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e-KYC: Opening the Door to Digital Financial Services

Financial institutions in Malaysia are legally required to conduct customer due diligence, which is a process to identify and authenticate a customer's identity, prior to on-boarding new customers. Traditionally, customer due diligence is required to be done face-to-face. e-KYC, as the name suggests, relies on digital technologies to perform the same task, without the need to have face-to-face interaction. It is undeniable that e-KYC carries a higher risk as the lack of physical presence in the identification and authentication process allows customers to impersonate another person or provide false data.

On 16 December 2019, Bank Negara Malaysia (**BNM**) issued an Exposure Draft on Electronic Know-Your-Customer (**Exposure Draft**), which sets out the proposed requirements and guidance in implementing e-KYC for the on-boarding of individuals in the financial sector. The requirements apply to financial institutions defined in the Exposure Draft (**Financial Institutions**).

One of the requirements worth highlighting is the need to adopt an appropriate combination of authentication factors to verify the identity of a customer being on-boarded. These authentication factors may be something that the customer possesses (e.g. identity card, registered mobile number), something the customer knows (e.g. PIN) or something that the customer is (e.g. biometric characteristics). Whichever combination and strength of authentication factors that Financial Institutions adopt should ultimately be commensurate with the risks associated with inaccurate identification of a particular financial product or service.

Besides that, where identification and verification process are automated with the use of predictive algorithms such as artificial intelligence, Financial Institutions must aim to ensure the overall False Acceptance Rate (**FAR**) of the e-KYC solution does not exceed 5%. FAR is a measurement of the capability of an e-KYC solution to identify non-genuine on-boarding cases. A lower FAR would indicate that the e-KYC solution has correctly identified non-genuine or fraudulent on-boarding cases on a regular basis. Note that there is a requirement to notify BNM where the FAR exceeds 5% for three consecutive months.

Other requirements include:

- (i) obtaining the board's approval prior to implementing e-KYC for each type of financial product or service;
- (ii) implementing additional safeguards as highlighted in the Exposure Draft for high-risk financial products or services and where circumstances specified in the Exposure Draft warrant; and
- (iii) maintaining a record of the performance of the e-KYC solution that uses predictive algorithms, and submitting the said record to BNM.

This Exposure Draft is meant to specify additional requirements and guidelines that must be observed when e-KYC is deployed, as the existing legal requirements relating to customer on-boarding via electronic means are not extensive. Financial Institutions that wish to implement e-KYC are encouraged to take proactive steps to comply with the necessary requirements in the Exposure Draft.

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