

CP(2016-02)

Consultation Paper – of the Cyprus Securities and Exchange Commission regarding the application of articles 61 and 62 of Law 188(I)/2007

The Cyprus Securities and Exchange Commission (“CySEC”) in adhering to effective regulation and consultation procedures with market participants in relation to the application of articles 61 and 62 of Law 188(I)/2007 for the prevention and suppression of Money Laundering and Terrorist Financing, following its recent amendment by Law 18(I)/2016, issues the present Paper requesting for the market’s comments/input on the proposed additional parameters that need to be taken into consideration by regulated entities when assessing the risk of commencing a business relationship with persons whose identity has not been verified.

It is noted that CySEC intends to issue soon, an amendment to Paragraph 1 of the Fourth Annex of CySEC Directive 144-2007-08 for the Prevention of Money Laundering and Terrorist Financing, regarding the practical procedures that may be followed in applying the measures set out in article 64 of the Law, in relation to non face-to-face customers.

Therefore, CySEC calls for comments on the above subject to be submitted by **Wednesday 20th April 2016** at legal@cysec.gov.cy

The proposed Circular which outlines the additional parameters is attached as **Annex A**.

April 13, 2016

Annex A

TO : i. **Cyprus Investment Firms ('CIFs')**
ii. **Administrative Service Providers ('ASPs')**
iii. **Undertakings for Collective Investment in Transferable Securities ('UCITs')**
iv. **UCITS Management Companies ('UCITs MC')**
v. **Alternative Investment Fund Managers ('AIFMs')**
vi. **Alternative Investment Funds ('AIFs')**
vii. **Alternative Investment Funds with a Limited Number of Persons ('AIFLNP')**

FROM : **Cyprus Securities and Exchange Commission**

DATE : **12 April 2016**

CIRCULAR NO. : **COXX**

SUBJECT : **Application of articles 61 and 62 of the Prevention and Suppression of Money Laundering and Terrorist Financing Law of 2007**

The Cyprus Securities and Exchange Commission ('CySEC'), wishes to inform all interested parties of article 30 of the Prevention and Suppression of Money Laundering and Terrorist Financing (Amending) Law of 2016 (L18(I)/2016), which amends article 62 of Law 188(I)/2007 for the Prevention and Suppression of Money Laundering and Terrorist Financing Law (the 'Law'), pertaining to the obligation for verification of the identity of clients/beneficial owners. Article 62 has been amended as follows:

«62. (1) ~~The identification~~ **The verification** of the identity of the client and the beneficial owner occurs before the establishment of a business relationship or the carrying out of an occasional transaction.

(2) By way of derogation from paragraph (1), ~~the identification~~ **the verification** of the identity of the customer and the beneficial owner may be completed during the establishment of a business relationship if this is necessary not to interrupt the normal conduct of business and where there is little risk of money laundering or terrorist financing occurring. In such situations these procedures shall be completed as soon as practicable after the initial contact and before any transactions take place.

(2A) Without prejudice of what is stated in paragraph (2) by way of derogation from paragraph (1), for cases that fall under the supervision of the Cyprus Securities and Exchange Commission the verification of the identity of the customer and the beneficial owner may be completed during the establishment of a business relationship if this is

necessary not to interrupt the normal conduct of business and where there is little risk of money laundering or terrorist financing occurring:

It is understood that in such situations these procedures shall be completed as soon as practicable after the initial contact.

[...]».

Following the above amendment, CySEC wishes to draw the attention of interested parties to the following:

- (i) According to article 61(1) of the Law, customer identification and customer due diligence procedures include identifying the customer/beneficial owner and taking adequate measures to verify the identity of the customer/beneficial owner, in accordance to their degree of risk (on the basis of documents, data or information obtained from a reliable and independent source).
- (ii) The identification of a customer/beneficial owner occurs **before the establishment** of a business relationship¹ with the said person.

It is noted that the identification procedure includes the following:

- i. Creation of an economic profile for the customer/beneficial owner, and
 - ii. Carrying out a suitability test for the customer/beneficial owner in accordance to article 36(1)(c) of the Investment Services and Activities and Regulated Markets Law of 2007 (the '**L. 144(I)/2007**') and paragraph 14 of CySEC Directive 144-2007-02 for the Professional Competence of Investment Firms and the Natural Persons employed by them (the '**Directive 2**'), and/or
 - iii. Carrying out an appropriateness test in accordance to article 36(1)(d) of L.144(I)/2007 and paragraph 15 of Directive 2.
- (iii) As a general rule, in accordance to article 62(1) of the Law, the verification of identity of a customer/beneficial owner, also takes place **before the establishment** of a business relationship with the said person.
 - (iv) By way of derogation to the general rule of article 62(1) of the Law, in accordance to the new article 62(2A) of the Law, the verification of identity of the customer/beneficial owner of a CySEC regulated entity may be completed **during the establishment** of a business relationship:
 - (a) if this is necessary not to interrupt the normal conduct of business, and
 - (b) where there is little risk of money laundering or terrorist financing occurring, and

¹ "business relationship" in accordance to article 2 of the Law, means a "a business, professional or commercial relationship which is connected with the professional activities of persons engaged in financial and other business activities in accordance with this section and which is expected, at the time when the contact is established, to have an element of duration."

(c) where the process of verifying the procedure is completed as soon as practicable after the initial contact.

(v) With the addition of the new article 62(2A) of the Law the obligation of not trading “during the establishment of a business relationship” is omitted, in cases where the conditions of paragraph (iv) above, for verification during the establishment of a business relationship, apply.

(vi) In relation to paragraph (iv) above, CySEC considers that, when commencing the establishment of a business relationship with a client/beneficial owner whose identity has not been yet verified, the risk may be assessed as low when, as a minimum, the following, among others, are taken into consideration:

- If the verification of the customer/beneficial owner’s identity has not been completed, the cumulative amount of deposited funds of a customer/beneficial owner should not exceed €2,000, irrespective of the number of accounts the client/beneficial owner holds with the regulated entity.
- The cumulative time in which the verification of the identity of a customer/beneficial owner is completed, must not exceed 15 days from initial contact.
- Within the timeframe of 15 days from initial contact, the regulated entity takes all reasonable measures to ensure that the percentage of customers that have not complied with the request to submit verification documents, is considerably low (e.g. the regulated entity issues requests/reminders to the customer/beneficial owner informing them of their obligation to submit the requested documents for the verification of their identity).
- Where the verification of the customer/beneficial owner’s identity has not been completed during the designated timeframe of 15 days, the commencement of a business relationship must be terminated **on the date of the deadline’s expiry** and all deposited funds must be returned **automatically** to the customer/beneficial owner, in the same bank account from which they originated: the return of funds must occur **immediately**, regardless of whether the customer has requested the return of their funds or not.

The returned funds (deposits) include any profits the customer has gained during their transactions and exclude any losses incurred.

- Within the timeframe of 15 days from initial contact, the customer/beneficial owner must undergo at least one Enhanced Due Diligence measure in accordance to article 64 of the Law.
- No funds are withheld and no accounts are frozen, save for those cases of suspicion of money laundering, where the regulated entity is under obligation to immediately report their suspicion to MOKAS and notify CySEC of the suspicious transaction incident in the designated procedure.

Regulated entities must warn their customers **appropriately/sufficiently/in due time** of the above procedure and receive their explicit consent as to the procedure that is to be followed, before the establishment of the business relationship.

It is noted that regulated entities are under obligation to include in their risk management/money laundering manual, the designated internal practice, the measures, procedures and controls undertaken for the proper and effective implementation and monitoring of compliance with the new article 62(2A) of the Law.

Therefore, regulated entities are required to identify all their customers/beneficial owners in all cases, prior to the establishment of a business relationship.

No deposits should be accepted by a regulated entity, where the customer/beneficial owner has not provided information as to:

- (i) The full identification of the client, and
- (ii) The creation of an economic profile, and
- (iii) The completion of the suitability test and/or
- (iv) The completion of the appropriateness test.

In relation to the verification of customers/beneficial owners' identity, CySEC urges regulated entities to complete the prescribed procedure before the establishment of a business relationship. In those extraordinary cases where the verification of a customer/beneficial owner's identity takes place during the establishment of a business relationship, regulated entities are required to take into consideration, in all cases, as a minimum, the parameters presented herein.

Yours sincerely

Demetra Kalogerou
Chairman, Cyprus Securities and Exchange Commission

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