Seminar on Fraud Risk & Governance: Professionals’ Responsibility & Liability

Anti Money Laundering (AML)/Combating Financing of Terrorism (CFT) Regime – Issues relating to Company Secretaries

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- Legal Framework
- Role of FIU-IND
- FATF Recommendations
- Key Issues
Background
Money Laundering is the process by which illegal funds and assets are converted into legitimate funds and assets.
Global Framework

  - 40 Recommendations - Counter-measures against money laundering
  - 9 Special Recommendations on Terrorist Financing
  - India is an observer member of FATF
  - Visit of Mutual Evaluation Team in Dec 2009

- **Asia/Pacific Group on money laundering (APG)(1997)**
  - FSRB (FATF Style Regional Body)
  - Set up to create awareness and encourage adoption of FATF standards
  - India is a member of APG

- **Egmont Group (1995)**
  - Serves as an international network for improved communication and interaction among FIUs
  - India became member of Egmont in May 2007
AML/CFT Timeline

- FATF Established at Paris
- Egmont Group Established at Brussels
- APG Set up
- 9/11 Terrorist Attack
- Prevention of Money Laundering Act, 2002 enacted
- FATF Recommendations
- Revised FATF Recommendations
- PMLA brought into force
- US Patriot Act, 2001
- Special FATF Recommendations
- FIU-IND set up
- SEBI KYC/AML Guidelines
- RBI KYC/AML Guidelines
- Amendment to PMLA
- Membership of FATF

- FATF
- AML/CFT
- Timeline
Legal Framework
The Prevention of Money Laundering Act, 2002

• Timeline
  – Enacted on 17th Jan, 2003
  – Brought into force from 1st July, 2005
  – Amended in 2009 (w.e.f. 1st June 2009)

• Main Components
  – Obligations of the financial entities - Financial Intelligence Unit-India
  – Investigation of and prosecution for money-laundering offences- Enforcement Directorate
# Reporting Entities under PMLA

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* *With effect from 1st June 2009*
Obligations of Reporting Entities under PMLA

The PMLA and the Rules impose obligation on:

- banking companies
- financial institutions
- intermediaries of the securities market

To

- appoint principal officer
- verify identity of clients
- furnish information
- maintain records

(Section 12 PMLA)
About FIU-IND
Financial Intelligence Unit - India (FIU-IND)

FIU-IND

Financial Intelligence Unit - India (FIU-IND) is the central, national agency responsible for receiving, processing, analyzing and disseminating information relating to suspect financial transactions to enforcement agencies and foreign FIUs.

More...
Domestic Cooperation Framework

**Reporting Entities**
- Banking Company
- Financial Institutions
- Intermediaries

**Regulators**
- RBI
- SEBI
- IRDA

**Intel./Law Enf. Agencies**
- IB
- RAW
- REIC
- CBDT-DGIT/CCIT
- CBEC-DGDRI/DGCEI
- ED
- EOW of Police
- EOW of CBI

**Foreign FIUs**
Types of Reports

• Suspicious Transaction Reports (STRs)
• Cash Transaction Reports (CTRs)
• Counterfeit Currency Reports (CCRs)
• NPO Transaction Reports (NTRs)*

* From 12th Nov 2009
Suspicious Transaction Reports (STRs)

**Suspicious transaction** means a transaction referred to in clause (h), including an attempted transaction, whether or not made in cash which, to a person acting in good faith –

(a) gives rise to a reasonable ground of suspicion that it may involve proceeds of an offence specified in the Schedule to the Act, regardless of the value involved; or

(b) appears to be made in circumstances of unusual or unjustified complexity; or

(c) appears to have no economic rationale or bona fide purpose; or

(d) gives rise to a reasonable ground of suspicion that it may involve financing of the activities relating to terrorism
A Suspicious Transaction

✓ May or may not involve use of cash
✓ May be in any currency
✓ Does not have any threshold limit
✓ May be an attempted transaction
✓ May or may not be linked to predicate offences
Cash Transaction Reports (CTRs)

- All cash transactions of more than rupees ten lakh
- All integrally connected cash transactions aggregating to more than 10 lakh within a month
- Monthly reporting
  - Within 15th of the succeeding month
FATF Recommendations
FATF Recommendations

Criminalization: To criminalize money laundering and terrorist financing. The definition of money laundering offenses has now expanded to include all serious offenses.

Provisional Measures and Confiscation: To put in place measures to identify, trace, freeze, or seize and finally to confiscate the illegal proceeds.

Customer due diligence: To impose duties on financial institutions to know their customers and to abolish the use of anonymous accounts.

Record keeping: Financial institutions to keep records on all the transactions that they conduct.

Suspicious transactions reporting: Financial institutions to report all transactions that raise their suspicion without alerting the clients.

Internal controls: Financial institutions adopt internal mechanisms that allow them to comply with the regulatory requirements.

Implementation: To create regulatory and supervisory agencies that are capable of implementing the international standards set by the Recommendations.

International cooperation: to put in place a system that allows it to cooperate with other countries on all aspects of law enforcement including exchange of information, preservation and confiscation of assets, and extradition.
Designated non-financial businesses and professions

“Designated non-financial businesses and professions means:

......

e) Lawyers, notaries, other independent legal professionals and accountants – this refers to sole practitioners, partners or employed professionals within professional firms. It is not meant to refer to ‘internal’ professionals that are employees of other types of businesses, nor to professionals working for government agencies, who may already be subject to measures that would combat money laundering.

f) Trust and Company Service Providers - refers to all persons or businesses that are not covered elsewhere under these Recommendations, and which as a business, provide any of the following services to third parties:

• Acting as a formation agent of legal persons.
• Acting as (or arranging for another person to act as) a director or secretary of a company, a partner of a partnership, or a similar position in relation to other legal persons.
• Providing a registered office; business address or accommodation, correspondence or administrative address for a company, a partnership or any other legal person or arrangement.
• Acting as (or arranging for another person to act as) a trustee of an express trust.
• Acting as (or arranging for another person to act as) a nominee shareholder for another person.”
Relevant activities

FATF standards are applicable when members prepare for or carry out transactions for their client concerning the following activities:

– Buying and selling of real estate;
– Managing of client money, securities or other assets;
– Management of bank, savings or securities accounts;
– Organisation of contributions for the creation, operation or management of companies;
– Creation, operation or management of legal persons or arrangements, and buying and selling of business entities.
Recommendations for DNFBP

- Recommendation 12 mandates that the requirements for customer due diligence, record-keeping requirements, and paying attention to all complex, unusual large transactions set out in Recommendations 5, 6, and 8 to 11 apply to DNFBPs.
- Recommendation 16 requires that FATF Recommendations 13 to 15 regarding reporting of suspicious transactions and internal AML/CFT controls, and Recommendation 21 regarding measures to be taken with respect to countries that do not or insufficiently comply with the FATF Recommendations, apply to DNFBPs.
- Recommendation 24 requires that countries ensure that a designated competent authority has responsibility for the AML/CFT regulatory and supervisory regime for DNFBPs.
Recommendations

• Countries may allow lawyers, notaries, other independent legal professionals, and accountants acting as independent legal professionals to send their STR to self-regulatory organizations, and they do not always need to send STR to the FIU.

• For Trust and Company Service Providers (TCSPs), obligations are applicable when as a business, they provide specified services to third parties.
Professional Privilege

• Lawyers, notaries, other independent legal professionals, and accountants acting as independent legal professionals, are not required to report suspicious transactions if the relevant information was obtained in circumstances where they are subject to legal professional privilege or legal professional secrecy. It is for each jurisdiction to determine the matters that would fall under legal professional privilege or legal professional secrecy.

• This would normally cover information lawyers, notaries or other independent legal professionals receive from or obtain through one of their clients: (a) in the course of ascertaining the legal position of their client, or (b) in performing their task of defending or representing that client in, or concerning judicial, administrative, arbitration or mediation proceedings. Where accountants are subject to the same obligations of secrecy or privilege, then they are also not required to report suspicious transactions.
Areas of concern

• Financial and tax advice – Criminals with a large amount of money to invest may pose as individuals hoping to minimise their tax liabilities or desiring to place assets out of reach in order to avoid future liabilities.

• Creation of corporate vehicles or other complex legal arrangements (trusts, for example) – such structures may serve to confuse or disguise the links between the proceeds of a crime and the perpetrator.

• Buying or selling of property – Property transfers serve as either the cover for transfers of illegal funds (layering stage) or else they represent the final investment of these proceeds after their having passed through the laundering process (integration stage).

• Performing financial transactions – Sometimes members may carry out various financial operations on behalf of the client (for example, cash deposits or withdrawals on accounts, retail foreign exchange operations, issuing and_cashing cheques, purchase and sale of stock, sending and receiving international funds transfers, etc.).

• Gaining introductions to financial institutions.
Threats and Vulnerabilities

Threats
• Establishment of companies or other complex legal arrangements to conceal the link between the proceeds of the crimes and the criminals
• Execution of financial operations on behalf of customers

Vulnerabilities
• Services that enable ownership and control through nominees and shareholding
• Services that inherently have provided more anonymity.
• Services that conceal improperly beneficial ownership from competent authorities
• The Self Regulatory Organisations (ICAI, ICWAI, ICSI etc.) sets standards for and regulates professional conduct
• Professional privilege prevents disclosure of client’s information
Red Flag Indicators.

- Legal structure of client has been altered numerous times (name changes, transfer of ownership, change of corporate seat).
- Management appears to be acting according to instructions of unknown or inappropriate person(s).
- Unnecessarily complex client structure.
- The client is reluctant to provide all the relevant information or the accountant has reasonable doubt that the provided information is correct or sufficient.
- Individual or classes of transactions that take place outside the established business profile, and expected activities/transaction unclear.
- Employee numbers or structure out of keeping with size or nature of the business (for instance the turnover of a company is unreasonably high considering the number of employees and assets used).
- Client starts or develops an enterprise with unexpected profile or early results.
- Indicators that client does not wish to obtain necessary governmental approvals/filings, etc.
- Payments received from un-associated or unknown third parties and payments for fees in cash where this would not be a typical method of payment.
Red Flag Indicators..

- Entities with a high level of transactions in cash or readily transferable assets, among which illegitimate funds could be obscured.
- Investment in real estate at a higher/lower price than expected.
- Large international payments with no business rationale.
- Unusual financial transactions with unknown source.
- Clients with multijurisdictional operations that do not have adequate centralised corporate oversight.
- Clients incorporated in countries that permit bearer shares.
- Over and under invoicing of goods/services.
- Multiple invoicing of the same goods/services.
- Falsely described goods/services – Over and under shipments (e.g. false entries on bills of lading).
- Misuse of pooled client accounts or safe custody of client money or assets.
- Advice on the setting up of legal arrangements, which may be used to obscure ownership or real economic purpose (including setting up of trusts, companies or change of name/corporate seat or other complex group structures).
- Misuse of introductory services, e.g. to financial institution.
Key Issues
Key Issues

• Regular interaction with Institutes
• Increase awareness amongst members
• Explore instances not covered by professional privilege
Thank You

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