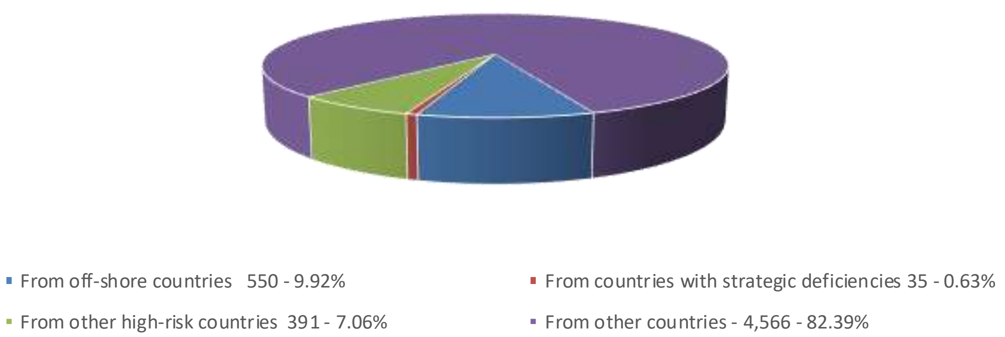
Chart 5 **Composition of non-resident natural persons by country's risk profile as at 31 December 2019**



The share of natural persons from high-risk countries in the total number of non-resident natural persons was 27.82%, while 1.39% of them were from countries with strategic deficiencies in the AML/CFT system. In addition, 1.88% of the share relates to non-resident natural persons from off-shore countries, while natural persons from other countries which do not have a high or elevated ML/TF risk hold a dominant share.

It is important to note that, relative to 31 December 2018, the share of non-resident natural persons from countries with strategic deficiencies in the AML/CFT system decreased, while those from off-shore countries recorded a mild increase.

Chart 6 **Composition of non-resident legal persons by country's risk profile as at 31 December 2019**

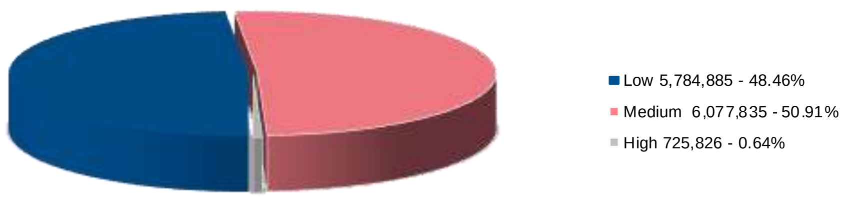


As with non-resident natural persons, the dominant share in the composition of non-resident legal persons belongs to legal persons from other countries which do not have an elevated ML/TF risk (82.39%), followed by off-shore countries (9.92%), high-risk countries (7.06%) and countries with strategic deficiencies in the AML/CFT system (0.63%). It is important to note that, relative to 31 December 2018, the share of non-resident legal persons from high-risk and off-shore countries declined.

IV Client composition by the assessed risk level

In accordance with the Law and the NBS Decision on the Guidelines for Assessing the Risk of Money Laundering and Terrorism Financing, all banks have an obligation to prepare the risk analysis for each group or type of client, and/or business relation, and/or services offered by the obligor within their activities and/or transactions, taking into account the results of the National Money Laundering Risk Assessment.

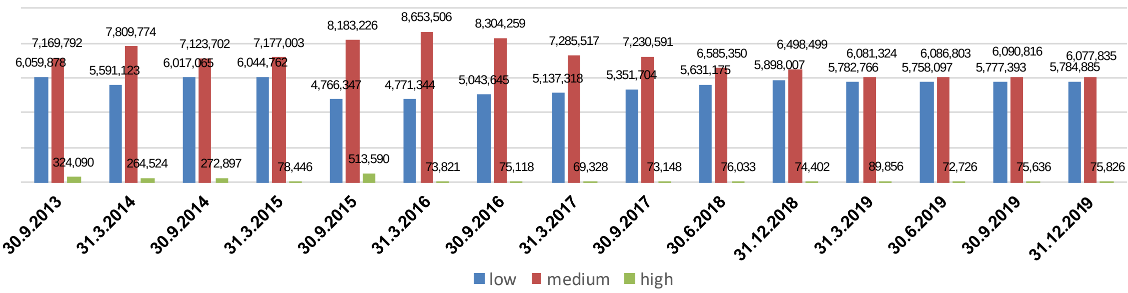
Chart 7 **Composition of clients by the assessed risk level as at 31 December 2019**



Depending on the results of the analysis, banks classified their clients into the following risk categories: low-, medium- and high-risk (Chart 7).According to the submitted data on client classification by degree of exposure to ML/TF risk, 11 banks classified over 80% of their clients in the low-risk category, while 11 classified the majority of their clients (over 80%) in the medium-risk category. Of the remaining four banks, three banks classified between 50% and 80% of their clients in the medium-risk category, while one bank, specific due to a small number of clients, classified over 59% of its clients in the high-risk category.

Chart 7a shows client composition by risk level as at a specific date, while Chart 7b shows the number of banking sector high-risk clients in different periods.

Chart 7a **Client composition by the assessed risk level in analysed periods**



Relative to the previously analysed year (2018), there were no significant changes in the composition of banking sector clients by risk level.

Chart 7b **Composition of high-risk clients in analysed periods**
(number of clients)

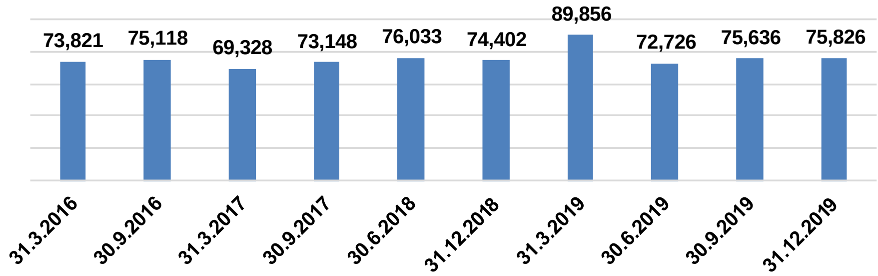
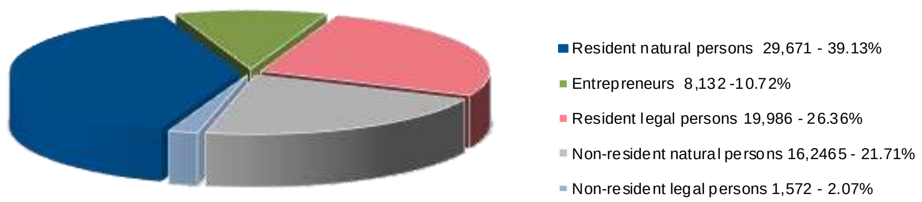


Chart 7b reveals that the number of high-risk clients in the analysed period was slightly above the average for the periods observed, which came at slightly more than 75.5 thousand.

Chart 8 shows the composition of clients classified in the high-risk category.

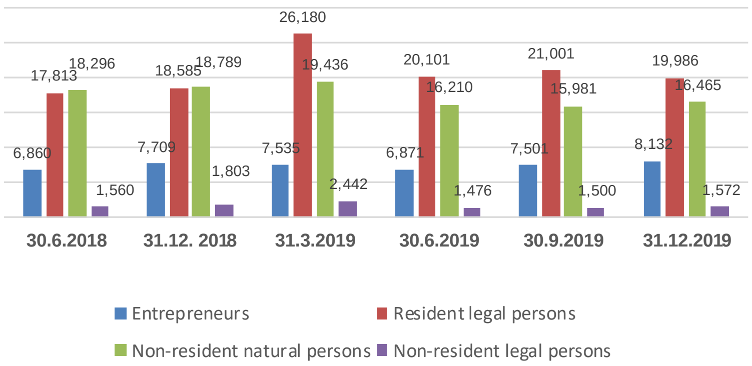
Chart 8 **Composition of high-risk clients as at 31 December 2019**



Resident natural persons have the largest share (39.13%), followed by resident legal persons (26.36%), non-resident natural persons (21.71%), entrepreneurs (10.75%) and finally non-resident legal persons with the smallest share (2.07%).

Chart 8a gives an overview of high-risk clients as at a specific date.

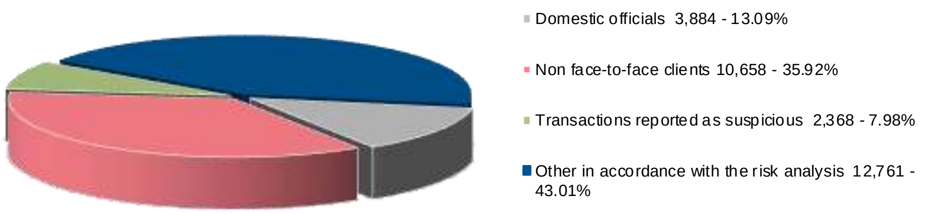
Chart 8a **Composition of high-risk clients in analysed periods**



As in the previously analysed periods, the dominant share belongs to resident natural persons, and the smallest to non-resident legal persons, in proportion to their total number. The fourth place belongs to entrepreneurs, while resident legal persons and non-resident natural persons share the second and the third place in the analysed periods, as shown in Chart 8a.

Charts 9, 10 and 11 show the composition of resident natural persons, legal persons and entrepreneurs by the basis for classification into high ML/TF risk category.

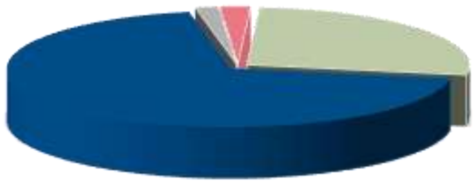
Chart 9 **Composition of high-risk resident natural persons as at 31 December 2019**



In accordance with the risk analysis, banks classified 43.01% of resident natural persons in the high-risk category, with 35.92% of these clients thus classified because they were not present when establishing business relationship. The share of clients classified as high-risk because they executed transactions reported as suspicious to the Administration for the Prevention of Money Laundering (hereinafter: the Administration) was 7.98%. In the composition of the high-risk resident natural persons, banks determined that 3,884 clients had the status of officials (13.09%).

Relative to 31 December 2018, there was a decrease in the share of resident natural persons classified as high-risk in accordance with the risk analysis, and an increase in the share of clients not present when establishing business relations, those who executed transactions reported as suspicious to the Administration and those who had the status of officials.

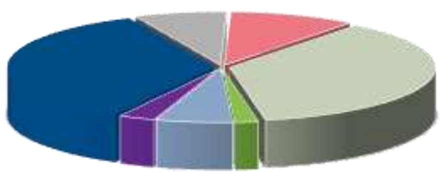
Chart 10 **Composition of high-risk entrepreneurs as at 31 December 2019**



Banks classified 5,631 entrepreneurs (69.24%) in the high-risk category for ML/TF, because they performed some of the high-risk activities, 2.21% because they executed transactions reported as suspicious to the Administration, 1.68% because they had the status of officials, while the remaining 26.86% were classified as high-risk in accordance with the risk assessment.

Relative to end-2018, there was a decrease in the share of entrepreneurs classified as high-risk in accordance with the risk analysis, and an increase in the share of those who perform some of the high-risk activities, those who executed transactions reported as suspicious to the Administration and those who had the status of officials.

Chart 11 **Composition of high-risk resident legal persons as at 31 December 2019**

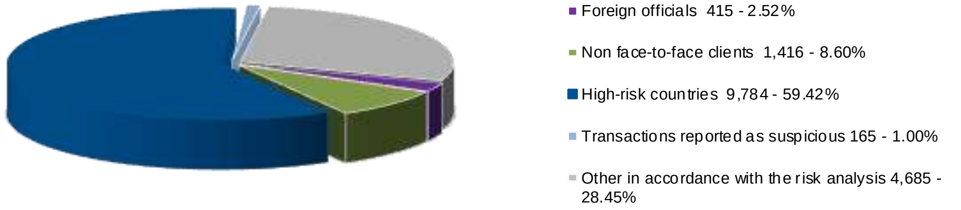


In the analysed period, banks classified 7,063 resident legal persons as high-risk because they performed some of the high-risk activities, 1,988 clients because of the risk assessment of the country of its founder/beneficial owner, 1,196 clients because they had an off-shore legal person in the ownership structure, 1,450 clients because their transactions were reported as suspicious to the Administration, 571 clients because they had an official in the ownership/governance structure, 368 clients owing to a complex ownership structure, and the remaining 7,350 were classified as high-risk in accordance with the banks' analysis.

Compared to to the previously analysed year, there was a rise in the number of legal persons with an official in their ownership/governance structure (by 132 cases), those whose transactions were reported as suspicious to the Administration (by 783) and those with an off-shore legal person in the ownership structure (by 148). The downward trend was also observed in the number of legal persons with a complex ownership structure and those who performed some of the high-risk activities.

Charts 12 and 13 show the composition of non-resident natural and legal persons by the basis for classification into high ML/TF risk category.

Chart 12 **Composition of high-risk non-resident natural persons as at 31 December 2019**

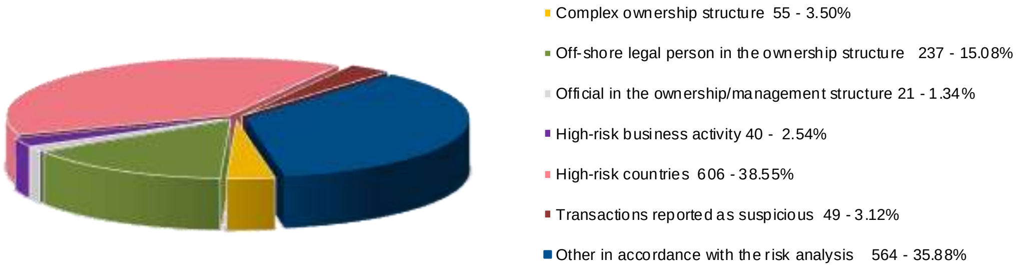


The bulk of non-resident natural persons (59.42%) were classified as high-risk, because they were from the countries for which banks assessed high ML/TF risk, 8.60% because they were not present when establishing business relationship, while the remaining 28.45% were classified as high-risk in accordance with the banks' analysis.

In addition to the above, 1% of non-resident natural persons were classified as high-risk because they executed transactions which were reported as suspicious to the Administration. Banks determined that 415 of the high-risk non-resident natural person clients had the status of officials.

Compared to the previously analysed year, the number of non-resident natural persons who had the status of officials increased by 19, and the number of clients who were not present when establishing business relationship by 575.

Chart 13 **Composition of high-risk non-resident legal persons as at 31 December 2019**



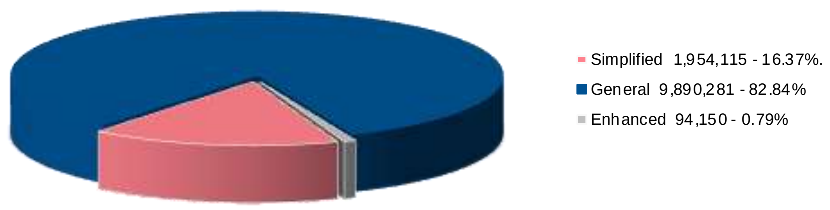
In the composition of high-risk non-resident legal persons, legal persons from countries for which banks assessed high ML/TF risk had the largest share of 38.55%, followed by off-shore legal persons with 18.08%, as well as 35.88% of those classified by the banks as high-risk in accordance with the performed analysis. Banks assessed only 3.5% of non-resident legal persons as high-risk due to the complex ownership structure, 1.34% because they had an official in the ownership/governance structure, 2.54% because they performed high-risk activities and 3.12% due to the reporting of suspicious transactions to the Administration.

Compared to the previously analysed period, the number of non-resident legal persons who had the status of officials edged down by 26, and the number of clients who performed transactions reported as suspicious to the Administration by 39.

V Client composition by CDD actions and measures

Pursuant to the Law, banks are required to apply general, simplified or enhanced CDD actions and measures. In the analysed period, general actions and measures were taken in respect of 82.84% of clients at banking sector level. Enhanced actions and measures were taken in respect of 0.79%, and simplified in respect of 16.37% clients, as shown in Chart 14.

Chart 14 **Composition of clients by CDD actions and measures applied as at 31 December 2019**



The table below shows a comparative overview of the number of clients by risk level and CDD actions and measures as at 31 December 2019:

Table 1 **Structure of banking sector clients by risk level and CDD actions and measures applied**

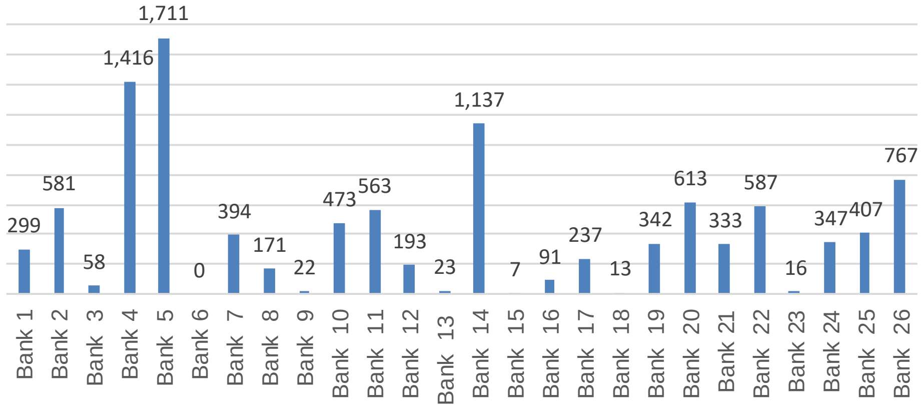
Risk level	No of clients	Share in %	Applied measures	No of clients	Share in %
Low	5,784,885	48.46	Simplified	1,954,115	16.37
Medium	6,077,835	50.91	General	9,890,281	82.84
High	75,826	0.63	Enhanced	94,150	0.79
	11,938,546	**100**		**11,938,546**	**100**

Based on the analysis of the data from the Questionnaire, it can be concluded that banks do not apply simplified actions and measures to all low-risk clients and that over 66% of such clients are subject at least to general CDD actions and measures. Enhanced actions and measures are applied to all clients classified as high-risk, but also to 18,324 clients classified as medium- or low-risk.

In the question from the Questionnaire about the number of cases in which the business relationship was discontinued due to the inability to apply CDD actions and measures, 18 banks responded that business relations with 133,440 clients were terminated (of which 90,999 clients pertained to one bank only). In the observed period, 16 banks refused the offer to establish a business relationship and/or execute transactions in 15,348 cases, due to the impossibility to take CDD actions and measures. Of this number of cases, 14,892 pertained to one bank only.

Chart 15 gives an overview of the number of clients on which in the last three years banks submitted data to the Administration at its request.

Chart 15 **Number of clients on which in the last three years banks submitted data to the Administration at its request**



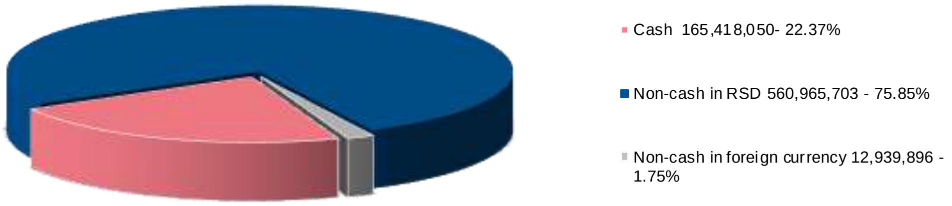
The analysis has shown that most of the clients for which data were submitted to the Administration were the clients of banks occupying leading positions by the number of clients in the banking sector.

VI Transactions and products

Banks executed 739,323,649 transactions in 2019.

Chart 16 shows the structure of cash and non-cash (dinar and foreign currency) transactions in the banking sector in the period January–December 2019.

Chart 16 **Composition of cash and non-cash transactions (executed in RSD and foreign currencies) in the banking sector in 2019**



According to the submitted data, the largest share in the total number of transactions executed in the entire banking sector belongs to non-cash transactions in dinars – almost 76%, followed by cash transactions with the share of 22.37%, and non-cash foreign transactions with the share of 1.75%.

In the same period, banks executed a total of 4,853,913 non-cash and cash transactions amounting to EUR 15,000 or more in the dinar equivalent at the NBS middle exchange rate, with non-cash transactions in dinars also accounting for the largest share – over 58%.

Chart 17 **Composition of cash and non-cash transactions ammounting to EUR 15,000 euro or more in the dinar equivalent in 2019**

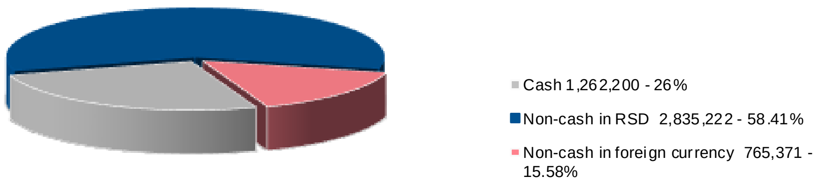
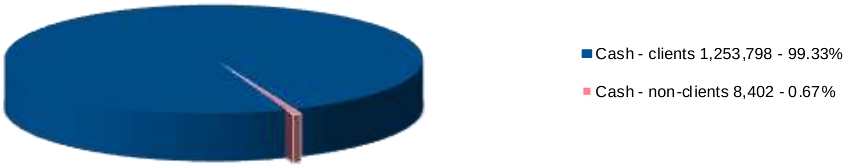


Chart 18 shows an overview of the number of cash transactions worth EUR 15,000 or more in the dinar equivalent at the NBS middle exchange rate, from the aspect of whether they were performed by the clients in the bank with which they have established a business relationship or not (so-called non-clients).

Chart 18 **Composition of executed cash transactions ammounting to EUR 15,000 or more – clients and non-clients in 2019**



Of the total of 1,262,200 executed cash transactions worth EUR 15,000 or more in the dinar equivalent at the NBS middle exchange rate, only 8,402 transactions with a share of 0.67% were executed by persons who were not clients of the bank in which these transactions were made.

Below is an overview of the number of inflow transactions from high-risk countries and off-shore geographical areas executed in 2019. In the analysed period, 184,442 payments were made to high-risk countries, as well as 38,036 payments to off-shore geographical areas, i.e. countries.

Chart 19 **Overview of the number of executed inflows/outflows with high-risk and off-shore countries in 2019**

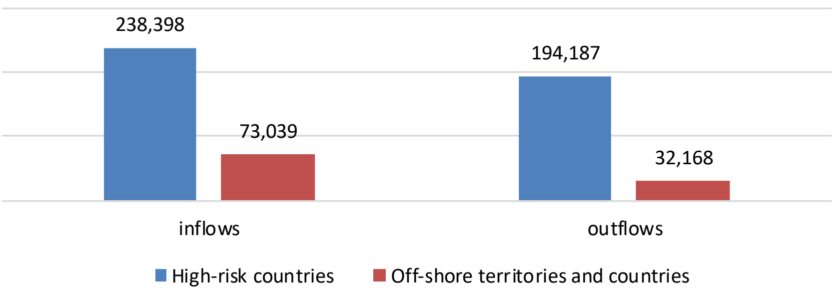
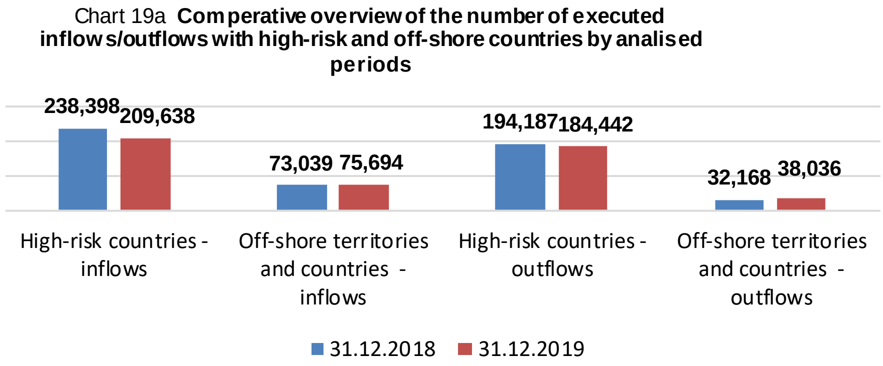


Chart 19a shows a comparative overview of the number of executed inflow and outflow transactions with high-risk countries and by analysed periods.



Relative to 31 December 2018, in the analysed period, the number of executed inflow and outflow transactions with high-risk countries decreased, while increasing for off-shore countries.

In the course of 2019, ten banks introduced a total of 103 new products into their business offer. According to the submitted data, nine banks stated that they did not have products that were assessed as high- and/or medium-high ML/TF risk.

In the analysed period, 13 banks identified a high ML/TF risk for 1–10 products; 3 banks did the same for 11–30 of their products, and one bank for more than 30 products.

Eleven banks reported no products from their business offer were assessed as medium-high risk, twelve banks assessed 1–10 products at this level of risk; one bank declared that it had 29 medium-risk products, while the remaining two banks had more than 30 products of medium-high ML/TF risk.

As regards e-banking, seven banks assessed this product as high-risk, and thirteen banks assessed it as medium-high ML/TF risk. Six banks assessed m-banking as a high-risk product, and eleven banks assessed it as medium-high ML/TF risk. E-banking is used by 2,401,483 clients, m-banking by 1,805,565, and private banking by only 685 clients. According to the data provided, in 2019, 21 out of 26 banks approved 4,616 loans worth EUR 123,328,409.70 against 100% deposit backing.

VII Outsourcing CDD actions and measures to third parties

In the entire banking sector, only six banks used the possibility to outsource some of the CDD actions and measures to third parties in the analysed period, in accordance with the Law, and thus obtained data and documentation for 553,049 clients (449,099 of these clients pertaining to one bank only). Relative to 31 December 2018, the number of clients, for which data and documentation were obtained by third parties in accordance with the Law, increased by 20,740.

VIII Correspondent relationship

In the analysed period, seven banks declared that they did not establish correspondent relationships with banks and similar institutions with a head office in a foreign country, while the remaining twelve banks established a total of 195 loro correspondent relations. All 26 banks declared that they did not establish loro correspondent relationship with a bank or another similar institution with a head office in a foreign country that is on the list of countries with strategic deficiencies in the AML/CFT system.

Asked whether there were cases of closing loro accounts in the period for which this analysis was carried out, six banks responded positively, stating they closed a total of 20 loro accounts and citing as the reason a small volume of turnover, i.e. inactivity. Banks have nostro correspondent relations with 231 banks, while three banks declared that they have established nostro correspondent relations with five banks with a head office in a foreign country that is on the list of countries with strategic deficiencies in the AML/CFT system.

IX Employee training

In the banking sector, front-office jobs are carried out a total of 13,707 employees. This is 301 persons more from 31 December 2018, while the relative share of front-office staff in total banking sector employment is 59.30% (58.68% in the previously analysed year).

Training is most often carried out by compliance officers and their deputies, trained managers of organisational units and Compliance Division staff. A total of 17 banks stated that training for front-office staff is organised once a year, six banks organise these trainings twice a year, while three banks do so three or more times a year.

According to the data provided, in two banks training is carried out in direct contact with employees (in training centres, interactive trainings, workshops using PowerPoint presentations), one bank carries out training without direct contact with employees, by electronic means (so-called E-learning), while most banks (23) carry out training in both ways.

Banks stated that in the period since the implementation of the Law on the Prevention of Money Laundering and Terrorism Financing (1 April 2018) until 31 December 2019, 27,130 employees successfully completed the training.

All banks stated they introduced their employees with the consequences of non-compliance with laws, procedures and findings of the ML/TF risk management control.

X Organisational structure

As Questionnaire responses reveal, 23 banks have a special organisational unit which deals exclusively with implementing the Law, whereas in three banks these tasks are performed by other organisational units. In 23 banks in separate organisational units, a total of 105 employees have been assigned to AML/CFT-related tasks, including a compliance officer and his deputy.

In 2019, twelve banks reported changes regarding the compliance officer and/or his deputy. Four banks reported changes of employees acting as compliance officer deputies, while eight banks reported such changes regarding the compliance officer function, citing as the reason the termination of employment of the person who previously held that position, replacement of positions of the compliance officer and his deputy, and taking maternity leave. All banks declared that they had reported such changes to the Administration, in accordance with the Law.

When asked if the compliance officer and his deputy who engage in AML-related activities in accordance with the Law, perform other tasks too, 24 banks gave a negative response, while two banks declared that the compliance officer and his deputy perform other tasks as well.

In six of the 26 banks (23.08 %), the AML staff or front-office staff churn rate was between 10% and 50%, while in all other banks it was below 10%.

According to the data provided, 25 out of 26 banks stated that they have special software for identifying suspicious transactions and persons, which also recognises transactions in the amount of EUR 15,000 or more in the dinar equivalent, while one bank said it was in the process of introducing such software. Twenty-two banks use external software (Smaragd, Norcom, Asseco SEE, Aseba AML Tool, etc.), while three banks have developed AML software in-house. In 25 banks, the aforementioned software recognises several interconnected cash transactions of the same client, whose total value is equal to or higher than EUR 15,000, and classifies clients according to the level of the ML/TF risk.

Asked whether the software allows filtering of clients and transactions by embargo and so-called blacklists (the UN Security Council list, the EU lists and the OFAC lists, etc.), including the list of designated persons of the Serbian Government, all 26 banks responded positively.

Banks also listed the indicators included in the software which they selected from the List of indicators for recognising suspicious transactions or persons and the List of indicators relating to terrorism financing published on the Administration's website.

The table below shows how many indicators for recognising suspicious transactions relating to money laundering published on the Administration's website were included in the software solutions of 25 banks:

Table 2 **Number of included indicators relating to money laundering**

Number of included indicators for banks	Number of banks
Fewer than 10	3
10–19	14
20–29	7
30–37	1

According to Questionnaire responses, indicators for recognising FT-related suspicious transactions are included in the software of 25 banks, as follows:

Table 3 **Number of included indicators relating to terrorism financing**

Number of included FT-related indicators	Number of banks
Fewer than 5	18
5–10	5
More than 10	2

Also, 22 banks stated 399 other scenarios, which they included in their software for the recognition of suspicious transactions and/or persons.

The table below shows the number of banks adding their own scenarios to the software:

Table 4 **Number of own scenarios included**

Number of scenarios included developed by banks	Number of banks
Fewer than 5	6
5–9	3
10–19	8
20 to 30	5
More than 40	3

Further improvement of IT solutions within existing systems can have an important impact on the level of operating risks that might arise through human error, and can enable a more efficient human resource management (especially in conditions of reduced staff numbers), by enabling employees to dedicate more attention to improving the quality of analysis of the clients' business, i.e. transactions which the banking system singles out based on the programmed parameters – indicators and scenarios.

XI Reporting to the AML/CFT compliance officer and to the Administration

The front-office staff submitted to the compliance officer 715 internal reports on suspected ML risk in relation to a client or a transaction, and only one report on suspected TF risk. However, the number of internal reports that bank staff sent to the compliance officer and based on which data were not submitted to the Administration, amounted to 402, meaning that only 4.8% of the total number of internal reports was reported to the Administration.

According to the data provided, in 2019 banks reported to the Administration a total of 206,228 cash transactions worth EUR 15,000 or more in the dinar equivalent, of which 110,870 were executed in dinars and 102,538 in a foreign currency. Also, banks declared that they reported a total of 1,077 of suspicious transactions to the Administration, of which over 68% (737 transactions) related to suspicious transactions in dinars, and somewhat less than 32% to suspicious transactions in a foreign currency.

In the analysed period, there was one internal report in which the suspicion related to terrorism financing. However, based on the opinion and decision of the compliance officer, this report was not submitted to the Administration as suspicious.

XII Internal audit and internal control

According to Questionnaire responses, all banks regulated the internal controls system in their internal acts.

In the majority of banks, internal control of the implementation of the Law is within the remit of the organisational unit in charge of internal audit, and at the same time within the remit of other organisational units such as the compliance unit, unit in charge of supervising "network" operations or the unit in charge of AML/CFT activities only.

According to Questionnaire responses, since the start of the year until end-December 2019, nineteen banks performed an internal AML/CFT-related audit. The remaining seven banks carried out an internal audit of that part of their operations in 2018.

All banks which identified omissions in the course of internal audit in 2019 (16) set deadlines for their removal, of which six banks removed such omissions within the set deadline, while in ten banks the deadline has not yet expired (the bank which carried out one such internal audit in Q4 2019).

As for the remaining three banks, one bank did not identify any omissions, while in other two banks, which carried out the internal audit in December 2019, the reports were not available in the moment this analysis was made.

The most commonly identified deficiencies include: incorrect client classification of legal persons with whom business relation was established in 2019, who perform high-risk activities in accordance with banks' risk analysis, and who were not assessed as high ML/TF risk; incompletely or incorrectly entered data on clients in the bank system; failure to re-assess the ML risk within the defined deadlines; inadequate description of competencies for performing certain actions and measures and reporting in the bank's procedures regulating AML/CFT-related area; the need to update the List of High-Risk Countries; identification of indicators for specific persons and their transactions for which there is a reasonable doubt of ML or TF, and for which no official notes were made and/or reports submitted to the Administration; deficiencies or inconsistencies of internal acts from different business processes (related to the procedure of establishing the political exposure status of the client and the beneficial owner, internal acts do not precisely define the dynamics of control over the completeness of data on the payer and payee); failure to identify the beneficial owner of the legal persons client (missing photocopies of IDs of beneficial owners – natural persons), missing some of the elements on ID documents of clients: date and time of identification, full name of the bank's employee who performed the identification, undefined status of persons changing the compliance officer and his deputy and insufficiently precise job description of the compliance officer and his deputy, lack of software for automatic verification of suspicious transactions in domestic payment transactions, no double control in the procedure of reporting transactions to the Administration, i.e. the four eyes principle has not been established, insufficient harmonisation of the bank's internal acts with the parent bank's acts, the need to improve training and the process of implementing AML/CFT activities, omissions in obtaining AML unit approval to establish business relations with high-risk clients and non-residents, etc.

When asked whether the External Auditor's Report included the ML/TF area, 21 banks gave the affirmative answer.

In 24 banks, a compliance officer/compliance officer deputy participates in the implementation of internal control and reports on the results of the control to the bank's management in the form of periodic reports (monthly, quarterly, semi-annual or annual).

In the analysed period, all banks performed AML/CFT-related internal control (two banks in H1 2019, four banks in Q3 2019, and the remaining 20 banks in Q4 2019). Four of these banks did not identify any irregularities.

Most frequently, internal control findings related to the following:

- incomplete client documentation,

- inadequate or incomplete documentation at the time of client identification for the purpose of establishing a business relationship or performing a transaction,

- inadequate documentation in the procedure of identifying the beneficial owner,

- internal forms with client data filled out inadequately,

- high-risk client files lack the statement on the origin of assets that are/will be the subject of a business relation,

- client files are not scanned into the electronic document management system,

- photocopies of client ID documents do not contain some of the identification elements: date, time of identification and/or full name of the bank employee who performed the identification,

- incorrectly determined status of an official for clients who are not officials,

- no periodic risk assessment (re-assessment) has been performed,

- omissions in obtaining statements for clients who are officials and printed searches of officials from the website of the Anti-Corruption Agency,

- outdated client records in the bank's system,

- incorrect client classification by degree of ML/TF risk exposure,

- deficiencies related to updating the documentation, errors in entering client data into the database in the bank's system, errors in marking client risks,

- official notes are not made or are not of appropriate scope and quality, and

- conduct that is not in accordance with the procedures for collecting the necessary documentation/data for clients of all risk levels as well as for clients with the status of officials.

All banks which detected irregularities in the course of internal controls in 2019 (22) set a deadline for the removal of such irregularities, 13 of which took and implemented measures to remove them, while in nine banks the deadline has not yet expired.

In the analysed period, eleven banks stated they are conducting a total of thirty disciplinary procedures due to problems with employee integrity (participation in fraud, theft, corruption, etc.), while six banks stated that 26 proceedings are conducted against the bank or employees in respect of ML/TF. Relative to 31 December 2018, the number of disciplinary procedures due to problems with employee integrity increased by 21 cases, and the number of proceedings against a bank or employees in respect of ML/TF increased by 23 cases.

* * *

Finally, it should be noted that the analysis of the data submitted in the Questionnaire for January–December 2019 revealed that a certain number of banks did not provide some data in the required format, i.e. the value of some data was not expressed in the currency required, before submitting those data to the NBS, and that they did not keep records for some of the required data. Therefore, it is necessary that banks provide such records and pay due attention when completing the Questionnaire in the future.