



CONSULTATION PAPER

OVERRIDING PRINCIPLES FOR A REVISED KNOW YOUR CUSTOMER FRAMEWORK

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A. Introduction

Financial services businesses will be aware that Guernsey (along with the other Crown Dependencies: Jersey and the Isle of Man) have recently been subject to two separate reviews of the Bailiwick's anti-money laundering systems.

The first review, carried out in 1999, was a FATF-style evaluation carried out under the aegis of the Offshore Group of Banking Supervisors ("OGBS"). The review team comprised representatives of both the Financial Action Task Force on Money Laundering ("FATF") and the OGBS. A summary of the OGBS/FATF review is available on the Commission's web site.

The second review, conducted earlier this year, was an examination of Guernsey under FATF's 25 criteria defining non-co-operative countries or territories. This examination was carried out by the Europe Review Group of FATF. Financial services businesses will be aware that the Crown Dependencies did not appear on FATF's list of non-co-operative countries or territories. It should also be noted that during 2001 FATF plan to discuss the issue of reliable introductions with a view to issuing recommendations on the subject. The Bailiwick would expect to follow any revised recommendations or interpretations issued by FATF.

Although the Crown Dependencies have emerged in a positive light from the two evaluations, it is apparent from the evaluation reports that the Bailiwick's anti-money laundering systems need to take account of recent international developments. With this in mind, representatives of all three jurisdictions have entered into detailed discussions and, where possible, have agreed to minimise any inconsistencies in their approaches to certain specified overriding principles for a revised know your customer framework. These are to be known as the Overriding Principles, which are not an exhaustive list of issues raised by FATF, but are major points relevant to the Commission's Guidance Notes on the Prevention of Money Laundering ("the Guidance Notes") that are common to all Crown Dependencies. It has also been agreed that the Islands will consult with their respective finance sectors on the Overriding Principles with a view to adopting guidance in these areas in each jurisdiction's anti-money laundering guidance notes. The areas to be covered by the Overriding Principles are as follows:

1. Other than in certain limited and specific circumstances (see section B.1 of this Consultation Paper), financial services businesses will be required to verify the identity of their customers and, if different, the principals behind their customers. No distinction is made between accounts (and other financial services products) opened in person and those opened remotely.
2. Reliable introductions must only be accepted from regulated entities subject to anti-money laundering regulations and resident in "approved" jurisdictions (known as Appendix C jurisdictions in Guernsey). There are also provisions to

permit certain group introductions from non-Appendix C jurisdictions. In all cases, documentary evidence of identity of the underlying customer **must** be held in Guernsey on the accepting financial services business' file.

3. A list of jurisdictions will be agreed by all three Crown Dependencies although each of the Crown Dependencies will have discretion to draw up from the agreed list their own list of "approved" jurisdictions. This will be reviewed regularly in light of international developments.
4. Financial services businesses must introduce a progressive client review programme to satisfy themselves that they have a true documentary record of the ultimate identity of all their customers prior to the coming into force of the Criminal Justice (Proceeds of Crime) (Bailiwick of Guernsey) Law, 1999.
5. Exemptions for certain postal, telephonic and electronic business may be restricted to certain businesses in specified circumstances.

These five Overriding Principles are described in detail in the remaining sections of this Consultation Document.

B. Overriding Principles

1. Knowing client identity

The Guidance Notes currently permit reliable introductions from specified financial services businesses. In such instances, financial services businesses might not be in possession of verification documentation (ie verifying the name and permanent address) of the underlying customers. However, this information must be available to financial services businesses on demand.

The Commission is of the view that this regime requires revision for the following reasons:

- (i) FATF is of the opinion that, if verification documentation must be produced upon demand, there is no reason why the information cannot routinely be provided at the commencement of a client relationship. This approach would avoid the potential problem of reliable introducers discovering legal obstacles to providing information requested of them. The Commission sees merit in FATF's opinion; and
- (ii) Financial services businesses cannot be said to know their customers (and be in a good position to recognise a suspicious transaction and the other risks to their business) if they are not in possession of verification documentation including the name, address, nationality, occupation, source of wealth, source of funds, etc. of a client.

The Commission therefore proposes that, although reliable introducers may continue to be utilised to carry out verification (along the lines laid out in the Guidance Notes), in future, copies of all verification documents (in hard or electronic format) should be

obtained by the accepting financial services business in Guernsey at the outset of a client relationship. Copies must be certified as a true copy of the original document by the reliable introducer. This documentation will include the name and permanent address nationality, occupation, source of wealth, source of funds, etc. of all underlying principals.

Financial services businesses are invited to comment on the proposal that in addition to being required to know the identity of all (underlying) customers they should be in possession of a copy of verification documentation.

With reference to the proposal above, the Crown Dependencies consider it desirable to adopt a common approach on who should be considered to be the underlying principals in a client relationship. The proposed common approach is as follows:

- (a) In the case of *deposits placed by banks in a fiduciary capacity* with a Guernsey bank; or

in the case of *deposits with banks* placed on behalf of employee benefit trusts, , unit trusts, limited partnerships, other collective investment funds, unit linked funds, small self administered schemes, and other “pooled” financial services products; or

in the case of lawyers’ and similar *client accounts* held at banks by a professional firm

the following shall apply:-

The introducer will be considered to be the principal where:

- The account (or other financial services product) may only be operated by the introducing financial services business. **No** underlying client shall have any direct relationship with the Guernsey financial services business; and
- There are numerous underlying customers making verification of identity impractical or impossible; and
- The Guernsey financial services business is able to identify its part in an audit trail which involves such a pooled financial services product; and
- The introducing financial services business is operating from an Appendix C jurisdiction.

- (b) Where a financial services business is providing for the *establishment of a trust* principals will include:

the settlor and any other person settling assets into the trust;

any person exercising significant influence over the trust; and

any beneficiaries who are:-

- (A) to receive a distribution from the trust without the need for the trustee to exercise his/her discretion; or
- (B) beneficiaries to whom payment of a distribution from the trust is imminent. This means that the identity of any such beneficiaries might only be verified when the trustee has already exercised his discretion to make a distribution to that beneficiary. (Of course where there is a finite list of known beneficiaries the trustee may be in a position to verify the identity of all beneficiaries from the outset. If this is so then the Commission would expect all beneficiaries to be identified at the beginning of the business relationship unless there are beneficiaries who are unaware that they might benefit from the trust.)
- (c) Where an applicant for business is *acting as trustee* and is seeking to enter into a business relationship in a trustee capacity, the principals will include the trustee and any other person whom the trustee has identified as a principal under (b) above.
- (d) Where an applicant for business is *acting as a nominee*, the principals will be the ultimate beneficial owner (ie a natural person) and any other individual on whose instruction the applicant is accustomed to act.
- (e) Where an applicant for business is a *corporate vehicle*, the principals will be the ultimate beneficial owner (ie a natural person) and any individual on whose instruction the applicant is accustomed to act. Where there are shareholders holding less than a certain percentage (see below) of a corporate vehicle's shares it may not be necessary to consider such small shareholders as principals. In the case of corporate vehicles quoted on a recognised stock exchange (or subsidiaries of such quoted companies), the corporate vehicle may be considered to be the principal.
- (f) Where the applicant for business is a *partnership* the principals will be the partners of that partnership.

Financial services businesses are invited to comment on the proposal that the persons described in paragraphs (a) – (f) above should be considered to be the underlying principals.

Financial services businesses are also invited to suggest what percentage they consider to be appropriate for the de minimis provisions suggested in paragraph (e) above.

2. *Reliable introductions*

The Guidance Notes currently permit financial services businesses to receive reliable introductions either from a financial services business in an Appendix C jurisdiction, or from a group company or from a Bailiwick of Guernsey financial services business.

Reliable introducers must, inter alia, be regulated and bound by anti-money laundering regulations at least equivalent to those in Guernsey.

The following is now proposed:

Financial services businesses would only be permitted to take reliable introductions from a regulated financial services business which is subject to anti-money laundering regulations **and** which is either:-

- (a) a Bailiwick of Guernsey financial services business; or
- (b) a financial services business based in an Appendix C jurisdiction.

In addition, financial services businesses would also be permitted to accept reliable introductions from other **regulated** group financial services businesses which are based in non-Appendix C jurisdictions but are part of a group subject to consolidated supervision in an Appendix C jurisdiction. All such entities within a group would be expected to be subject to an anti-money laundering standard at least equivalent to the relevant Appendix C jurisdiction's anti-money laundering legislation and policy. The introducer must demonstrate to the accepting financial services business the enforcement of a group compliance policy.

In all cases, a revised reliable introductions regime will also require that copies of verification documentation must be held on the accepting institution's files.

(Proposals on knowing your customer and obtaining verification documentation are discussed in section B.1 above and financial services businesses are invited to comment on this proposal there.)

Financial services businesses are invited to comment on the proposal that reliable introductions should only be from those entities described in B.2 above.

3. *Approved jurisdictions*

Until recently, Guernsey had included jurisdictions in Appendix C to the Guidance Notes which were not FATF members or Crown Dependencies. The Bailiwick received criticism in this area during both of the evaluations mentioned in section A. above. The decision was therefore taken on 21 July 2000 to remove all non-FATF members from the list with the exception of the Isle of Man and Jersey.

It should be noted that there are currently seven FATF members whom Guernsey does not consider to be equivalent in terms of anti-money laundering policy. These are Argentina, Aruba, Austria, Brazil, Mexico, Netherlands Antilles and Turkey. (Aruba and Netherlands Antilles are considered to be FATF members as they are part of the Kingdom of the Netherlands.)

It is proposed that the Crown Dependencies should draw up a list including no more than FATF members, jurisdictions covered by the European Union's anti-money laundering directive and the Crown Dependencies. *Each Commission in each of the*

Crown Dependencies will exercise its judgement over which FATF and EU members are to be included on their own list. The list of jurisdictions will be regularly reviewed, taking into account FATF and other pronouncements and evaluations.

Financial services businesses are invited to comment on the proposed method of selecting approved jurisdictions.

4. *Business relationships existing at the date of the introduction of “all crimes” legislation*

Another area which attracted the attention of FATF was the verification of the identity of clients current at the time of the introduction of the Criminal Justice (Proceeds of Crime) (Bailiwick of Guernsey) Law, 1999 (“the Law”).

The Law does not have retrospective effect and does not require the production of evidence of identity of customers who were taken on before 1 January 2000. The Commission recognises the difficulties that arise in this area, especially in the case of financial services businesses with large numbers of customers. The following action is therefore proposed:

- (a) Financial services businesses must undertake the identification procedures required under law and set out in the Guidance Notes and satisfy themselves that they have on record evidence of the true identity of the underlying principals of all of their accounts or other financial services products, along with other information necessary to know their customers (refer to section B.1).
- (b) Financial services businesses will be required to confirm in writing to the Commission the existence of a risk-based programme for achieving the above. This would include the completion of the client review programme normally within five years.
- (c) The Commission will require periodic reports from financial services businesses to monitor progress towards meeting this client review programme.

Financial services businesses are invited to comment on the proposed regime for reviewing pre-2000 customer files.

5. *Exemptions for certain postal, telephonic and electronic business.*

It is proposed that the exemptions for certain postal, telephonic and electronic business detailed in paragraphs 54 to 56 of the Guidance Notes be restricted to certain financial services businesses and to circumstances where the risk of money laundering is minimal.

Financial services businesses are invited to comment on which businesses should benefit from these exemptions and under which circumstances these exemptions should be available to those businesses.

C Conclusion

The Commission invites comments on the above **in writing** from all financial services businesses and other interested parties. Comments should be sent to the address shown below. In submitting comments to the Commission, respondents are asked to be mindful of the need for Guernsey to adhere to FATF's 40 Recommendations and to not meet any of the 25 criteria for defining non-co-operative countries and territories. *Comments should be provided to the Deputy Director of Banking at the Commission no later than Friday 2 February 2001.*

These comments will be considered as part of the process of producing revised Guidance Notes. It is anticipated that this revised version will be posted (in draft) on the Commission's web-site in 2001 for further consultation.

Guernsey Financial Services Commission
18 December 2000

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