



Consultation on the revised AML/CFT Guidance Notes

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Aims of the presentation

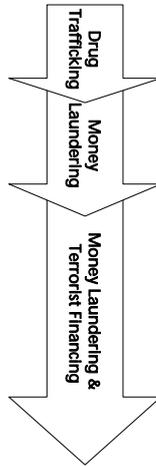
- To highlight the structure and format of the revised Notes
- To introduce the main concepts of the revised AML/CFT Notes
 - Threat Matrix
 - Statements of Principles
 - Risk Based Approach
 - Minimum Customer Identification Documentation (Customer Due Diligence) – New or revised requirements
 - Senior Management Responsibilities & the MLRO
- The consultation process
- **NOT – an open discussion forum, this is for the consultation feedback process**

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A brief History of AML/CFT Measures



- 1986 – DTOO
- 1990 – FATF 40 Recommendations Published
- 1995 – DTOO Revised and CJO introduced
- 1996 – AMLGNs 1st published (followed almost exactly the UK notes)
FATF Recommendations revised
- 2000 – KYC Processes localised
- 2001 – Pre 1st April 1995 Retrospective KYC introduced
Terrorism Orders Published
FATF Special recommendations on Terrorist Financing
- 2003 - FATF Recommendations substantially revised
- 2004 – Risk based processes make an appearance
2MLD introduced
Controlled Activities Caught by legislation
- 2005 - Terrorism Ordinance published
- 2006 - 3MLD

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The drivers for change

- A tick-box approach to AML risks adopted by many industry participants at present
- Inability to handle the exception
- Poor understanding by a minority of industry participants on the actual requirements of the AMLGNs
- Revised FATF 40+9 Recommendations
- 3rd Money Laundering Directive Implementation

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Format of Notes

- Introductions – Chapters I and II
- Context – Chapter III
- Statements of Principle – Chapter IV
- Detail of compliance with each
Statements of Principle – Chapters V to X

Rx Requirements of the notes

! Expectations

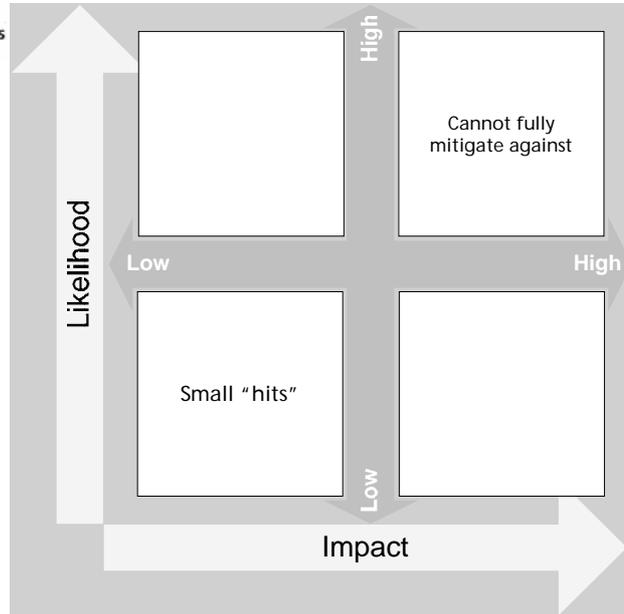
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The new approach

- Statements of Principle
 - The Notes outline the basis for compliance with the Statements of Principle
- Risk based is the default
 - Firms need to take a view of how to comply with the requirements
 - Prescriptive approach is only taken in given scenarios
 - Firms need to document their thought processes
 - Senior management is accountable for the translation of the requirements into practice
 - Firms need not adopt the risk framework outlined in the notes if their existing systems already capture and mitigate the risks
 - A firm's practice must match the methodology adopted

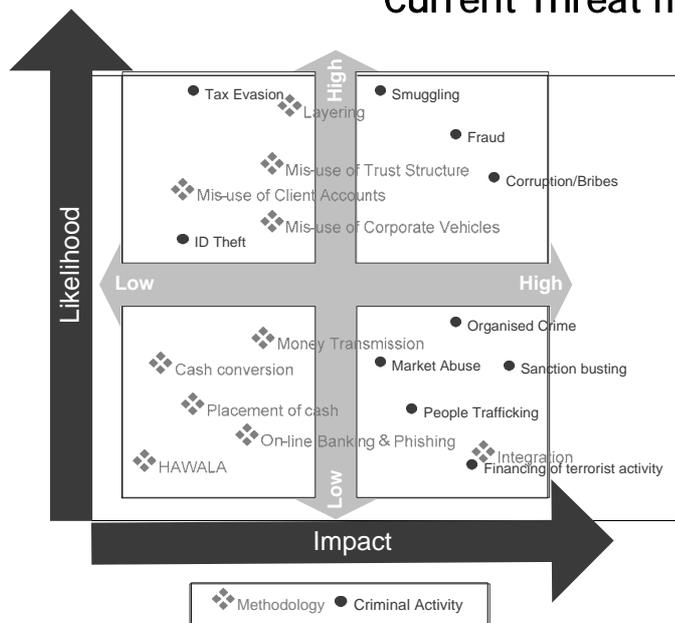
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Threat matrix – How it works



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Current Threat matrix



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Statements of Principle

- SP1 The senior management of a firm is responsible for ensuring that the systems of control operated in the firm appropriately address the requirements of both the legislation and these guidance Notes.
- SP2 Firms must adopt a risk-based approach to these statements of principles and their requirements.
- SP3 All firms must know their customer to such an extent as is appropriate for the risk profile of that customer.
- SP4 Effective measures must be in place that requires firms to have both internal and external reporting requirements whenever money laundering or terrorist financing is known or suspected.
- SP5 The firm will establish and maintain effective training regimes for all of its officers and employees.
- SP6 Firms must be able to provide documentary evidence of their compliance with the legislation and these Notes.

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Making Senior Management Accountable

- R2 Senior management of firms must ensure that the following processes have been adopted;
 - a. The **allocation to a director or senior manager** overall responsibility for the establishment and maintenance of effective AML and CFT systems of control **AND** the appointment of a person as MLRO
 - b. That **appropriate training** on money laundering is identified, designed, delivered and maintained
 - c. That regular and timely **information is made available to senior management** relevant to the management of the firm's money laundering and terrorist financing risks
 - d. That the firm's risk management policies and methodology are **appropriately documented**
 - e. That appropriate measures to ensure that **money laundering risk is taken into account** in the day-to-day operation of the firm.
 - f. Senior management of the firm must ensure that the **MLRO has sufficient resources** available to him.

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Enhanced role for the MLRO

- R3 Responsible for the oversight of the firm's anti-money laundering activities
- R4 Senior to be free to act on their own authority
- R5 The MLRO will act as the "appropriate person" to receive and process internal and external suspicious transaction reports.
- R6 Central point of contact with the law enforcement
- R7 It is not appropriate for the MLRO to be located outside Gibraltar.
- R8 Reasonable access to information that will enable him to undertake his responsibility. Should keep a written record of every matter reported to him, of whether or not the suggestion was negated or reported, and of his reasons for his decision.
- R9 A firm is required to carry out regular assessments of the adequacy of its systems and controls to ensure that they manage the money laundering/terrorist financing risk effectively. MLRO must therefore ensure that appropriate monitoring processes and procedures across the firm are established and maintained.

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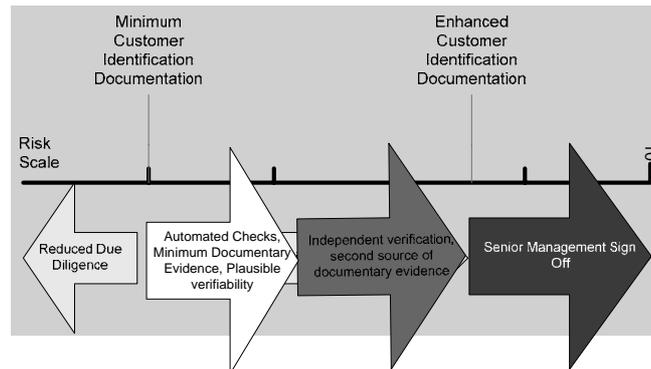
MLRO's Annual Report

- R10 At least annually the senior management of a firm, **with five or more full-time employees**, must commission a report from its MLRO which assesses the operation and effectiveness of the firm's systems of control in relation to managing money laundering/terrorist financing risk. The report must include;
 - a. The numbers and types of internal suspicious transaction reports that have been made internally and the number of, and reasons why, these that have or have not been passed onto GFIU;
 - b. bringing to the attention of senior management areas where the operation of AML/CFT controls should be improved, and proposals for making appropriate improvements;
 - c. the progress of any significant remedial programmes; and
 - d. the outcome of any relevant quality assurance or internal audit reviews of the firm's AML/CFT processes, as well as the outcome of any review of the firm's risk assessment procedures
- R11 The firm's senior management must consider the MLRO's annual report, and take any necessary action to remedy deficiencies identified in it, in a timely manner.

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What do we mean by risk-based?

- Appropriate
- Proportionate



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The Four Risk Elements

- **Customer Risk**
This is the identification of the risk posed by the type of customer
- **Product Risk**
This is the risk posed by the product proposition itself
- **Interface Risk**
This is the risk that the firm faces as a result of the mechanism through which the business relationship is commenced and transacted.
- **Country Risk**
Country risk is used to describe the risk posed to the firm by the geographic provenience of the economic activity of the business relationship.

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Customer Risk

- **Individuals**
 - Known or suspected terrorists
 - Sanctions
 - PEPs
- **Legal Entities**
- **Reduced Due Diligence on;**
 - Publicly Listed Companies
 - Financial Institutions

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Product Risk

- **Anonymous/Opaque Structures**
- **Correspondent Banking**
- **Powers of Attorney**
- **Bearer Instruments**
- **Wire Transfers**
- **Reduced Due Diligence on;**
 - One off transactions
 - Small Insurance Contracts
 - Recognised Occupational Pension Schemes
 - E-Money

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Interface Risk

- Face-to-face
- Non face-to-face
- Introducers
- Intermediaries
 - Client Accounts
- Postal Concession
- On-line and internet access

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Country Risk

R48 Firms must assess and document the risks posed by different countries and territories, or classes of countries and territories, and what additional systems of control it will implement to mitigate these risks.

- **The Equivalence Test**

R49 In making a determination of the equivalence the following three factors have to be taken into consideration:

- Legal Framework
- Enforcement and Supervision
- International Co-operation

R50 Firms must guard against customers or introductions from countries where the ability to co-operate internationally is impaired either via failings in the judicial or administrative arrangements and subject these business relationships to enhanced due diligence requirements.

R51 FATF maintain a list of Non-Cooperative Countries and Jurisdictions. Firms must take additional measures when transaction with business relationships whose source of funds derives from NCCT countries and territories.

- **Corruption Index**

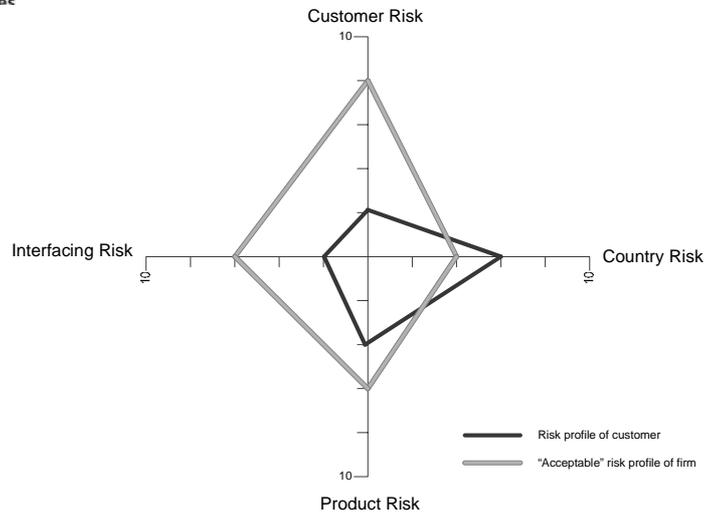
R52 Firms whose policy includes the acceptance of Politically Exposed Persons (PEPs) as customers need to take additional measures to mitigate the additional risk that the firm is exposed to from such persons originating in countries with a high propensity for bribery and corruption. This includes

- a. conducting and documenting an assessment of the countries which are more vulnerable to corruption; and
- b. the application of additional monitoring over customers from high risk countries whose line of business is more vulnerable to corruption (e.g. oil or arms sales).

- **Sanctions**

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Risk Profiling a business relationship



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When customer due diligence needs to be applied

- R53 Firms must apply customer due diligence measures in the following cases;
- When establishing a business relationship;
 - When carrying out a one-off transaction amounting to €15,000 or more, whether the transaction is carried out in a single operation or in several operations which appear to be linked;
 - Where there is a suspicion of money laundering or terrorist financing, regardless of any derogation, exemption or threshold;
 - When there are doubts over the veracity or adequacy of previously obtained customer identification data.

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Customer Due Diligence Measures

R54 Customer due diligence measures shall comprise of the following, but the extent to which each of this is applied shall be determined on a risk-sensitive basis;

- a. Identifying the customer and verifying the customer's identity on the basis of documents, data or other information **obtained from reliable and independent sources**;
- b. Identifying, where applicable, the **beneficial owner** so that the firm is satisfied that it knows who the beneficial owner is, including, as regards legal persons, trusts and similar legal arrangements **understanding the ownership and control structure of the customer**;
- c. Obtaining information on the **source of the income or wealth** and the **purpose and intended nature** of the business relationship;
- d. Conducting **ongoing monitoring** of the business relationship including scrutiny of transactions undertaken throughout the course of that relationship to ensure that the transactions being conducted are **consistent with the firm's knowledge of the customer**, the business and risk profile, including, where necessary, the source of funds and ensuring that the **documents, data or information held are up to date**.

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Beneficial Owner Corporate Entities

R55 The person(s) who ultimately owns or controls the customer and/or the natural person on whose behalf a transaction or activity is being conducted and includes, at least, the following;

- 1 In the case of a corporate entity;
 - a The natural person(s) who ultimately own or control a legal entity through direct or indirect ownership or control over a sufficient percentage of the shares or voting rights in that legal entity, including through bearer share holdings, other than a company listed on a regulated market that is subject to disclosure requirements consistent with Community legislation or subject to equivalent international standards; **a percentage of 25% plus one share** shall be deemed to meet this criterion;
 - b The natural person(s) who otherwise exercises **control over the management** of a legal entity;

■ (Cont/...)

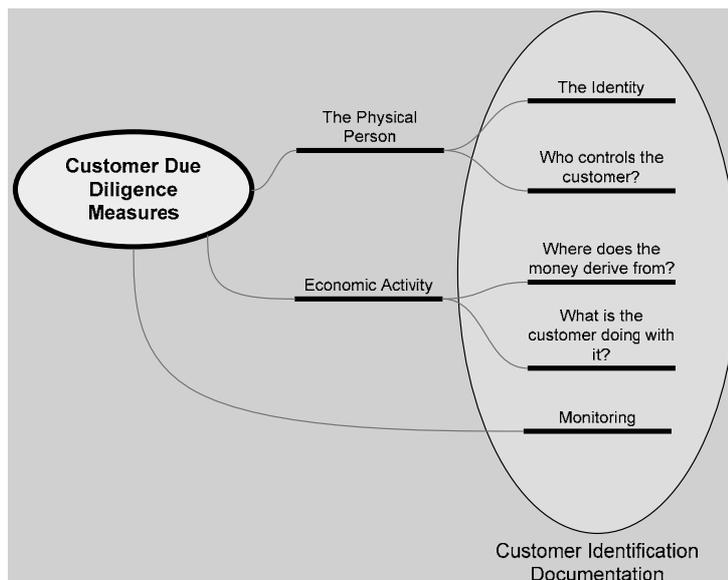
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Beneficial Owner Legal entities and arrangements

- 2 In the case of a legal entity, such as foundations, and legal arrangements such as trusts which administer and distribute funds;
 - a Where the future beneficiaries have already been determined, the natural person(s) who is the **beneficiary of 25% or more of the property** of a legal arrangement or entity;
 - b Where the individuals that benefit from the legal arrangement or entity have yet to be determined, **the class of persons in whose main interest** the legal arrangement or entity is set up or operates;
 - c The natural person(s) who **exercises control over 25% or more** of the property of a legal arrangement or entity."

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Knowing the customer



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What is minimum Customer Identification Documentation?

1. The physical person

R67 The requirements in relation to the completion of satisfactory customer identification documentation are that:

- the applicant for business will produce satisfactory evidence of his identity; **OR**
- procedures established by the firm will produce such satisfactory evidence.

2. The nature of the economic activity

R85 The minimum due diligence requirements to satisfy customer identification documentation on nature and source of income or wealth is ascertained by documenting this to a level of "plausible verifiability".

- **Plausible.**
- **Verifiability.**
- The purpose and intended nature of the relationship.

3. Monitoring

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Customer Identification Documentation INDIVIDUALS

R68 Confirming the name and likeness by gaining sight of a document from a reliable and independent source which bears a photograph

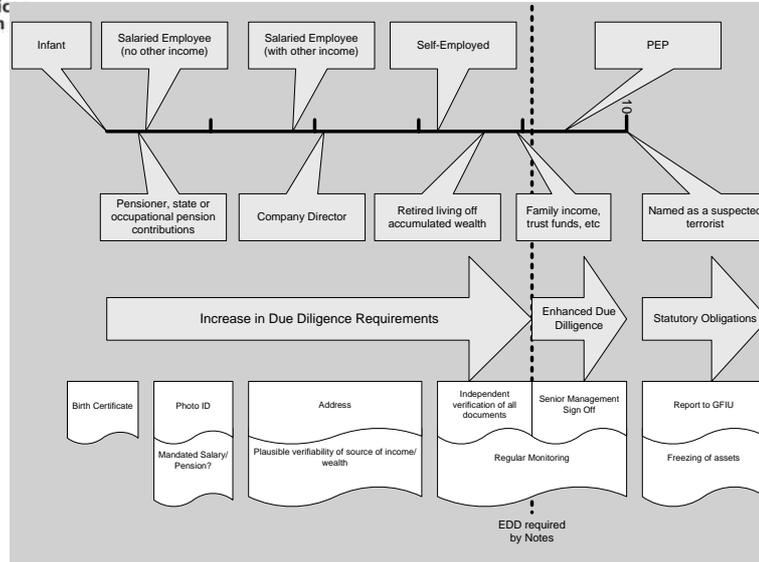
R69 The customer identification documentation obtained should demonstrate that a person of that name exists at the address given, and that the applicant for business is that person.

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Risk and CDD - Individuals



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Customer Identification Documentation BODY CORPORATE

- R72 The firm must ensure that;
- it fully understands the company's legal form,
 - it understands the company's structure and ownership.

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Customer Identification Documentation BODY CORPORATE

- R74 For corporates perceived to present a low risk, a firm can satisfy the minimum due diligence requirements by obtaining the following:
- Either:
 - Obtaining a copy of the certificate of incorporation/certificate of trade or equivalent which should include the:
 - full name
 - registered number
 - OR
 - Performing a search in the country of incorporation which confirms the items above.
 - Registered office and business addresses;
 - copy of the latest report and accounts (audited where applicable);
 - copy of the company's Memorandum & Articles of Association;
 - copy of the board resolution to open the relationship and the empowering authority for those who will operate any accounts;

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Customer Identification Documentation BODY CORPORATE

- R75 The following persons and beneficial owners as (i.e. individuals or legal entities) must also be identified:
- The beneficial owner(s) of the company
 - The shareholders of the company (if different from the beneficial owners) who own or control through direct or indirect ownership of 25% plus one share
 - The natural person(s) who otherwise exercise control over the management of the company.

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Customer Identification Documentation TRUSTS

R80 In respect of trusts, the firm should obtain the following information:

- Full name of the trust;
- Nature and purpose of the trust (e.g., discretionary, testamentary, bare);
- Country of establishment;
- Identity of the settlor or grantor;
- Identity of all trustees ;
- Identity of any protector;
- Where the beneficiaries have already been determined, the identity of the natural person(s) who is the beneficiary of 25% or more of the property
- Where the individuals that benefit from the legal arrangement have yet to be determined, the class of persons in whose main interest the arrangement is set up

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Customer Identification Documentation CLUBS AND SOCIETIES

R83 The following minimum due diligence must be conducted on clubs and societies:

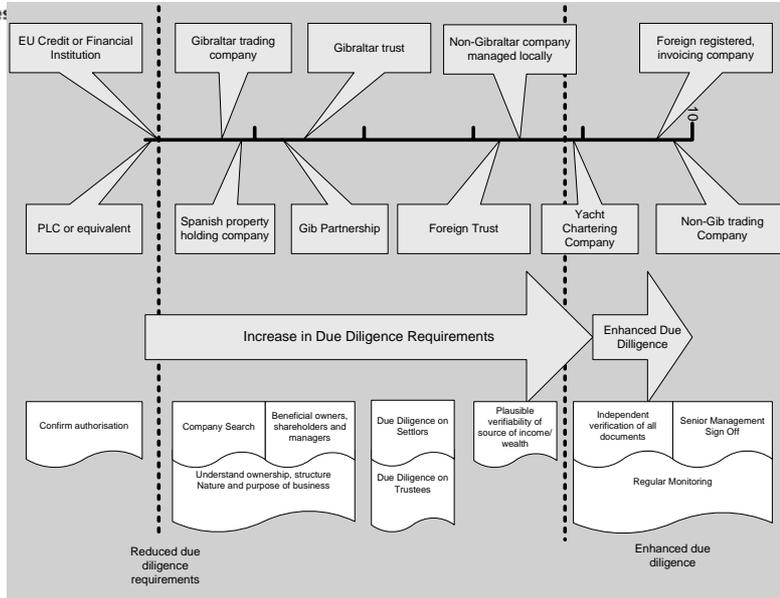
- Full name of the club/society
- Legal status of the club/society
- Purpose of the club/society
- Names of all officers

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Risk and CDD – Legal Entities

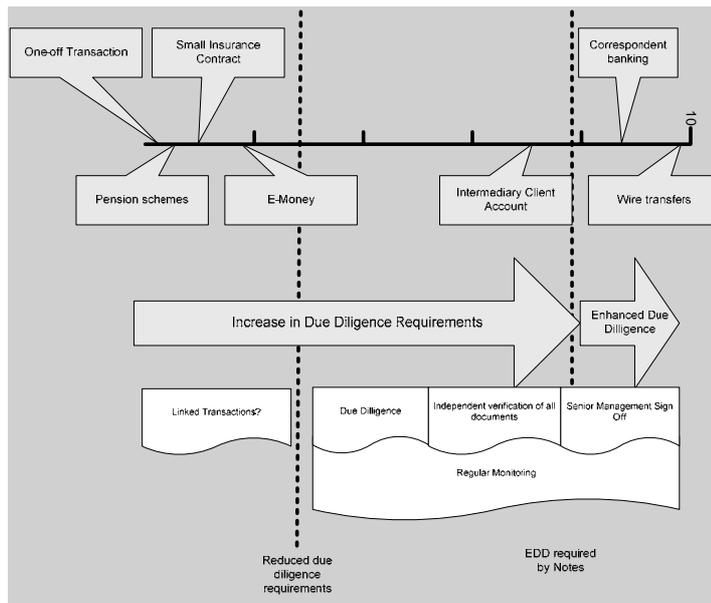


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CDD & Product Risk

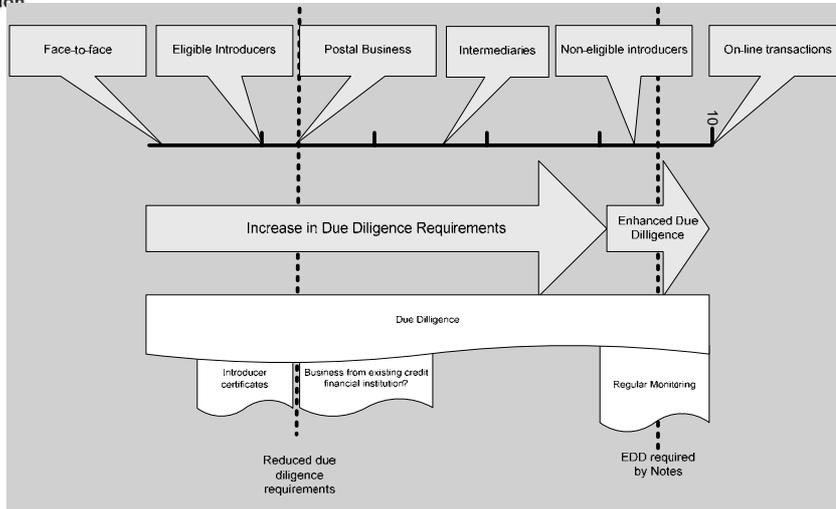


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CDD & Interface Risk

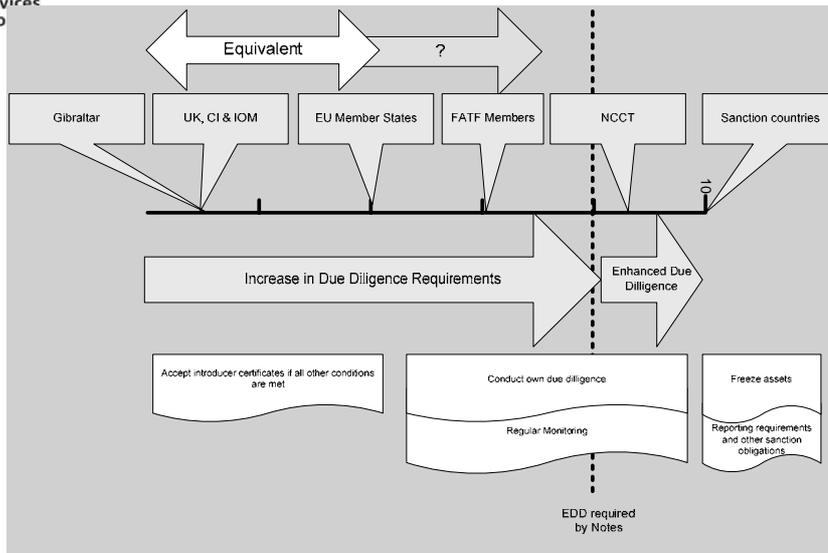


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CDD & Country Risk



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Customer Identification Documentation ECONOMIC ACTIVITY

- Nature or source of income or wealth
 - R85 The minimum due diligence requirements to satisfy customer identification documentation on nature and source of income or wealth is ascertained by documenting this to a level of “plausible verifiability”.
 - R86 As the business relationship’s risk profile increases, the firm must move away from “plausible verifiability” to “independent verification” of economic activity in order to satisfy the customer identification documentation requirements in relation to the source of income or wealth.
 - R87 Independent verification requires that firms seeks additional information on the economic activity of the business relationship from reliable and independent sources.
- Purpose and Intended Nature
 - R88 At the commencement of the business relationship a firm must document the purpose and intended nature of that relationship. This information must form part of the customer identification documentation.

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Customer Identification Documentation MONITORING

- SP3 All firms must know their customer to such an extent as is appropriate for the risk profile of that customer.
- R54 -d Conducting ongoing monitoring of the business relationship including scrutiny of transactions undertaken throughout the course of that relationship to ensure that the transactions being conducted are consistent with the firm’s knowledge of the customer, the business and risk profile, including, where necessary, the source of funds and ensuring that the documents, data or information held are up to date.
- R89 Firms must pay special attention to any activity which they regard as particularly likely, by its nature, to be related to money laundering or terrorist financing and in particular complex or unusually large transactions and all unusual patterns of transactions which have no apparent economic or visible lawful purpose.

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Customer Identification Documentation MONITORING

R90 The essentials of any system of monitoring are that:

- it flags up transactions and/or activities for further examination;
- these reports are reviewed promptly by the MLRO; and
- appropriate action is taken on the findings of any further examination.

Monitoring can be either:

- in real time, in that transactions and/or activities can be reviewed as they take place or are about to take place, or
- after the event, through some independent review of the transactions and/or activities that a customer has undertaken and in either case, unusual transactions or activities will be flagged for further examination,

and does not necessarily require sophisticated electronic systems.

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Internal Reporting

R92 Firms must establish clear processes for the reporting, processing, reporting and subsequent co-operation with law enforcement agencies arising out of an internal report. These process must ensure that;

- a. The reporting lines as short as possible and that all members of staff have direct access to the MLRO;
- b. MLRO to consider each such report and be considered in the light of all other relevant information
- c. further transactions or activity in respect of that customer, whether of the same nature or different from that giving rise to the previous suspicion, should be reported to the MLRO as they arise;
- d. MLRO must report the matter to GFU as soon as is reasonably practicable after the information comes to him ;
- e. all reports properly documented
- f. the MLRO should formally acknowledge receipt of the report which includes a reminder to the person who submitted the report of the "tipping off" provisions of the legislation;
- g. the records of suspicions and their associated investigations and documentation, including those not made externally be kept for at least five years.

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Attempted Money Laundering

- R91 Where a potential or existing business relationship attempts to conduct money laundering through a new or established relationship but fails, the obligation to report to GFU remains as this knowledge or suspicion came about from the firms trade, business or profession.

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Suspected Terrorists or Terrorist Financing Activities

- R95 Where a firm has a suspicion or belief that terrorist financing is taking place it must ensure that the transaction or activity does not proceed any further until a disclosure to GFU has been made and consent for the transaction or activity to proceed has been given.
- R96 A disclosure made under the Terrorism Ordinance must be accompanied with the information on which the suspicion or belief is based and must be made as soon as is practicable after the suspicion or belief was raised.
- R97 Firms are required, in order to comply with the provisions of the Terrorism Orders to search their customer base to ascertain whether any individuals named in them are positively matched. If a positive match is discovered, firms are required to freeze these business relationships and the report this to the Governor.

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Training Requirements

- R2b That appropriate training on money laundering is identified, designed, delivered and maintained to ensure that employees are aware of, and understand;
- their legal and regulatory responsibilities and obligations;
 - their role in handling criminal property and terrorist financing;
 - the management of the money laundering and terrorist financing risk;
 - how to recognise money laundering and terrorist financing transactions or activities; and
 - the firm's processes for making internal suspicious transaction reports.

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Documenting Compliance with the Notes

- SP5 **Firms must be able to provide documentary evidence of their compliance with the legislation and these Notes.**
- As part of the FSC's risk-based methodology for assessing regulated firms, the checklist in Chapter XI and its accompanying action plan will be requested together with any risk questionnaires that form part of the normal risk assessment process.

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KYC Review forms, etc

- Revised notes will replace existing AMLGNs
- FSC will still demand existing KYC review/retrospective review programs to be conducted and completed
- Risk methodology can be used to determine priorities
- Revised notes do not require retrospective risk profiling of existing business relationships

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Summary

- Notes are easier to understand
- Requirements are easily spotted within the text of the Notes
- Firms are required to adopt principles as they apply to their businesses
- Application must be appropriate and proportionate – Risk Based
- Application must be documented
- Practice must equal theory
- Senior Management is held accountable for compliance

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Public Consultation

- Consultation seeks views from industry and any other interested parties as to practical issues raised by the revised Notes.
- Responses requested by 31st January 2007.

The screenshot shows a web browser window displaying the Financial Services Commission Gibraltar website. The page title is "Consultation Papers and Policy". A navigation menu includes "Home", "FSC", "Consumer", "ESB", "Area of", "Evaluations", and "Sanctions". A dropdown menu is open under "ESB", listing "Data Protection", "Introduction", "Training Events", "Consultation Papers", "Presentations", "MIFID", and "Select B".

The main content area states: "The FSC has issued the following consultation paper. (Click on description to open. Will open in new window)". Below this is a table with the following data:

| Date issued | Date replies requested by | Description | Format |
|-------------|--|--|--------|
| 1 Nov 2006 | 31st January 2007 | Consultation Paper on the Revision to the AML and CFT Guidance Notes | |
| | | Revised Guidance Notes on Systems of Control to prevent the financial system from being used for money laundering or terrorist financing activities. | |
| 10 May 2006 | Date for submissions expired. Paper provided by way of background to current consultation. | Discussion Paper Re-writing the AMLGNs | |

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