ΕΠΙΤΡΟΠΗ ΚΕΦΑΛΑΙΑΓΟΡΑΣ ΚΥΠΡΟΥ
CYPRUS SECURITIES AND EXCHANGE COMMISSION

To : **Regulated Entities**
i. CIFs
ii. ASPs
iii. UCITS Management Companies
iv. Internally managed UCITS
v. AIFMs
vi. Internally managed AIFs
vii. Internally managed AIFLNPs
viii. Companies with sole purpose the management of AIFLNPs

From : **Cyprus Securities and Exchange Commission**

Date : **21 April 2021**

Circular No : **C437**

Subject : **Common weaknesses/deficiencies and good practices identified during the onsite inspections performed in relation to the prevention of money laundering and terrorist financing**

The Cyprus Securities and Exchange Commission ('the CySEC') wishes, with this circular, to inform the Regulated Entities of the following:

During the year 2019-2020, the CySEC performed onsite inspections to its Regulated Entities to assess their compliance with the Prevention and Suppression of Money Laundering and Terrorist Financing Law ('the Law') and the CySEC's Directive for the Prevention and Suppression of Money Laundering and Terrorist Financing ('the Directive').

Although CySEC has identified some good practices applied by Regulated Entities, some common weaknesses/deficiencies were also observed across Regulated Entities. Thus, in addition to the measures already outlined by the CySEC to facilitate Regulated Entities' full compliance, CySEC provides recommendations for Regulated Entities to implement.

A. <u>Consolidating good practices identified</u>

The CySEC identified the following good practices when carrying out its onsite inspections:

- **EU/UN Sanctions screening** – measures and sufficient resources allocated to maintain proper records for screening, and to implement procedures for ongoing sanctions screening against new or updated terrorists and sanctions lists after the establishment of a business relationship.

- **AML/CFT Risk Assessment** – updated risk-based AML/CFT supervision framework, based on the Joint Guidelines under Articles 17 and 18(4) of Directive (EU) 2015/849 on simplified and enhanced customer due diligence. This has led in establishing a multifaceted system to assist in proper categorization of customers and efficient resource allocation, leading to effective screening processes, application of adequate EDD measures and increased focus on high-risk customers.
- **Ongoing monitoring** - Increased and continuous scrutiny of the customers' business relationships (at initial points of contact and during the business relationship with customers) resulting in the reduction of onboarding risky customers and reducing the overall ML/TF risk.
- **Increased AML/CFT staff training** – multi-faceted approach to training and awareness of staff. Targeted e-learning delivered to relevant staff, including use of relevant typologies and red flags, such as those contained in the FATF guidance.
- **AML/CFT Internal Control Measures**: Keeping AML/CFT policies and procedures up to date to ensure compliance with evolving legal and regulatory obligations.
- **Record keeping:** Records of customer identification and transactions data and information are retrieved quickly and without delay.

B. <u>Common weaknesses/deficiencies identified</u>

The CySEC identified the following common weaknesses/deficiencies when carrying out its onsite inspections:

i. Customer Due Diligence (CDD) Measures

- The customers' economic profile, on some occasions, was not complete. Specifically, information such as the size and source of income, expected turnover, source of funds and size of wealth was not always documented, leading to ineffective monitoring and thereby increasing the vulnerability of Regulated Entities being used for illicit purposes.
- Furthermore, the CySEC found weaknesses in the risk-based approach processes to verifying the collected customer' data and information, thus contributing to poor customer economic profile-building. This included insufficient measures taken to verify the size of income and the source of customer funds and wealth.
- In some cases, it was observed that the complexity of an underlying corporate ownership structure, did not drive the level of EDD at the onboarding stage, including assessing whether the complexity of the structure was proportionate to the rationale for the business relationship. Understanding customers' business model, activities and operations is key to subsequently understand whether a customer's trading activity could be suspicious.

- A number of Regulated Entities were found to document insufficient and/or inaccurate information about the customers' main business activities and operations. A broad and generalised description and documentation of customers' activities and operations, or lack of (accurate) information, may lead the Regulated Entity to not fully understanding the risks associated with the customers' business activities. This entails a risk that the Regulated Entity will not be able to conduct accurate follow-up of the business relationships, therefore reducing the ability to monitor the customers' transactions in a satisfactory manner – ultimately increasing the overall ML/TF risk.

ii. AML/CFT Risk Assessments

- On a number of occasions, it was observed that the AML/CFT risk assessments were not reviewed to evaluate whether they needed adjustment upon subsequent changes of the customers' risk profiles. As a result, the assessment of the customers' ML/TF risks was not up to date and therefore CDD and ongoing monitoring was not always effective or as effective as they could have been.

iii. Transaction Monitoring

- It has been observed that transaction monitoring systems include a combination of applying standard or predefined transaction monitoring rules and thresholds along with applying rules that are based on customer history and deviations from established patterns of behavior. However, it is noted that where such systems have not been calibrated sufficiently based on a customer's business model, there is a risk that monitoring may not be proportionate or appropriate to the specific risks faced by that customer.

Regulated entities need to be making constant and continuous efforts to ensure processes to prevent ML/TF are adequate. The consequences of failing to manage risks associated with ML/TF are serious and cause damage not only to Regulated Entities, but to the financial system as a whole.

The publication of the above common weaknesses and deficiencies identified during the onsite inspections may prove useful to Regulated Entities when identifying and managing risk and in considering their AML/CFT policies, procedures and controls, thus ensuring full compliance with the Law and the Directive. CySEC also takes this opportunity to inform Regulated Entities to be aware of the above findings and avoid similar pitfalls. In the event of non-compliance, Regulated Entities will be subject to the administrative sanctions available to and enforced by CySEC under the Law.

Sincerely,

Demetra Kalogerou
Chairwoman of the Cyprus Securities and Exchange Commission