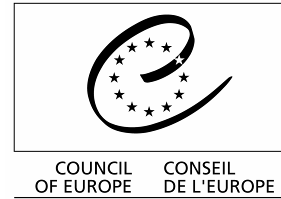

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Committee of experts on the evaluation of anti-money laundering measures and the financing of terrorism

MONEYVAL

Typology research

Use of securities in money laundering schemes[1]

[1] Adopted by MONEYVAL at its 27 Plenary meeting (7-11 July 2008).

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INTRODUCTION

1. The present report is a result of the project[2] initiated in 2007 by MONEYVAL in the framework of its typologies-related activities. When launching this project, it was noted that that there was no up-to-date typology review concerning money laundering in the securities market and that it would be valuable to consider the specific needs and requirements of the MONEYVAL member countries in this respect. The financial markets across the MONEYVAL member countries are at various stages of development and, in a number of securities markets, trading involves financial instruments (such as bills of exchange) which are not actively traded in other markets. It was therefore considered that it would be valuable to prepare a report which takes into account the specific experiences of MONEYVAL countries.

2. The banking system will always be vulnerable to money laundering. Even when money launderers use securities transactions, settlement of these transactions will normally be through the banking system. The systemic risk to banks and securities houses of becoming involved in money laundering is also similar in that there are severe reputational risks of being found to be involved in money laundering schemes and such involvement also heightens the risk of fraud being perpetrated against the institution and its customers.

3. As countries improve their controls over and defences against money laundering, criminal organisations will seek to utilise more sophisticated techniques to disguise their sources of finance. It was considered that the securities market could be vulnerable to money laundering for a number of reason, namely:

   - the speed with which securities transactions can be executed and settled;
   - the number of large value transactions;
   - The large volume of over-the-counter securities transactions in MONEYVAL member countries;
   - the international nature of the securities markets;
   - mixing 'clean' and 'dirty' money in securities market transactions together with the large volume of transactions making investigations extremely difficult; and
   - many MONEYVAL members are developing their securities markets and may experience rapid growth both in the volume sophistication and complexity of transactions. The rapid evolution of securities markets and the complexity of some of the transactions can mean that systems and controls do not develop as rapidly.

4. The original objectives of the project were to:

   - obtain details of money laundering schemes in the securities sector, which would include obtaining details of sanitised cases that could be included in a published report;
   - obtain details of other types of fraud conducted in the securities market within the MONEYVAL jurisdictions, considering the relationship between these frauds and money laundering; and
   - develop recommendations to enhance detection and investigation of money laundering schemes, including identifiers (red flags) as well as developing recommendations on improved co-operation between regulators and law enforcement agencies.

5. It was agreed to circulate a survey to participating MONEYVAL member countries. The objectives of the survey were to obtain information on:

   - the type and volume of securities trading in each participating country
   - national money laundering legislation
   - monitoring techniques and procedures
   - details of money laundering investigations involving securities

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[2] This project was supported by a voluntary contribution of the United States of America.

6. As noted above it was appreciated that, in certain economic climates securities markets can develop rapidly in the number, type and complexity of products traded. During the first review of the project at the MONEYVAL typologies meeting in Becici, Montenegro in 2007 representatives of MONEYVAL members FIUs, supervisors and law enforcement agencies stated that there was a clear need for guidance for the securities market together with a description of the instruments traded on securities markets. At this meeting it was agreed that the scope of the report would be linked to the securities covered by the European Union's Markets in Financial Instruments Directive as set out in Annex 1. It was also agreed that there would be a description of the main financial instruments traded on the securities markets as well as a consideration of the relative vulnerability to money laundering of the main areas of business.

7. Some of the activities described may not be currently applicable to all MONEYVAL countries at the present time. It is, however, noted that securities markets are dynamic and can develop rapidly as a result of borrower and investor demand as well as in reaction to the requirements of a developing economy. Furthermore, in a global economy, investors and borrowers may seek to utilise products in other countries if these are not available in their domestic market. It is therefore important that regulators and law enforcement agencies remain aware of the evolution of their domestic securities markets and trends adopted by investors and borrowers and are alert to the potential for money laundering posed by newly developed securities products.

8. The report was compiled by the project team[3] from contributions by nineteen countries (Armenia, Azerbaijan, Bosnia and Herzegovina, Bulgaria, Croatia, Cyprus, Estonia, Latvia, Liechtenstein, Lithuania, Malta, Moldova, Montenegro, Poland, Romania, Slovenia, "the former Yugoslav Republic Macedonia", United Kingdom and Ukraine) as well as drawing on a number of publicly available sources. Several countries made presentations during the workshop held in Becici, in the framework of the 2007 MONEYVAL typology exercise. Various elements of the presentations and replies to the questionnaire have been incorporated into this report.

9. The report is intended to be used as a guide for all those who have an interest in the detection and prevention of money laundering in the securities markets, both supervisors and market participants.

[3] Oleksiy Feschenko, Project leader (Ukraine), John Baker (United Kingdom), Irina Talianu (Romania), Galyna Sapunova (Ukraine).

EXECUTIVE SUMMARY

1. As a result of more stringent controls introduced by banks, criminal organisations are constantly looking for alternative ways in which to legitimise the proceeds of crime. Due to the substantial transaction volumes and short execution and settlement deadlines the securities market is seen as an attractive alternative means of money laundering. Furthermore, the continuing development of financial markets in MONEYVAL countries provides new opportunities for criminals. This report seeks to provide guidance on securities instruments and the potential for abuse of the securities markets. Although the report has been prepared from information supplied primarily by supervisors, financial intelligence units and law enforcement agencies it can also be used as a guide for market participants

2. This report seeks to analyse the underlying vulnerabilities in the securities markets and highlight a number of methodologies which have been employed in laundering money through securities transactions. It also provides guidance on techniques to prevent and detect money laundering as well as giving a brief description of some of the main products that are traded in the securities markets.

3. The report has also highlighted the links between money laundering on the securities market and other criminal activities (e.g. tax evasion, fraud, corruption, market manipulation and insider trading) as well as non-criminal activities (e.g. capital flight, transfer pricing etc).

4. The report is divided into a number of sections:

   - **Section 1** "**Problem overview"** This section highlights the main vulnerabilities of the securities market to money laundering and the features that make it attractive for the laundering of illicit funds. There is also an overview of the wholesale and retail securities sectors together with an analysis of the money laundering risks in these sectors. It is noted that the areas most vulnerable to money laundering were wholesale markets, unregulated funds, wealth management, investment funds, bearer securities and bills of exchange.

   - **Section 2 "Current situation in MONEYVAL countries"** This section provides statistics on securities markets received from countries participating in the survey. Most of markets are developing with a significant volume of the over-the-counter transactions. This is a further factor which increases the vulnerability of securities markets to money laundering risks and also requires that FIUs, law enforcement and supervisory agencies develop an understanding of the main product features and underlying trading techniques. This section indicates that although securities markets are at varying stages of development countries are introducing sanctions and penalties which act as a deterrent to money laundering and market abuse.

   - **Section 3 "Information exchange"** This section is devoted to the interaction between financial intelligence units, regulatory bodies, security market participants and other state agencies. The main conclusion is that government agencies have access to sufficient information and expertise to combat frauds and money laundering on the securities market. It is, however, noted that this information, expertise and competency are frequently distributed among different agencies. This problem can be solved by establishing an interagency workgroup to which facilitates the sharing of information with a view to combating the misuse of securities markets and by providing law enforcement agencies and FIUs with access to securities specialists. This can be achieved either through the creation of specialist units and training of dedicated specialists or by the temporary transfer or secondment of market professionals to state agencies.

   - **Section 4 "Money laundering schemes and methodologies"** This section sets out various methodologies that have been utilised to launder money through securities transactions and gives examples of both typical schemes and case studies. Although certain retail investments may be used for layering purposes, it is noted that the securities market is also vulnerable to the layering and integration stages of money laundering due to the speed with which transactions can be executed and settled and the international nature of the market.

- **Section 5 “Criminal activity linked to money laundering”** This section considers some of the underlying criminal offences linked to money laundering on the securities market. It is noted that money laundering is frequently an integral part of complex frauds, tax evasion, corruption and other crimes. In the most serious cases organised crime can use the securities market to provide “complex services” for criminals.

- **Section 6 “Red flags and indicators”** This section sets out various red flags and indicators of money laundering which have been drawn from a number of sources. Many of these indicators may be found at various stages of the trading cycle. It is noted that many of these indicators may also be identified within other sectors of the financial sector including banking and insurance.

- **Section 7 "Financial analysis and investigation techniques"** This section provides guidance on analysis and investigation techniques. It is noted that investigations on securities markets frequently require large amounts of transaction data and therefore, the use of specialised software for the detection and investigation of offences. The role of inter-agency co-operation and expertise is crucial. This section also considers the fact that, in cases of abuse of the securities market, asset recovery may require special approaches such as the confiscation of an equal value of crime proceeds.

- **Annexes** The annexes provide background information on securities markets and the underlying systems and controls that should be utilised by securities market participants. This guidance enables this report to be used as an AML guide on securities markets by both market participants and state agencies.

PROBLEM OVERVIEW

1 SECURITIES MARKET VULNERABILITY

1. The process of money laundering involves a series of complex transactions designed to disguise the real origin of criminal assets. Criminal assets are converted from one asset to another through numerous and various financial transactions. Generally, money laundering transactions will be structured as legal transactions, although the origin of funds will stem from criminal activity. The criminals use various mechanisms and financial instruments for laundering, including securities.

2. The securities market is a potentially attractive mechanism for money laundering. This attraction stems from the variety and complexity of financial instruments available, the ease and speed of transaction execution (for example, on-line auction) and the ability to easily execute transactions across international boundaries.

3. Securities can be used in laundering schemes to "break the chain" of documented transactions, to disguise the signs of illegal transactions and to justify high profits. The use of securities in trade based laundering schemes, including "carousel schemes" followed by VAT fraud, requires special attention.

4. It is also noted that there is a problem involving manipulation of securities markets and the use of insider information. During recent years there have been a number of cases that involved large companies and securities market participants, sometimes as perpetrators, sometimes as victims of fraud.

5. The incidence of securities market manipulation and misuse of insider information have led international financial regulators to introduce strict conditions for the disclosure of information by companies, and restrictions on the use of non-public information. In 2003 the European Parliament and the Council of the European Union adopted Directive 2003/6/EC "On insider dealing and market manipulation", strengthening the requirement of disclosure of non-public information.

6. Investigators face the problem of large volumes of securities transactions coupled with the probability of "co-mingling" of legitimate transactions with those involving criminal assets. This problem requires the use of special methods of investigation.

7. The securities market has certain features that make it potentially vulnerable for money laundering:

    - Rapid transaction execution and settlement, substantial transaction values and the large volume of transactions makes the security market a perfect tool for layering;
    - The use of cash to purchase securities is possible although it is not typical;
    - Where a number of financial institutions are involved in a transaction CDD measures may be omitted due to reliance procedures conducted by the institution initiating the transaction;
    - Execution, settlement and delivery of transactions may be done separately;
    - The possibility of co-mingling of 'clean' and 'dirty' funds;
    - Insider transactions/manipulation of the security market and predicate offence are interconnected;
    - The rapid development and regular emergence of complex new products, particularly in the wholesale markets;
    - The use of bearer securities and the ability to transform registered securities into bearer securities by attaching blank signed, transfer forms;
    - The ability to open internet-based trading accounts without face-to-face contact;
    - The ease and low cost of establishment of securities intermediaries.

2 MONEY LAUNDERING RISKS IN SECURITIES MARKETS

8. The wholesale securities market includes private equity, corporate finance, wholesale markets, name passing securities companies in inter-professional markets and unregulated funds. The retail securities market includes wealth management, financial advisers, non-life providers of investment fund products, discretionary and advisory investment management and execution-only securities companies.

9. The following section describes each of these areas of securities business and analyses the vulnerability to money laundering. This section is based on the work of the Joint Money Laundering Steering Group in the United Kingdom. The descriptions of each area are necessarily brief and are designed to provide an introduction to each area of the securities industry. In the event of an investigation being undertaken further research should be undertaken into the characteristics of the underlying products.

10. Some of the activities described may not be currently applicable to MONEYVAL countries at the present time. It is, however, noted that securities markets are dynamic and can develop rapidly as a result of borrower and investor demand as well as in reaction to the requirements of a developing economy. Furthermore, in a global economy, investors and borrowers may seek to utilise products in other countries if these are not available in their domestic market. It is therefore important that regulators and law enforcement agencies remain aware of the evolution their domestic securities markets and tends adopted by investors and borrowers and are alert to the potential for money laundering posed by newly developed securities products.

2.1 Wholesale Securities Markets

2.1.1 Private equity

a) Overview of private equity

11. Private equity business (for the purposes of this guidance) means activities relating to:

    - The raising and acceptance of moneys into private equity funds (usually from institutional investors);
    - The investing of these funds by providing long term finance to a range of businesses, from early stage to large established companies. Usually the investee companies are unquoted;
    - The management of these investments (often involving active board participation) and exercise of negotiated equity holder rights; and
    - The subsequent realisation of the investment.

12. Investors in private equity funds tend to have long established relationships with the private equity firm, normally resulting in a very well known investor base. Prior to making any investment in a business, the private equity firm will conduct extensive due diligence on the business identifying areas of risk, including money laundering considerations. Such due diligence will include a thorough investigation into the senior management of the company concerned as well as any participating shareholders or other controllers.

13. Once invested, ongoing monitoring of the investment through active board participation and regular involvement allows the firm to assess whether the investee's activities are consistent with the financial performance of the company, and also enables the firm to observe the conduct of the key managers of the business at first hand.

14. For AML/CFT purposes, in a private equity context there are two distinct groups:

    - Investors in fund vehicles operated, managed or administered by private equity firms – (investors);
    - Persons involved with the private equity firm when investing and divesting (e.g., investee companies when investing and purchasers on exit) – (transactions).

b) Money laundering risks in private equity

Investors

(i) Product risk

15. Investors typically invest in a fund as limited partners in a limited partnership. The limited partnership will usually be collectively managed or advised by the private equity firm. Investors invest for the long term and the timing of any return of capital is unpredictable. This form of investment is very illiquid, with no ready market. Transfers of interest in the partnerships can take place, but only after strict due diligence (and in some funds only after a minimum initial investment period) and usually only with the specific approval of the general partner or manager. Payments/repayments would also only tend to be made to the investor itself (any payment to a third party would usually only be made with the express consent of the general partner and/or manager of the fund). Furthermore, extensive due diligence would normally be undertaken before any investment is made.

(ii) Customer risk

16. Investors in a fund are mostly institutional, such as insurance companies, pension funds of large corporates or state organisations, other financial companies and some funds of funds. There may also be a small number of high net worth individuals.

17. The acceptance of investors into a fund is a relatively long process with significant levels of due diligence performed by the firm and the prospective investor(s). Key representatives of the investors will often meet face to face with senior executives of the firm.

18. The relationship between the firm and investor is such that a high proportion of investors will often commit to consecutive funds of the firm; thus the relationship continues over a long period and source of funding remains constant.

19. For the reasons set out above, these investors would generally be considered to be low risk, although certain high net worth individuals may require extra consideration in any risk evaluation.

20. Firms seeking to raise funds for the first time, or from a significantly larger investor base, may be under pressure to accept funds from potentially higher risk investors, and the extent of the due diligence should be adapted accordingly.

Transactions

(i) Product risk

21. The product is the provision of funds by the firm in a number of different structures predominantly to unquoted companies. The funding is usually provided for the long term, after the company and its management have been subject to detailed due diligence and investigation. The firm has an ongoing obligation to monitor its investment, often involving representation on the board of the company and receipt of regular financial and operational information.

22. The shareholding is highly visible and any failings on the part of the company would be closely aligned to the reputation of the private equity firm.

23. If all these factors are present it is considered unlikely the provision of funding will be used for illegal purposes and that therefore the product will be a lower risk. The absence of one of these factors, such as the non availability of detailed due diligence work or the reliance on a third party, may require the firm to obtain more detailed verification to satisfy itself that the funds are being provided for legitimate purposes.

(ii) Customer risk

24. There are a number of parties involved in a private equity transaction, and the level of identification required in respect of each will vary.

Investee company (company into which funds are being paid) and its directors

25. This company will either has been the subject of extensive due diligence, or will be an "off the shelf" vehicle, especially established by the firm for the purpose of acquiring the investee company.

26. The jurisdiction of the vehicle may cause the risk profile of the investee company to increase, but provided that the company has been properly established and that the reason for the selection of jurisdiction is understood and appropriate, there should be no need to obtain additional verification.

27. Whilst the legal obligation relates to identifying the investee company into which funds are being paid, where that vehicle is itself undertaking a linked transaction there must be a clear understanding of the ultimate recipient of the funds and the flow of financing, particularly with the increasing complexity of deal structures.

Relevant Co-investor

28. Where the firm acts as lead investor in the round of financing where it has arranged co-investors' involvement in the deal, and where the co-investors are relying on the firm, it must identify the co-investors.

29. Following the firm's assessment of the overall risk presented by those co-investors, it may decide to verify their identity.

30. The identification requirements exist not only at the initial investment stage but also at any follow-on financing, to the extent that any new relevant co-investors are taking part. The firm should understand the business of a new co-investor and the reasons for it wanting to invest, particularly when the target of the financing is not performing well.

Purchaser on exit

31. The realisation of a private equity transaction will typically be made either by means of a listing, to a trade buyer, to existing management or to another private equity fund. If the sale is to a member of existing management who has been known to the private equity firm in the context of the investment concerned (or of another investment), the firm should consider the relevance of any verification given its existing relationship with, and knowledge about, the management.

32. The pressures of achieving a successful exit may heighten the risk of limiting the amount of due diligence performed on any potential purchaser on exit. In these circumstances the firm needs to ensure that its controls for proper verification of identity and source of funding remain robust. Where the purchaser is a private equity fund, consideration should be given to a risk-based approach of the kind described in relation to fund of fund investors into a private equity fund. This will often be appropriate.

(iii) Market risk

33. The range of companies invested in is determined by the stated parameters of the fund as agreed with the investors and the level of regulation and standard of controls in which each operates will vary enormously. The strength of the firm's due diligence process serves to identify where any risk exists within the investee companies and the firm should develop its AML/CTF approach accordingly.

34. Providing funding to a company which operates across a number of unregulated territories, even if the parent is incorporated or registered in a well-regulated territory, may be a higher risk than an equivalent business which operates out of one well-regulated territory, and appropriate levels of verification should be considered.

35. An assessment may be required as to whether the type of business being invested in is likely to be a target for money launderers, and the approach to due diligence adapted accordingly. Businesses which involve high volumes of cash or near cash transactions, for example, casinos, hotels, are likely to be at greater risk than, for example, an early stage biotech company.

2.1.2 Corporate finance

a) Overview of corporate finance

36. "Corporate finance" is activity relating to:

- The issue of securities. These activities might be conducted with an issuer in respect to itself, or with a holder or owner of securities. Examples include: arranging an initial public offering (IPO), a sale of new shares, or a rights issue for a company, as well as making arrangements with owners of securities concerning the repurchase, exchange or redemption of those securities;

- The financing, structuring and management of a body corporate, partnership or other organisation. Examples include: advice about the restructuring of a business and its management, and advising on, or facilitating, financing operations including securitisations;

- Changes in the ownership of a business. Examples include: advising on mergers and takeovers, or working with a company to find a strategic investor;

- Business carried on by a firm for its own account where that business arises in the course of activities covered by (a), (b) or (c) above, including cases where the firm itself becomes a strategic investor in an enterprise.

b) Money laundering risks in corporate finance

37. As with any financial service activity, corporate finance business can be used to launder money.

38. The money laundering activity through corporate finance will not usually involve the placement stage of money laundering, as the transaction will involve funds or assets already within the financial system. However, corporate finance could be involved in the layering or integration stages of money laundering. It could also involve the concealment, use and possession of criminal property and may used to design securities transactions designed to disguise the source or destination of criminal funds.

Securitisation transactions

39. Securitisation is the process of creating new financial instruments by pooling and combining existing financial assets, which are then marketed to investors. A firm may be involved in these transactions in one of three main ways in the context of corporate finance business:

a) as advisor and facilitator in relation to a customer securitising assets such as cash flow receivable in the future. The firm will be responsible for advising the customer about the transaction and for setting up the special purpose vehicle (SPV), which will issue the asset-backed instruments. The firm may also be a counterparty to the SPV in any transactions subsequently undertaken by the SPV;
b) as the owner of assets which it wants to securitise;
c) as counterparty to an SPV established by another firm for its own customer or for itself - that is, solely as a counterparty in a transaction originated by an unconnected party.

40. Securitisation transactions can be utilised to disguise the source of funds and to create financial instruments that facilitate the transfer of property or assets.

2.1.3 Wholesale markets

a) Overview of wholesale markets

41. The wholesale markets comprise exchanges and dealing arrangements that facilitate the trading (buying and selling) of wholesale investment products, and hedging instruments ("traded products"), including, but not limited to:

- Securities: equities, fixed income, warrants and investment funds (Exchange Traded Funds – ETFs);
- Money market instruments: foreign exchange, interest rate products, term deposits;
- Financial derivatives: options, futures, swaps and warrants;
- Commodities: physical commodities and commodity derivatives, including exotic derivatives (e.g., weather derivatives); and
- Structured products (e.g., equity linked notes).

42. Traded products confer 'rights' or 'obligations'; either between an investor and the issuer, or between parties engaged in the trading of the instruments. Traded product instruments can be bought, sold, borrowed or lent; as such, they facilitate the transfer of property or assets and usually represent an intrinsic value, which may be attractive to money launderers. Traded products can be bought or sold either on an exchange ("exchange traded products"), or between parties 'over-the-counter' (OTC).

43. Some traded products or instruments, such as equities, are issued in a 'primary' market, and are traded in a 'secondary' market, allowing investors in the primary market to realise their investment. Other traded products are created to enable investors to manage assets and liabilities, exchange risks and exposure to particular assets, commodities or securities.

Exchange-traded products

44. Exchange-traded products are financial products that are traded on exchanges, which have standardised terms (e.g. amounts, delivery dates and terms) and settlement procedures and transparent pricing. Firms may deal in exchange-traded products as principal or as agent for their customers. In the financial and commodity derivatives markets, firms will typically deal as principal, and on certain exchanges may only do so when dealing as a clearing member in relation to their customers' transactions. In the securities markets, firms can deal as either principal (for their own account) or as agent for the firms' underlying customers.

OTC products

45. OTC products are bilateral agreements between two parties, or multilateral, depending on the settlement process, that are not traded or executed on an exchange. The terms of the agreement are tailored to meet the needs of the parties, i.e. there are not necessarily standardised terms, contract sizes or delivery dates. Where firms deal OTC, they usually deal as principal. Some OTC dealing is

facilitated by securities companies and while settlement is normally effected directly between the parties, it is becoming increasingly common for exchanges and clearing houses to provide OTC clearing facilities.

b) Wholesale market sub-sectors

46. The products set out above are, largely, securities focused, but equally apply across the wholesale markets. The following sections look at particular products associated with other sub-sectors within the wholesale markets.

Foreign exchange

47. To the extent that firms dealing in foreign exchange (FX) in the wholesale market tend to be regulated financial institutions and large corporates, the money laundering risk may be viewed as generally lower. However, this risk may be increased by the nature of the customer, or where, for example:

    - high risk clients (including PEPs) undertake speculative trading; and/or
    - requests are made for payments to be made to third parties: for example, customers, particularly corporates, that need to make FX payments to suppliers and overseas affiliates.

48. FX (as well as many other traded products) is commonly traded on electronic trading systems. Such systems may be set up by securities companies or independent providers. When a firm executes a transaction on these systems the counterparty's identity is not usually known until the transaction is executed. The counterparty could be any one of the members who have signed up to the system. Firms should examine the admission policy of the platform before signing up to the system to ensure, that the platform only admits regulated financial institutions as members, or that the rules of the electronic trading system mean that all members are subject to satisfactory AML checks.

Financial derivatives

49. Financial products are utilised for a wide range of reasons, and market participants can be located anywhere within the world; firms will need to consider these issues when developing an appropriate risk-based approach. The nature, volume and frequency of trading, and whether these make sense in the context of the customer's and firm's corporate and financial status, will be key relevant factors that a firm will need to consider when developing an appropriate approach.

Structured products

50. Structured products are financial instruments specifically constructed to suit the needs of a particular customer or a group of customers. They are generally more complex than securities and are traded predominantly OTC, although some structured notes are also listed on exchanges (usually the Luxembourg or Irish Stock Exchanges).

51. There is a wide range of users of structured products. Typically they will include:

    - Corporates,
    - Private banks,
    - Government agencies,
    - Financial institutions

52. Transactions are normally undertaken on a principal basis between the provider (normally a financial institution) and the customer. Some structured products are also sold through banks and third party distributors.

53. Because of the sometimes complex pricing structures of the products, they may generally be more difficult to value than cash securities. The lack of transparency may make it easier for money launderers, for example, to disguise the true value of their investments.

54. The complexity of the structure can also obscure the actual cash flows in the transaction, enabling customers to carry out circular transactions.

55. The cash movements associated with structured products may present an increased money laundering risk, although this risk may be mitigated by the nature and status of the customer and the depth of the relationship the customer has with the firm. For example, if the use of structured products is part of a wider business relationship, and is compatible with other activity between the firm and the customer, the risk may be reduced.

c) Money laundering risks in wholesale market

56. Traded products are usually traded on regulated markets, or between regulated parties, or with regulated parties involved acting as agent or principal.

57. However, the characteristics of products that facilitate the rapid, and sometimes opaque, transfer of ownership, the ability to change the nature of an asset, and market mechanisms that potentially extend the audit trail, together with a diverse international customer base, have specific money laundering risks that need to be addressed and managed appropriately.

58. One of the most significant risks associated with the wholesale markets and traded products, is where a transaction involves payment in cash and/or third party payments.

59. Firms dealing in traded products in the wholesale markets are not as likely to be used in the placement stage of money laundering as, for example, deposit takers. That said, given the global flows of funds in the wholesale financial markets, it is important to recognise that although customers may remit funds from credit institutions, a firm could still be targeted with respect to the layering and integration stages of money laundering. Traded products might, for example, be used as a means of changing assets rapidly into different form, possibly using multiple securities companies to disguise total wealth and ultimate origin of the funds or assets, or as savings and investment vehicles for money launderers and other criminals.

60. Firms dealing in traded products in the wholesale markets do not generally accept cash deposits or provide personal accounts that facilitate money transmission and/or third party funding that is not related to specific underlying investment transactions. In the money markets, however, customers may request payments to third parties (e.g., FX payments to suppliers). There may also be third party funding of the transactions in the commodities markets. Also, where a bank is lending funds to a customer to purchase a physical commodity, and the customer hedges the risks associated with the transaction in the derivatives market through a securities company, the bank may guarantee the payment of margin to that securities company; this results in a flow of money between the securities company and bank on the customer's behalf.

61. The extent to which certain products are subject to margin or option premium payment arrangements will affect the level of risk. The nature and form of any margin will need to be taken into account by the firm when identifying the customer and determining appropriate payment procedures.

62. OTC and exchange-based trading can also present very different money laundering risk profiles. Most exchanges are regulated, transparent, and cleared by a central counterparty, and thus can largely be seen as carrying a lower generic money laundering risk. OTC business may, generally, be less well regulated and it is not possible to make the same generalisations concerning the money laundering risk as with exchange-traded products. When dealing in the OTC markets firms will, therefore, need to take a more considered, and undertake more detailed assessment.

63. For example, exchanges often impose specific requirements on position transfers, which have the effect of reducing the level of money laundering risk. Exchanges also monitor prices of exchange

traded securities and will frequently investigate pricing anomalies. These procedures will not apply in the OTC markets, where firms will need to consider the approach they would adopt in relation to any such requests in respect of customers dealing OTC.

2.1.4 Name-passing securities companies in inter-professional markets

a) Overview of Name-passing securities companies in inter-professional markets

64. In the inter-professional markets, wholesale market securities companies pass the names of customers from one principal to another, either by the traditional voice broking method or via an electronic platform owned by the securities company. The securities company passing the names takes no part in any transaction or trade between the two counterparties.

65. The activity enables the securities company to use this wide range of contacts across the wholesale markets to provide liquidity to the market, by putting in touch principals with a wish to transact, but who may not have the securities company's depth of information about willing counterparties. The use of a securities company also allows pre-trade anonymity for those counterparties who do not wish their position to be made known to the wider market.

66. In principle, transactions of all types may take place between any of these parties. There is no difference in how the name-passing takes place, although there is an awareness that standards of regulation and corporate governance will vary across jurisdictions.

b) Money laundering risks in name-passing

67. Across all wholesale markets, the vast majority of participants are known to the other market counterparties. Many participants are subject to financial regulation, and most corporates who are dealt with are listed, and subject to public accountability. In principle, therefore, the money laundering risk in name-passing is very low. The risk associated with name-passing relates to the resultant transactions and business relationships, which are covered by other parts of the sectoral guidance.

2.1.5 Unregulated funds

a) Overview of unregulated funds

68. An unregulated fund is a vehicle established to hold and manage investments and assets, which is not subject to regulatory oversight. The fund usually has a stated purpose and/or set of investment objectives. Unregulated funds will normally be a separate legal entity, formed as limited companies, limited partnerships and trusts (or the equivalent in civil law jurisdictions).

69. Unregulated funds are stand-alone entities in order that the assets and liabilities may be restricted to the fund itself. Sub-funds typically take the form of different classes of shares, fund allocations to separately incorporated trading vehicles or legally ring-fenced portfolios.

70. Unregulated funds may also operate as a "master/feeder" arrangement, whereby investors, perhaps from different tax jurisdictions, invest via separate feeder funds that hold shares only in the master fund. Feeder funds may also on occasion invest/deal directly, and therefore a firm may act for a fund acting in its own right whilst also at the same time being a feeder fund.

71. Dependent upon structure, an unregulated fund is controlled by its directors, partners or trustees. However, in most instances the powers of the directors, partners or trustees will be delegated to the investment manager. It is not unusual to find that the key personnel of a fund are also the key personnel of the investment manager.

b) Money laundering risks associated with unregulated funds

72. Unregulated funds are perceived as attractive vehicles for money launderers. There are seven primary factors giving rise to this perception:

    - The identity of those who invest into the unregulated funds will, in most cases, not be known to the firm providing services to the unregulated fund;
    - The unregulated status of the fund implies that it may be more difficult to ensure that the AML requirements applied to investors are of the appropriate standard;
    - An unregulated fund can have complex structures and consequently may appear to lack transparency of ownership and control;
    - A fund offers a private agreement between investors and the fund, and has traditionally been subjected to limited, or no, regulatory oversight or control;
    - Money flows in and out of an unregulated fund in the form of new subscriptions and redemptions of investors' interests (subject to the fund's subscription and redemption terms) and the bank accounts of the fund may be held offshore, sometimes in jurisdictions with banking secrecy;
    - The volume and size of unregulated fund trading activity and the complexity of underlying trading strategies; and
    - The fund may accept nominee investments.

73. The level of risk actually posed by the unregulated fund will depend upon the nature of the fund and its transparency. The risks can be determined through undertaking appropriate customer due diligence, and in particular through understanding to whom the fund is marketed and its structure and objectives, as well as the track record and reputation/standing of the investment manager and/or other relevant parties in control of the fund.

74. The status and reputation of other service providers, such as executing, clearing or prime brokers and the administrator, may also be a factor in determining the risks associated with an unregulated fund.

75. Where a firm agrees to undertake third party payments on behalf of an unregulated fund, the risk of money laundering and fraud is increased.

2.2 Retail Securities Markets

2.2.1 Wealth management

a) Overview of wealth management

76. Wealth management is the provision of banking and investment services in a closely managed relationship to high net worth clients who may be based in another country or may regularly travel between a number of countries. Such services will include bespoke product features tailored to a client's particular needs and may be provided from a wide range of facilities available to the client including:

- current account banking
- high value transactions
- use of sophisticated products
- non-standard investment solutions
- business conducted across different jurisdictions
- off-shore and overseas companies, trusts or personal investment vehicles

b) Money laundering risks in wealth management

77. Money launderers are attracted by the availability of complex products and services that operate internationally within a reputable and secure wealth management environment that is familiar with high value transactions. The following factors contribute to the increased vulnerability of wealth management:

- **Wealthy and powerful clients** – Such clients may be reluctant or unwilling to provide adequate documents, details and explanations. The situation is exacerbated where the client enjoys a high public profile, and where they wield political or economic power or influence.
- **Multiple and complex accounts** – Clients often have many accounts in more than one jurisdiction, either within the same firm or group, or with different firms.
- **Cultures of confidentiality** – Wealth management clients often seek reassurance that their need for confidential business will be conducted discreetly.
- **Concealment** – The misuse of services such as offshore trusts and the availability of structures such as shell companies helps to maintain an element of secrecy about beneficial ownership of funds.
- **Countries with statutory banking secrecy** – There is a culture of secrecy in certain jurisdictions, supported by local legislation, in which wealth management is available.
- **Movement of funds** – The transmission of funds and other assets by private clients often involve high value transactions, requiring rapid transfers to be made across accounts in different countries and regions of the world.
- **The use of concentration accounts** – i.e. multi-client pooled/omnibus type accounts - used to collect together funds from a variety of sources for onward transmission is seen as a potential major risk.
- **Credit** – The extension of credit to clients who use their assets as collateral also poses a money laundering risk unless the lender is satisfied that the origin and source of the underlying asset is legitimate.
- Commercial activity conducted through a personal account so as to deceive the banker.

Secured loans

78. Secured loans, where collateral is held in one jurisdiction and the loan is made from another, are common in wealth management. Such arrangements serve a legitimate business function and make possible certain transactions which may otherwise be unacceptable due to credit risk. Collateralised loans raise different legal issues depending on the jurisdiction of the loan. Foremost among these

issues are the propriety and implications of guarantees from third parties (whose identity may not always be revealed) and other undisclosed security arrangements.

Relationship management

79. The role of the relationship manager is particularly important to the firm in managing and controlling the money laundering or terrorist financing risks it faces. Relationship managers develop strong personal relationships with their clients, which can facilitate the collection of the necessary information to know the client's business, including knowledge of the source(s) of the client's wealth. Relationship managers must, however, at all times be alert to the risk of becoming too close to the client and to guard against the risks from:

- a false sense of security
- conflicts of interest – including the temptation to put the client's interests above that of the firm
- undue influence by others

Cash transactions

80. Cash transactions may sometimes be required as part of a comprehensive wealth management service. In these circumstances, a client should be required to deposit or withdraw cash at the counter of a recognised bank that is at least subject to local supervision. In extremely rare circumstances where this is not possible, there should be a documented policy and procedures in relation to the handling of cash by relationship managers.

2.2.2 Financial advisers

a) Overview of financial advisers

81. Financial advisers give customers advice on their investment needs (typically for long-term savings and pension provision) and selecting the appropriate products.

Typical customers

82. The typical customers of financial advisers are personal clients (including high net worth individuals), trusts, charities and companies.

b) Money laundering risks of financial advisers

83. The vast majority of financial advice business is conducted on a face-to-face basis, and investors generally have easy access to the funds involved.

84. Some criminals may seek to use financial advisers either as the first step in integrating their criminal property into the financial system or by seeking assistance in designing complex transactions to disguise the source or destination of funds.

85. The offences of money laundering or terrorist financing include aiding and abetting those trying to carry out these primary offences, which include tax evasion. This is the main risk generally faced by financial advisers. In carrying out its assessment of the risk the firm faces of becoming involved in money laundering or entering into an arrangement to launder criminal property, the firm must consider the risk related to the product, as well as the risk related to the client.

86. Clearly, the risk of being involved in money laundering will increase when dealing with certain types of customer, such as offshore trusts/companies, politically exposed persons and customers from higher risk non-FATF countries or jurisdictions, and may also be affected by other service features

that a firm offers to its customers. Customer activity, too, such as purchases in secondary markets – for example, traded endowments – can carry a higher money laundering risk.

2.2.3 Non-life providers of investment fund products

a) Overview of investment fund products

87. The guidance contained within this section is directed at firms offering the following types of investment vehicle:

- **Retail investment funds** - authorised unit trusts and open-ended investment companies (oeics).

- **Other investment fund-based products/services** - which may comprise one, or a combination of, regular savings schemes (including those relating to investment trusts), regular withdrawal schemes, personal pension schemes and fund supermarkets/wrap platforms.
  Typical investors using retail funds and associated products/services vary depending upon the product, but include private individuals, regulated firms investing as principal (e.g. life companies); other regulated firms (including nominee company subsidiaries) acting on behalf of underlying customers, other corporates, personal and corporate pension schemes, charities and other trusts.

- **Institutional funds** - authorised and unauthorised collective investment schemes and unitised life assurance funds that are dedicated to investment by institutional investors.

b) Money laundering risks in investment fund products

Retail funds and products/services

88. The vast majority of investment fund business is conducted on a non-face-to-face basis (post, telephone, internet, etc.) and investors generally have easy access to the funds involved. In addition, some firms accept payment by debit card, which exposes them to the risk of card fraud.

89. In some cases units in investment funds can be purchased for cash either as part of a regular savings scheme or in one-off transactions. As some jurisdictions require a "cooling-off" period whereby a customer can cancel his investment with a full refund procedures should be in place to ensure that this provision is not exploited for money laundering purposes.

90. However, there are also factors that limit the attractiveness of these products for any money laundering process, which therefore mitigate some of these risks. In particular, in order to mitigate the money laundering risk, firms invariably take steps to identify any third party subscribers or payees, and some firms refuse to accept or make third party payments. Furthermore, most retail investors use these products for medium and long-term savings, which makes short-term investment or high turnover unusual and often relatively straightforward to monitor.

91. Investors are rarely asked to provide additional customer information about the purpose of the relationship, which will be self-evident, or their background. However, their behaviour is better measured against that of other investors than against uncorroborated customer data, which any criminal could provide in support of their expected activity.

92. Holdings of investment fund units may be transferred freely between different parties. Such transfers will be recorded by the registrar of the fund (usually the product provider or a third party administrator acting on their behalf). Investment funds may also be deposited with a credit institution as collateral for a loan.

93. It is accepted that those who are able to provide convincing evidence of identity and behave in the same way as other investors will be very difficult to detect, in the absence of any other information to cause the firm to have doubts about the customer. Nevertheless, whilst investment fund products may generally be unattractive vehicles for the money laundering process, firms must be alert to the fact that career criminals will almost certainly invest in their sector using the proceeds of crime, and should consider any unusual activity in that light.

Institutional funds

94. As with retail funds, investors are rarely asked to provide additional customer information. However, in many cases the investment will be made on behalf of a client by the firm itself, another group company or another regulated firm, who will have obtained such information in the context of their role as an investment manager.

95. Overall, many institutional funds may be considered to be of lower risk than their retail counterparts, albeit by virtue of the restricted types of investor, rather than the product features. The risk will increase, however, in the case of "non-exempt" funds or share classes.

2.2.4 Discretionary and advisory investment management

a) Overview of discretionary and advisory investment management

96. *Investment management* includes both discretionary and advisory management of segregated portfolios of assets (securities, derivatives, cash, property etc.) for the firm's customers.

97. Discretionary managers are given powers to decide upon selection of securities and to undertake transactions within the portfolio as necessary, according to an investment mandate agreed between the firm and the customer.

98. Advisory relationships differ, in that, having determined the appropriate selection of securities, the manager has no power to deal without the customer's authority - in some cases the customer will execute their own transactions in light of the manager's advice. This should not be confused with "financial advice", which involves advising customers on their investment needs (typically for long-term savings and pension provision) and selecting the appropriate products.

99. The activities referred to above may be carried out for private or institutional investors.

b) Money laundering risks in investment management

100. In terms of money laundering risk, there is little difference between discretionary and advisory investment management. In both cases, the firm may itself physically handle incoming or outgoing funds, or it may be done entirely by the client's custodian.

101. In either case, the typical firm deals with low volumes of high value customers, for which there is likely to be a take-on process that involves a level of understanding of the customer's circumstances, needs and priorities and anticipated inflows and outflows of funds, in order to determine suitable investment parameters.

102. There is likely to be ongoing contact, often face-to-face, with the customer in order to review market developments and performance, and review the customer's circumstances, etc. Unexpected inflows/outflows of funds are not common occurrences - ad hoc requirements and movements are usually the subject of discussion between the firm and the customer.

103. In most cases, all money and other assets within the portfolio are held under the control of a regulated custodian, with money paid to or from the customer through their local bank account. Investment management is not a mechanism for the movement of assets from one person to

another, although some third party payments may be made (e.g. in the case of private customers, for the payment of school fees).

104. The risk of money laundering to the investment management sector, in the context of the "typical" circumstances described above, would be low. Clearly, however, the risk will increase when dealing with certain types of customer, such as offshore trusts/companies, PEPs and customers from higher risk non-FATF jurisdictions, and may also be affected by other service features that a firm offers to its customers. Likewise, some criminals may seek to use financial advisers either as the first step in integrating their criminal property into the financial system or by seeking assistance in designing complex transactions to disguise the source or destination of funds.

2.2.5 Execution-only securities companies

a) Overview of execution-only securities companies

105. *Execution-only (ExO) securities companies* carry out transactions in securities with regulated market counterparties, as agent for individual customers. ExO transactions are carried out only on the instructions of the customer.

b) Money laundering risks in execution-only securities broking

106. Some ExO securities companies deal with high volumes of low value customers, whereas others direct their services towards higher net worth customers, and thus have fewer customers. Securities broking customers may adopt a variety of trading patterns; the firm is offering no advice and may have little or no knowledge of a particular customer's motives.

107. ExO customers are also free to spread their activities across a variety of securities companies for perfectly valid reasons, and often do. Each securities company may therefore actually have little in terms of transaction history from which to identify unusual behaviour. Many firms provide ExO securities broking services on a non-face-to-face basis, including via the internet.

108. In view of the above, whilst securities broking might be regarded as being of *lower* risk compared to many financial products and services, the risk is not as low as in providing investment management services to the same types of customer from similar jurisdictions.

109. The risk of money laundering arises from settlement in cash or from unusual trading or settlement patterns. Firms should seek to design systems to identify unusual dealing and settlement patterns.

2.2.6 Bearer securities

a) Overview of bearer securities

110. Bearer securities available in certain jurisdictions represent a particularly useful instrument in the setting up of international money laundering schemes.

111. Securities instruments in bearer form consist of bearer bonds and bearer security certificates or “bearer shares”. As with registered securities, both of these instruments are issued by a particular corporate entity in order to raise capital. The difference between registered securities and securities in bearer form, among other things, is the method of transfer. In the case of registered securities, the instrument is issued to a particular individual, and the “owner” is recorded in a register maintained by the issuing entity. In the case of securities in bearer form, the instrument is issued; however, the owner is not recorded in a register. When registered securities are transferred to a new owner, the new owner must be recorded in order for the transfer to be valid. When bearer securities are transferred, since there is no register of owners, the transfer takes place by the physical handing over of the bond or share certificate.

112. Where registered securities are not in dematerialised form, transfer of title is normally effected by lodging with the registrar the securities together with a share transfer form, signed by the registered owner and purchaser, whereby a new share certificate, registered in the name of the new owner, will be issued. It is noted however, that where a share transfer is merely signed by the registered owner, but not by the new purchaser, this has the effect of transforming the registered share into a bearer share.

113. A number of countries have phased out the use of bearer shares and no longer permit corporate entities operating in their territories to issue such instruments. Nevertheless, as has been noted above, unless full dematerialisation of share certificates is introduced, blank share transfer can effectively transform registered shares into bearer shares.

114. Certain jurisdictions have rules that require ownership of a company to be declared when specified threshold percentages of ownership are reached, and some require bearer shares to be deposited in custodial or safekeeping accounts at financial institutions where anti-money laundering rules on customer identification would normally apply.

b) Money Laundering risks of bearer securities

115. Share certificates, whether in registered or bearer form represent equity within a corporate entity, that is, they represent shareholdings or ownership of a particular corporate entity. The number of shares owned by a person determines the degree of control that such an individual may have over the legal entity that issued the shares. In the case of registered shares, determining ownership is relatively straightforward, as the record of ownership is maintained in the share register of the issuing entity. Determining the ownership of bearer shares, in contrast, is not so easy since it depends on who possesses or has physical control of the share certificates. The obstacles to determining easily the ownership of bearer shares (and thus the ultimate owner of the corporate entity that has issued such instruments) are a factor that has been exploited by launderers to conceal or disguise true ownership of entities used in some money laundering schemes.

116. Bearer bonds, according to one expert, have been observed as part of large-scale fraud operations, and the resulting schemes have been reported as suspected money laundering operations. Because of the nature of bearer bonds as debt instruments however, it is possible that their anonymous transferability represents the chief characteristic that could be exploited by launderers rather than an ability to conceal ownership.

117. When used in the context of money laundering operations, other types of financial instruments in bearer or negotiable form may also be misused. As observed above, bearer shares have been used to conceal ownership of corporate vehicles. It is suspected that bearer debt instruments can be used for concealing or disguising the true ownership of funds and for moving them easily without leaving traces that could be picked up by investigators.

2.2.7 Bills of exchange

a) Overview

118. Bills of exchange (including drafts and promissory notes) are popular instruments for investment in MONEYVAL member states. A bill of exchange is a written order by the *drawer* to the *drawee* to pay money to the *payee*. Bills of exchange are used primarily in international trade, and are written orders by one person to his bank to pay the bearer a specific sum on a specific date sometime in the future. Bills of Exchange can be payable at sight or at a future date, and if either accepted and/or guaranteed by a third party (normally a bank), represent a commitment by the accepting or guarantor to pay funds, thus making them the primary obligor.

119. By its nature the bill of exchange is a security, the physical holder of such bill has all legal rights unless the opposite is proven. A bill of exchange usually is transferred by making an endorsement.

Making the last endorsement 'blank' effectively gives the bill of exchange many features of a bearer security.

b) Money Laundering risks of bills of exchange

120. Bills of exchange can be used in the layering and integration stages of money laundering as the enormous volume of trade flows obscure individual transactions and the complexities associated with the use of multiple foreign exchange transactions and diverse trade financing arrangements permit the commingling of legitimate and illicit funds. Money laundering risks for bills of exchange are similar to ones for bearer securities. There is also a high risk of tax evasion related to the nature of bills of exchange and transactions may be considered as usual payment of trade debt (subject to VAT) as well as securities deals (no VAT). FATF conducted a detailed study of Trade-Based Money Laundering in 2006[4] .

121. A key risk around bills of exchange is that seemingly legitimate transactions and associated documents can be constructed simply to justify the movement of funds between parties, or to show a paper trail for non-existent or fraudulent goods. In particular the level and type of documentation received by a firm is dictated principally by the applicant or instructing party, and, because of the diversity of documentation, firms may not be expert in many types of the documents received as a result of such business. Such a risk is probably greatest where the parties to an underlying commercial trade transaction are in league to disguise the true nature of a transaction. In such instances, methods used by criminals to transfer funds illegally range from over and under invoicing, to the presentation of false documents or spurious calls under default instruments. In more complex situations, for example where asset securitisation is used, receivables can be generated from fictitious parties or fabricated transactions.

122. This duality (security / trade instrument) may mean that there is no regulation of the issuance and registration of bills of exchange and that there is no overall supervision over deals transactions. This makes detection of money laundering schemes with bills of exchange extremely difficult.

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[4] For further information see www.fatf-gafi.org/dataoecd/60/25/37038272.pdf

CURRENT SITUATION IN MONEYVAL MEMBER STATES

1 MARKET SIZE

123. Out of 19 countries participating in the survey, 11 have provided data on the annual turnover of securities. This amount varies from €5.7 mln (Armenia) to €175 bn (Poland).

Distribution of yearly value of deals

Average value of transactions per year	Countries
Less than €100 mln	2 countries (Armenia, Moldova)
€100mln - €1bn	4 countries (Azerbaijan, Latvia, Slovenia, "the former Yugoslav Republic of Macedonia".)
€1bn – €10bn	3 countries (Estonia, Lithuania, Malta)
€10bn – €100bn	1 country (Romania)
More than €100bn	1 country (Poland)

124. In most countries the most popular instruments are shares and bonds. However, in Poland and Romania a substantial volume of transactions in derivatives instruments was reported.

125. Only 4 countries have provided data on the relative size of the organised and over-the-counter market:

Size of over-the-counter market

Country	% of OTC deals
Armenia	55%
Azerbaijan	38%
Estonia	53%
Moldova	70%

2 REGULATORY FRAMEWORK

126. In most of the countries participating in the survey there are specific laws on security trading together with secondary legislation which has been developed by the supervisory agencies. The only exception is Azerbaijan where the securities market is regulated by Civil Code and secondary legislation.

127. In most of the countries participating in the survey the securities market is regulated by a specialised supervisory agency (securities commission, financial services agency etc.). The only exception is Azerbaijan where the securities markets are supervised by the Central Bank.

3 BEARER SECURITIES

128. There are various approaches to the question of bearer securities. The main approaches are set out in the following table:

Bearer securities	Countries
No limits	Azerbaijan, Bosnia and Herzegovina, Latvia, Montenegro, Poland and Slovenia
Other restrictions	Armenia materialised (not more than 100 items per issue), Cyprus(enhanced CDD)
Issue prohibited	Bulgaria, Lithuania, Malta, "the former Yugoslav Republic of Macedonia"

4 TRANSACTION REPORTING

129. In some the countries participating in the survey supervisors receive reports on all securities transactions (or all transactions above a nominated threshold). This enables supervisor to:

- monitor suspicious activities and detect possible market violations;
- maintain a database of transactions to support future investigations.

130. Supervisors in the countries with the largest markets (Poland, Romania, and Estonia) that have receive such data either utilise specially designed software for the monitoring of transactions or are in the process of developing it.

Securities deal archive

Country	All deals reported to	Software used
Armenia	Over predetermined threshold – to FIU	
Azerbaijan	Supervisor	
Bosnia and Herzegovina	Supervisor and FIU	
Bulgaria	Supervisor	Under development
Estonia	Supervisor	Under development
Lithuania	Supervisor (regulated market deals)	
Poland	Supervisor	Yes
Romania	Over predetermined threshold – to FIU and supervisor	Monitoring software
Slovenia	Clearing house	

5 COST OF ESTABLISHMENT OF A SECURITY TRADING COMPANY

131. In countries participating in the survey the cost of establishment of a security trading company are relatively low (compare to the establishment of a bank) – license costs range from €145 (Lithuania) up to €4500 (Poland); minimal capital requirements vary from €50 000 to €730 000 depending on the type of company.

6 SANCTIONS AND PENALTIES

132. In countries participating in the survey the responsibility for investigating and prosecuting violations of procedures and regulations concerning securities transactions is normally regulated by law. As a rule, in MONEYVAL member states, breaches of security market laws or regulations are subject to either civil or criminal penalties.

133. The administrative penalties are applied by the supervision authorities and range from warnings and fines to the withdrawal of license or a temporary prohibition of carrying out certain activities and services.

134. In some jurisdictions, the market supervision authority conducts the investigation in the initial stages and if there are indicators of crime (e.g. insider trading or market manipulation) the case is transferred to law enforcements agencies.

135. As a result, while administrative offences are easier to investigate and prosecute, due to the availability of experienced professionals in the supervision and control authority, penal criminal cases are more difficult to investigate by law enforcements professionals, who may not have such in-depth experience of securities markets. In this context, one of the most difficult things to proof in such a criminal case is the element of intent. A possible solution to this problem could be the appointment of specialised professionals to work within law enforcements agencies.

Examples of sanctions, applied by countries for breach of rules of regulating securities transactions:

Armenia. Sanctions include warnings, an administrative order for correcting violations, fines and suspension or revocation of the license.

Azerbaijan. Sanctions include suspension of license, liquidation of license, fines, restriction of operation, suspension of operations and reference to the court.

Bosnia and Herzegovina. The licenses of professional participants in conducting operations with securities (securities dealers, etc.) can be revoked by the Commissions for Securities for infringement of the rules of conduct on the capital markets.

Bulgaria. Sanctions include fines and confiscation of income resulting from the offending transaction[5].

Croatia. The Croatian Financial Services Agency can file administrative and criminal charges on authorised bodies, it can also require remedial action certain procedures and can issue public warnings to participants in the capital market.

Cyprus. Sanctions include administrative fines, withdrawal and/or suspension of an investment firm's license as well as criminal sanctions including imprisonment.[6]

[5] Sanctions for AML/CFT are imposed only by the Financial Intelligence Agency and the Financial Supervision Commission is obliged to submit to FIA information on its findings (as part of its general supervision). Sanctions were as follows:

- Investment intermediaries - Art. 11a LMML (reporting CTRs) – 1 sanction of 5000 BGN imposed 2005
- Securities exchange - Art. 16, Para. 1 LMML (lack of internal rules) sanction of 2000 BGN imposed 2004

[6] According to the Investment Firms Law of 2002-2005 which mainly implements the European Directive 93/22/EC:

- Administrative Fine of up to CY£600,000 depending on the nature of the violation of the Law.
- Withdrawal and/or suspension of an Investment Firm's license.

According to the Law on Insider Dealing and Market Manipulation (Market Abuse) of 2005, (Law 116):

Estonia. The Financial Services Authority has the power to impose administrative sanctions for infringements of the Securities Market Act. Market manipulation, insider dealing and violations of restrictions as set out in the law on investment of assets are criminal offences punishable by fines and in market manipulation and insider dealing cases by up to 3 years imprisonment.
Latvia. Sanctions include warnings, fines, withdrawal of license and criminal liability.
Lithuania. Sanctions include fines which may be linked to the value of the transaction[7].
Malta. Sanctions include fines and imprisonment[8].
Moldova. Sanctions include warnings, withdrawal of licenses and deferral of licenses. Cases involving criminal activity are referred to the law enforcement agencies.
Montenegro. In accordance with the law on securities and the regulations of the Commission for rules violation the following penalties are prescribed:
- suspension from trading of securities on the securities market;
- removal of securities from securities market quotation;
- temporary or permanent ban for the authorised participant on the securities market;
- temporary ban for carrying out certain authorised activities;
- temporary or permanent ban from managing securities portfolios;
- public sanction.

Poland. Sanctions include:
- exclusion of securities from trading on a regulated market;
- deletion of a securities company from the relevant list;
- revocation or limitation of a securities company license;
- deletion of an investment firm agent from the register;
- prohibiting the operation of a management company or its branch in the territory of the Republic of Poland;
- ordering an investment fund to amend its articles of association;
- imposition of fines.

Romania. Sanctions include administrative warning, fines, complementary sanctions, applied as the case may be, suspension of authorisation, withdrawal of authorisation and temporary prohibition from carrying out certain activities and services which are subject to the law.
Slovenia. Sanctions include orders to eliminate violations, temporary ban on the provision of services, withdrawal of authorisation, conditional withdrawal of authorisation, public admonition and fines[9].
"The former Yugoslav Republic of Macedonia". Sanctions include cancellation of transactions, temporary suspension from conducting business services, revocation of license and public reprimand.
Ukraine. Sanctions include admonition, suspension of securities circulation, suspension of bids on the securities exchange, in some cases - criminal sanctions are utilised[10].

- Administrative Fine of up to 500.000 CYP. - (appx. € 855.000) and, in case of a repeated violation, an administrative fine not exceeding 1.000.000 CYP. - (appx. € 1.710.000), depending on the gravity of the violation.
- A criminal offence punishable by imprisonment of up to 10 years or by a fine of up to 100.000 CYP. - (appx.€170.860), or by both of these penalties.

[7] For legal persons – in most cases fines up to 100 thousand LTL (approx. 40 thousand USD); in some cases – up to 500 thousand LTL (approx. 200 thousand USD); in case of market abuse (market manipulation and insider dealing) – up to 100 thousand LTL (approx. 40 thousand USD) if profit gained illegally does not exceed 100 thousand LTL, and up to double income gained illegally if it exceeds 100 thousand LTL. For natural persons – administrative fines up to 5000 LTL (approx. 2000 USD).
[8] Violation of the Investment Services Act, Chapter 370 – a fine of not more than Lm200,000 or four (4) years imprisonment or both such fine and imprisonment; violation of the Prevention of Financial Markets Abuse Act, Chapter 476 – a fine of not less than Lm1000 and not more than Lm400,000 or imprisonment of not more than seven (7) years or to both such fine and imprisonment; violation of the Securitisation Act, Chapter 484 - a person found guilty of an offence is liable to a fine of not more than Lm50,000.
[9] All fines may be between 523 USD and 15.705 USD for natural persons, and from 15.705 USD to 471.135 USD for legal persons.
[10] Articles 223, 224, 234 of the Criminal Code of Ukraine envisaged responsibility for violation of procedures related to emission and circulation of securities; manufacture, sale and use of counterfeit non-government securities.

136. One of the main methodologies for money laundering utilising securities is abuse of the securities market itself. In order to prevent and counteract such abuse, many of the countries responding to the survey have established criminal liabilities for market manipulation on the securities market. Furthermore, it is apparent that market manipulation and insider trading are regarded as predicate offences.

Examples[11]
Sanctions for market manipulations and insider trading include:

Malta: a fine of not less than Lm1,000 (approx €2,329) and not more than Lm400,000 (approx €930,000), or imprisonment of not more than seven (7) years, or both such fine and imprisonment;
Lithuania: fines up to 100,000 LTL (approx. US$40,000) if profit has been gained illegally and does not exceed 100,000 LTL, and up to double the income gained illegally if it exceeds 100,000 LTL or imprisonment up to 3 years;
Estonia, Ukraine: Fines or imprisonment up to 3 years;
Poland:
- for market manipulation. Anyone who engages the market manipulation is liable to a fine of up to PLN 5m. (approx. €1.5m.) or imprisonment for a period from three months to five years, or to both these penalties jointly. Anyone who engages in collusion with other persons for the purpose of market manipulation is liable to a fine of up to PLN 2m. (approx. €600,000.);
- for professional secrecy. Anyone who is bound by an obligation for professional secrecy and who discloses or uses information covered by such obligation in securities trading shall be liable to a fine of up to PLN 1m. (approx. €300,000.) or imprisonment for up to three years, or to both these penalties jointly;
- for insider dealing. Anyone who, in violation of the prohibition, discloses inside information shall be liable to a fine of up to PLN 2 mln. (approx. €600,000.) or a penalty of imprisonment for up to three years, or to both these penalties jointly. Anyone who, in violation of the prohibition uses inside information is liable to a fine of up to PLN 5 mln. (approx. €1.5m.) or imprisonment for a period from three months to five years, or to both these penalties jointly.

7 SECURITIES MARKET MANIPULATION AND INSIDER DEALING

137. Market manipulation concerns deliberate attempts to interfere with the free and fair operation of the securities market and create an artificial, false or misleading appearance with respect to the price of, or market for, a security. This is typically done either by spreading false or misleading information in order to influence others to trade in a particular way, or by using buying and selling orders deliberately to affect prices or turnover, in order to create an opportunity for profit. Insider dealing occurs where investors take advantage of non-public or confidential information in order to deal in shares for personal profit.

138. As a rule, the following types of market manipulation are observed on securities markets:

- **Pools.** Agreements, often written, among a group of traders to delegate authority to a single manager to trade in a specific securities for a specific period of time and then to share in the resulting profits or losses.
- **Churning.** When a trader places both buy and sell orders at about the same price. The increase in activity is intended to attract additional investors, and increase the price.
- **Runs.** When a group of traders create activity or rumours in order to drive the price of a security up. Recent examples are the alleged HBOS and Bear Stearns share-trading frauds in 2008. This activity is sometimes referred to as “painting the tape”.

[11] For more information about other European Union member countries, see the Report on Administrative Measures and Sanctions as well as the Criminal Sanctions available in Member States under the Market Abuse Directive: *The Committee of European Securities Regulators, 17.10.07,*
http://www.cesr.eu/index.php?page=document_details&id=4853

- **Ramping (the market).** Actions designed to artificially raise the market price of listed securities and to give the impression of voluminous trading, in order to make a quick profit.
- **Wash sale.** Selling and repurchasing the same or substantially the same security for the purpose of generating activity and increasing the price.
- **Bear Raid.** Attempting to push the price of securities down by heavy selling or short selling.

139. In many cases money laundering may be linked to fraud or other crimes committed on the securities market, including market manipulation and insider dealing and therefore may result in significant losses for legitimate investors.

140. There have been a number of significant cases involving market manipulation and insider dealing a selection of which are set out below.

Examples of market manipulation

United Kingdom
Journalist Mr H, used the City Slickers column in a newspaper (a mass circulation daily in the country concerned) to ramp shares in a scam that netted him nearly £41,000. For months he repeatedly purchased low-priced share issues, recommended them to readers and then quickly sold them as values soared. Mr H was subsequently sentenced to six months in jail.

Cyprus
Two businessmen registered an IT company abroad. Within a very short period the company was able to gain a listing on the local securities exchange. The owners of the company managed to drive the share price of the company upwards by presenting misleading annual reports and by reporting to the investors on forged or non existing contacts with major companies in the IT sector. The same businessmen were also involved in insider trading regarding the purchase and selling of their company's shares. The owners of the company managed to earn hundred of millions of USD through these activities. Profits from these activities were transferred mainly to the 2 off-shore countries. Several millions of USD were frozen both in these countries. The money was finally returned back to investors.

Examples of Insider Dealing

USA
Ms S, director of a stock exchange was imprisoned for lying about her well-timed sale of shares in a pharmaceutical company that she learned was about to receive a negative ruling from the Food and Drug Administration.

United Kingdom
Mr S, Mr M, Mrs S and Mr P were found guilty of conspiracy to commit "insider dealing".
Mr P worked as a proof reader for Company B. Amongst other things, Company B printed confidential documentation for takeover and merger transactions. As a proof reader, Mr P had access to confidential and price sensitive information. Sometimes, Company B would begin printing the documentation for takeover/merger transactions before these transactions had been announced to the public through the one of the European Securities Exchanges.
Mr P would provide inside information to his friend Mr M and/or Mrs S (the business partner of Mr M), one or other of who would pass that inside information on to Mr S (the estranged husband of Mrs S). Mr M, Mrs S and Mr S, or any one of them, would then deal in shares that were price affected by that inside information and in the knowledge that they were in receipt of inside information. Mr P was paid for the information he disclosed. Mr M, Mrs S and Mr S profited from dealing as insiders.
Some 27 takeover/merger transactions featured in the conspiracy. Over the period in question Mr M invested approximately £110,000 and made profits of about £36,000; Mrs S invested more than half a million pounds and made a profit of more than £100,000 and Mr S allegedly invested over £2 million and made a profit of approximately £200,000.

United Kingdom

A top investment banker was convicted for insider dealing.

Mr C, former head of securities trading at Company A, was given a 12-month suspended sentence and was fined £25,000 with £7,000 costs at the High Court.

The court heard that Mr's C crime began when he was working on the secret takeover of engineering Company B.

Mr C rang a colleague at the foreign branch of his former employer and instructed them to buy 60,000 Company B shares through a nominee company.

Trading began in City X with Company B shares valued at 239p. When the bid was announced 15 minutes later the shares had shot up to 265p. Mr C had made £15,000 profit in less than an hour.

His actions were uncovered by colleagues who traced the deal to the off-shore company that Mr C had formed several years earlier.

141. Market manipulation, insider trading and fraud are 'generic' crimes for securities markets, and proceeds are frequently laundered immediately through the same market. In many circumstances, it is often difficult to distinguish where the predicate offence ends and money laundering begins. This leads to the certain conclusions:

- analysis of suspicious activities on the securities market should consider not only pure money laundering but other frauds also;
- FIUs should have the capability to transfer information on suspicious transactions on securities markets not only to law enforcement, but to market supervisors as well.

INFORMATION EXCHANGE

1 EXCHANGE OF INFORMATION BETWEEN MARKET PARTICIPANTS AND STATE AGENCIES

142. Market participants are usually required to submit information about securities transactions to financial intelligence units and financial services supervisors.

143. Information may be sent to FIUs as required by anti-money laundering laws. These requirements will generally apply to a broad range of financial transactions and securities transactions are just a part of the overall requirement.

144. There are three main reporting requirements:

- Reports on all transactions that exceed a defined threshold (e.g. Armenia, Lithuania, Moldova, Poland),
- Reports on suspicious transactions involving securities (Malta, Slovenia),
- A combined requirement to report all transactions as well as submitting reports of suspicious transactions. Usually countries that require reports over a defined threshold also require reporting of suspicious transactions.

145. Supervisors usually receive reports on securities transactions on a periodic basis.

Examples

Malta. Reports are submitted to the Malta Financial Services Authority monthly and quarterly basis on an aggregated basis.

Slovenia. Financial institutions report all transactions in securities issued Slovenia to the Central Securities Clearing House.

Poland. Financial institutions are obliged to submit reports to the Polish Financial Supervision Authority on any transaction conducted on securities admitted to the regulated market.

146. In some countries supervisors perform the initial review on possible money laundering transactions and can submit a report to the FIU.

Examples

Lithuania. Financial institutions are required to report transactions with securities, which are admitted to trading on a regulated market no later than the following working day. The reports are made to the Central Depository (the data is also available to the Lithuanian Securities Commission). Starting from 01/11/2007 these reports will be made directly to the Lithuanian Securities Commission. The FIU receives the data on all suspicious transactions exceeding 50 thousand LTL (approx. €15,500). Investment companies must keep a register of suspicious transactions and report them directly to the FIU.

Bulgaria. In the Financial Supervision Commission (FSC) there are built two supervision systems: "SecuritiesWatch" and "EXTRI" for exchanging information between the FSC, the Bulgarian Securities Exchange and the Central Depositary.

- SecuritiesWatch - A system for supervision of trading on the securities market. The main role of the system is to perform real-time analysis of transactions on the securities market. The system allows both real-time and historic enquiries.
- EXTRI – The FSC manages the exchange of information between the Central Depository AD and the Bulgarian Securities Exchange – Sofia for the purpose of exercising control and

supervision over the securities market. The main aim is the disclosure of public information. Entities regulated by the FSC are obligated to disclose information to the Commission, the regulated securities markets and the Central Depository.

Azerbaijan Financial institutions are required to report securities transactions to the State Committee for Securities monthly. The State Committee for Securities manages the exchange of information between regulatory bodies and also initiates investigations.

147. Information concerning underlying customers will be held by the financial institution conducting the transaction. It is, however, noted that with securities transactions a number of different financial institutions may be involved with a single transaction, namely:

- Broker(s) arranging and executing the transaction;
- Security Exchange which may act as a central counterparty to the transaction;
- Bank(s) that carry out payment for the transaction; and
- Registrar or custodian that records the change of ownership rights and may also hold or register the securities.

148. A single securities transaction may become the object of CDD measures at any or all of these entities. There is therefore the risk that each financial institutions may rely on another institution involved to conduct full CDD with the risk that the transaction will not be properly reviewed.

149. In money laundering cases the access of FIU to the sufficient amount of data is crucial. Usually legislation grants the FIU full access to the all relevant data. There are, however, factors that can limit this access:

- Insufficient initial information. Banking and professional secrecy rules may often present a barrier to providing access to all necessary information concerning securities dealings. In such circumstances, it may necessary to obtain an order from the courts before access is granted to all relevant information required. Yet, in order to get enough data to justify the opening of a criminal case, the FIU may need to know what information is available prior to seeking court permission. This situation can be avoided either by granting the FIU or financial services supervisor unrestricted access to information.
- Dispersed information sources. Regulators and law enforcement agencies may hold sufficient information to support an investigation but information may be distributed between different agencies. This can result in multiple investigations into the same situation or failure to appreciate the magnitude of a problem. A solution to this problem is to establish an interagency coordination group and build an IT system that provides access to a central repository of relevant information.
- Time.

2 EXCHANGE OF INFORMATION BETWEEN FINANCIAL INTELLIGENCE UNITS AND SUPERVISORS

150. FIUs and financial services supervisors usually receive information about different types of suspicious activities; FIUs will receive reports of suspicious transactions which may link in to reported predicate offences, whereas supervisors will receive transaction information which facilitates detection of market abuse. Therefore, neither agency may hold the full picture of a course of transactions.

151. It is therefore necessary to ensure that there is an efficient mechanism to allow the sharing of information on relevant cases. Such information exchange is facilitated in two ways:

- **Warning.** The FIU and supervisor can notify each other of suspicious activity that may be falling within the scope of responsibilities of the other agency.

- **Access to data.** The FIU and supervisor can exchange all relevant data available on the subject of investigation (or provide direct access to data).

152. Examples of the handling of the exchange of information are set out below

Armenia. The Financial Monitoring Centre (the FIU) signed an MoU with the Financial Supervision Department of the Central Bank (the regulator of the financial sector) which sets out the mechanisms for the exchange of information. The MoU stipulates that in cases where the FSD identifies any patterns of security transactions which give rise to ML/TF suspicions it should file the appropriate information with the FMC. This information will then be analysed by the FMC and, if the basis for suspicion is confirmed, an STR should be furnished to law enforcement agencies (in the meantime, the FMC shall provide feedback to the FSD).

Bosnia and Herzegovina. Arrangements for co-operation on investigations and the exchange of information have been established between the Financial Intelligence Department and the Commissions for Securities. This co-operation has introduced a mechanism for mutual reporting and informing about those transactions that might indicate that money laundering and/or infringement of rules of doing business by securities houses has taken place.

Bulgaria. The Financial Supervision Commission (FSC) is one of the reporting entities under the Law on Measures against Money Laundering (LMML). The Bulgarian FIU, the Financial Intelligence Agency (FIA) is empowered to receive information from the FSC in two directions – first it may receive STRs from the FSC or notifications under the art. 3a of the Bulgarian AML, the LMML, which provides that supervisory authorities of Bulgarian reporting entities under this law are obliged to report any findings regarding AML/CTF compliance of the reporting entities to the FIA. Further the FSC may request checks on particular persons or entities in the FIA databases in relation their supervisory capacity. In addition the legal provisions on information exchange between FIA and FSC are elaborated in Instruction № 3/15.05.2003 on the co-operation and interaction among FIA and FSC.

Croatia. The Croatian Financial Services Supervisory Agency concluded an agreement with the Ministry of Finance, FIU, on the co-operation and the exchange of information in the process of preventing and detecting money laundering and the financing of terrorism. The goal of this agreement is co-operation and the exchange of information and data within the scope of authority as prescribed by the Securities Market Law and the Law on the Prevention of Money Laundering. It is frequently used when conducting supervision of securities companies, investment funds and investment fund management companies, as well as the securities exchange and other legal persons authorised to conduct business with securities.

Cyprus. The appropriate Supervising Authority that regulates operations with Securities in Cyprus is the "Cyprus Securities and Exchange Commission" which has the responsibility to assess and supervise compliance. According to The Prevention and Suppression of Money Laundering Activities Law, when the "Cyprus Securities and Exchange Commission" is of the opinion that any person subject to its supervision may have been engaged in a money laundering offence, it shall as soon as is reasonable practicable, transmit the information to the Cyprus financial intelligence Unit, which is the Unit for Combating Money Laundering.

Malta. In accordance with the Prevention of Money Laundering and the Financing of Terrorism Regulations, the Malta Financial Services Authority is obliged to inform the Financial Intelligence Analysis Unit (FIAU) and pass all relevant information to the latter if:
- during its supervisory functions, it encounters any suspicious transaction/s that are in anyway connected or suspected to be connected with ML/FT;
- it is requested by the FIAU to give information on any person or company or any transaction suspected to be involved or in any way connected with ML/FT.

Poland. All securities regulatory bodies are designated "co-operating" units and they are required to provide the FIU with information – according to the provisions of AML/CFT Act - about transactions, where money-laundering is suspected.

Romania. **R**he FIU (National Office for Preventing and Control of Money Laundering) can receive information from regulatory agencies on transactions involving securities, in two situations:
- The regulatory agency (National Securities Commission (NSC) – the prudential supervision authority) shall immediately inform the FIU, when the information obtained (usually in the course of a supervisory review) indicates suspicions of money laundering, terrorist financing or other violations of the provisions of AML Law.
- If in the course of an investigation, additional information is necessary, the FIU has the legal possibility to request and receive information from the NSC on operations with securities related to money laundering cases.

Slovenia. When the Securities Market Agency, as a regulatory and supervisory agency, detects securities transactions which indicate that money laundering has been involved, and the financial institution which executed the transactions hasn't reported these transactions to the Office of Money Laundering Prevention (OMLP), it sends a report to the OMLP. It is then the OMLP`s decision whether to start an investigation.Conversely, when the OMLP is investigating a case on the basis of a report from a financial institution or a report from a state agency, OMLP may send a request for data, documentation or information to any financial institution or regulatory agency. They are obliged by The Law on Money Laundering Prevention to provide the OMLP with all the data and documentation at their disposal.

153. One example of data access is Ukraine's Single Information System (EDIS):

EDIS was created in Ukraine in 2003-2007 to collate data relating to money laundering transactions.
A number of public bodies have dedicated servers and software for providing access to data. All servers are connected via a protected network with a central system which is located in the FIU.
The structure of EDIS is set out below.

Thus, the FIU of the Ukraine is able to receive on-line information, relating to securities transactions from State Securities Market and Securities Commission by means of secured electronic connection. The information available includes: a register of professional participants of the securities market and self-regulated organisations; quarterly reporting on transactions executed by securities companies; information concerning shareholders, who hold more than 10% of the statutory funds of the issuer; information on registered capital issues; lists of joint-stock companies and companies including bonds issuers;data on amounts and participants of concluded securities transactions; data on net assets value of mutual investment funds.

3 TRANSFERRING CASES TO LAW ENFORCEMENT

154. Rules and regulation applied to the securities market, including restrictions for use of bearer securities, market manipulations and insider dealing, and other preventive measures represent only one side of the AML process. Another important aspect is prosecution. Prosecution of money launderers is the final product of the processing of information sent from reporting entities to FIUs.

155. Statistics concerning money laundering cases utilising securities are quite similar in a number of MONEYVAL countries. Attention is, however, drawn to the number of investigations and the amounts of money frozen in Poland, Romania and "the former Yugoslav Republic of Macedonia".

Statistics of money laundering cases using securities in some MONEYVAL countries in 2006

Currency, €	*Bosnia and Herzegovina*	*Bulgaria*	*Croatia*	*Malta*	*Poland*	*Romania*	*Slovenia*	*"The former Yugoslav Republic of Macedonia"*
Money Laundering cases using securities								
Investigations	4	0	4	1	19	11	0	10
Amount	8 117 305	n/a	16 451 673	n/a	n/a	n/a	n/a	n/a
Criminal Proceeds	2	0	0	0	1	4	0	n/a
Amount	243 685	n/a	n/a	n/a	n/a	n/a	n/a	n/a
Transfer into securities	1	0	0	0	11	n/a	0	
Amount	204 510	n/a	n/a	n/a	n/a	n/a	n/a	n/a
Used for laundering	1	0	0	1	3	n/a	0	
Amount	7 669 110	n/a	n/a	n/a	n/a	n/a	n/a	n/a
Legalised proceeds		0	0	0	4		0	
Money frozen	0	0	4	0	3 987 563	150,000,000	0	2 543 870
Court cases	2	0	0	0	0		0	2
Amount	243 685	n/a	n/a	n/a	n/a	n/a	n/a	n/a
Market Abuse								
Statistics	3	13	0	0	27	4	17	n/a
Market Manipulation	n/a	n/a	n/a	n/a	15	3	3	n/a
Insider dealing	n/a	n/a	n/a	n/a	12	1	14	n/a

Bosnia and Herzegovina. During 2006, the Financial Intelligence Department conducted 4 investigations which related to money laundering utilising securities transactions in amounts totalling 15,876,624 BAM.
Bulgaria. Several transactions utilising the trading of shares among linked subjects were identified. In these situations sales and purchase of shares have been performed over a very short time period. In these transactions, the seller would sell at large loss and the purchaser has purchased shares at a substantial discount to the market price.
Croatia. In 2006 and 2007 the Croatian Financial Services Supervisory Agency received a total of 4 suspicious activity reports which were related to securities transactions. The Agency notified the FIU in all 4 cases. There is no information on possible judicial proceedings at present. There were no related FIU freezing orders.
Cyprus. During 2006 there was one investigation of money maundering using securities conducted by the FIU. Suspicious funds were transmitted in order to be used for the purchase of shares. Moreover there were 2 cases in which the FIU assisted the SEC in reviewing intelligence regarding foreign investment firms. A predicate offence was not established; therefore the only thing that can be stated is that there is a possibility that this was the intention of the persons under investigation.

Estonia. In 2006, The Financial Supervision Authority co-operated with the Financial Intelligence Unit, an independent structural unit of the Central Criminal Police, in two cases of possible money laundering notified to the Financial Supervision Authority by foreign authorities. No money was frozen.
Malta. The FIAU analysed only one case in 2006 concerning money laundering which could have involved dealing in securities. The use of securities in this case appears to have been utilised to facilitate tax evasion. This is still under investigation by the Police.
Poland. In 2006 GIFI conducted 19 investigations concerning money laundering using securities and their derivatives. In 10 cases those investigations resulted in notifications filed with the Public Prosecutor. The other cases are still under investigation by GIFI. Around 13,500,000 PLN has been frozen (approximately €3,700,000).
Romania. In 2006 NOPCML received 15 STRs concerning suspicions of money laundering using securities. From this, 4 STRs were sent to the General Prosecutor's Office (GPO) and the rest are still under investigation. In those cases which were sent to the GPO, either securities were used as an instrument of money laundering or the apparently legitimate proceeds were in the form of securities.
In 2006, DIOCT investigated 4 cases of money laundering involving violation of capital market law. The criminal proceeds were introduced into the capital market system as cash and securities. Securities listed on the RASDAQ market and securities in their first day of listing on the Securities Exchange were used. 5.4 billions securities valuing €150,000,000 were frozen. One case was sent to court and it is still on trial, 3 cases are still under investigation by DIOCT.
Slovenia. In 2006 the OMLP did not conducted any investigations on money laundering using securities. Investigations conducted in previous years revealed that most of the suspicious transactions reported were carried out at prices significantly below or above the market value in order to minimise or avoid taxes. The OMLP has not issued any orders for temporary postponement of transactions in cases of money laundering using securities.

MONEY LAUNDERING SCHEMES AND METHODOLOGIES

156. This section describes the schemes and methodologies that have been utilised to launder money on the securities. It is noted that these methodologies are linked to underlying predicate offences which are explained in greater detail in Section 5.

157. The transactions set out in this section and the following section on case studies are primarily designed to assist in the layering and integration of the proceeds of crime and it is noted that transactions in securities are less frequently utilised to place cash into the system. It should, however, be noted that placement of cash into the financial system can occur in using securities transactions. In particular, placement of cash can be carried out by investing small amounts of money in retail securities using cash and then subsequently selling the securities and asking for a bank transfer or cheque. A variation on this is where regulations require that securities have a "cooling-off" period which requires that investors can get a full refund if they cancel the contract within a designated period, obtaining a full refund of the purchase. This is a feature in the regulation of packaged investment funds in some countries.

1 USAGE OF ILLIQUID SECURITIES OR SHARES IN FICTITIOUS COMPANIES

158. Money laundering schemes frequently utilise securities that do not have a real market or for which a true market value is difficult to ascertain. Examples are:

- illiquid securities;
- shares of non-existing companies;
- shares which have been removed from listing on a recognised stock exchange;
- bills not covered by any assets.

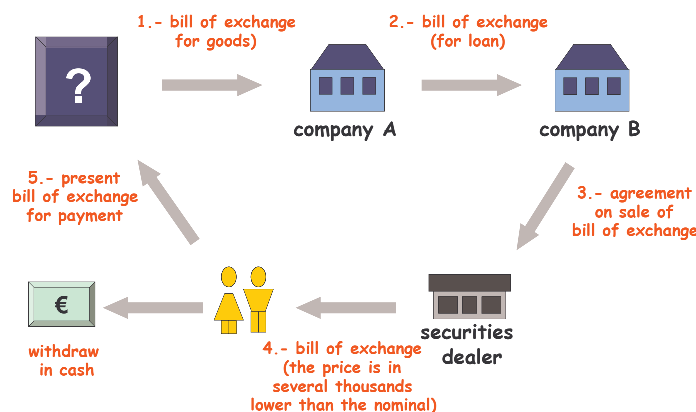
159. Frequently such schemes involve transactions with non-residents. The aim of the scheme will frequently be to transfer funds across national boundaries utilising fictitious profits or losses as a result of securities transactions. Underlying offences may include capital flight, tax evasion or transfer of the proceeds of criminal activity to avoid detection and confiscation.

Example I
A non-resident entered into a series of securities transactions for the purchase and sale of shares of fictitious companies. The proceeds of these transactions were then used to purchase foreign currency which was transferred abroad.

Example II
An agreement was entered into for the purchase of agricultural equipment from a non-resident company. The equipment was paid for by bills of exchange.
The issuer of the bills of exchange held illegal funds. The bills of exchange were issued to a non-resident company who discounted the bills which were then sold and subsequently redeemed by a thirds party. It was noted that agricultural equipment was never delivered.
The steps in the transaction were:
1. The owner of the illegal funds issued a bill of exchange[12] to company A in payment for the agricultural equipment.

[12] Bill of exchange (draft, promissory note) – an unconditional order issued by a person or business which directs the recipient to pay a fixed sum of money to a third party at a future date. The future date may be either fixed or negotiable. A bill of exchange must be done in writing and signed and dated.

2. Company A in its turn passes this bill of exchange to company Y as collateral for a loan.
3. Company B entered into an agreement with a securities dealer to sell the bill of exchange at a discount to its face value.
4. The dealer sold the bill of exchange to natural persons at a discounted price.
5. The natural persons then presented the bill of exchange for payment to the original issuer who held illegal funds.
A large number of participants were engaged in this scheme:
- 9 natural persons - residents, who eventually received cash in Ukraine;
- 8 legal entities – Ukraine residents which were affiliated to the holder of illegal funds;
- approximately 50 non-resident "transit" companies, facilitated the transaction in bills of exchange;
- 3 companies – non-residents, registered in offshore zones.
Source: Ukraine



2 COMPANIES CONTROLLED BY CRIMINALS

160. Companies controlled by criminals are utilised in most methodologies where securities transactions are involved in money laundering.

161. Companies controlled by criminals can be established in two ways:

- Establishment of a new company, using false documents and fictitious persons;
- Purchase of a legitimate company with a good reputation and trading record from its owners.

162. Frequently, the companies operate for a short period of time, with the use of forged documents and nominees. For conducting of financial transactions nominees including young persons, persons that were convicted for small offences, persons connected with drugs trafficking, homeless persons and alcoholics.

163. Funds derived from criminal activities are transferred to these organisations, frequently disguised as normal business transactions. These funds are then transferred to the accounts of linked or subsidiary companies, often located in offshore zones.

164. In some cases companies operate for a short period of time and avoid registering with domestic tax authorities. Conversely, other companies operate for longer periods of time submitting reports to tax authorities.

165. In general the criminal controlled companies can be categorised in three ways:

- **"Black" company** – frequently used for one-off transactions.

As a rule, such a company is registered by individuals using forged or stolen passport, passports. It is established for a short period of time and doesn't maintain any books or records of account.
Typically, the company will be utilised for one illicit transaction only. The proceeds of the transaction will then be laundered using overpriced securities.

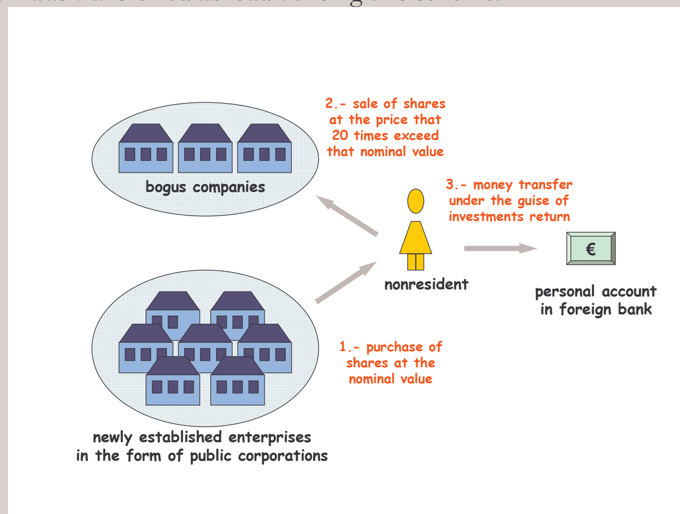
- **"Grey" company** – for multiple transactions.

With utilisation grey companies more complex mechanism are created. Such company will frequently be established using dummy directors. They will frequently provide reports to tax authorities and accounting records are maintained. Transactions will normally be conducted exclusively though a network of criminal controlled companies, located in other regions/countries with the aim of complicating detection of criminal activities and money laundering schemes.

- **"Buffer" company** – for consolidation of mechanism.

Buffer companies are established as apparently legitimate companies to complicate the work of state authorities and protect company conducting criminal activities which sit behind the buffer company either as a subsidiary or as a controller.
The buffer company protects the company conducting criminal activities from punitive measures as it is a legal structure and all transactions with it are legitimate. The buffer company will frequently act as an "honest" intermediary in transactions and may purchases the goods from another bogus company for further resale.
When investigations are held into the companies conducting criminal activities the buffer company may be used to frustrate or delay investigations. This may allow the companies conducting criminal activities to take remedial activity which may include liquidating activities and closing the companies down.

Example
A group of newly established public corporations issued shares. A foreign citizen purchased these shares at their nominal value. She then sold these on to enterprises A, B and C at a price 20 times higher than their nominal value. These newly established public corporations were fictitious and had not underlying business activity. The foreign citizen subsequently transferred the sale proceeds to her own account abroad declaring this as a return on investments.
It was detected that the foreign person:
- presented a lost passport as proof of identity;
- did not cross Ukrainian border;
- was an elderly woman of 69.
More than €59million was transferred abroad utilising this scheme.



Source: Ukraine

166. Criminals often use shares of public corporations that are traded in the securities market, as the means to launder "dirty" money. The founders of newly created companies are frequently found to be straw men who agreed to sign the registration documents of the enterprise at the request of anonymous individuals without being fully aware of their background. Such companies do not subsequently conduct the activity which is set out in their statutory documents and funds are not subscribed for the shares of the company. Likewise, the registered addresses of such companies are not real as they are registered under forged documents. They conduct no activity; do not report to the tax authorities or securities commissions. They hold no tangible assets on their balance sheet. Their sole function is for their shares to be used by financial institutions as the mean of money laundering.

Example

Bearer shares are frequently used to transfer funds between the legitimate economy and criminal organisations. Bearer saving certificate are transferred through a number of intermediaries as a means of complicating and disguising the transactions.

As an example, an enterprise bought bearer saving certificate through wire transfer and then delivered the bearer certificates to a "strawman". The transactions are conducted directly within a bank, using false identities "stolen" from legitimate persons.

Source: Ukraine

3 TYPICAL SCHEMES

3.1 Overpricing and underpricing of securities

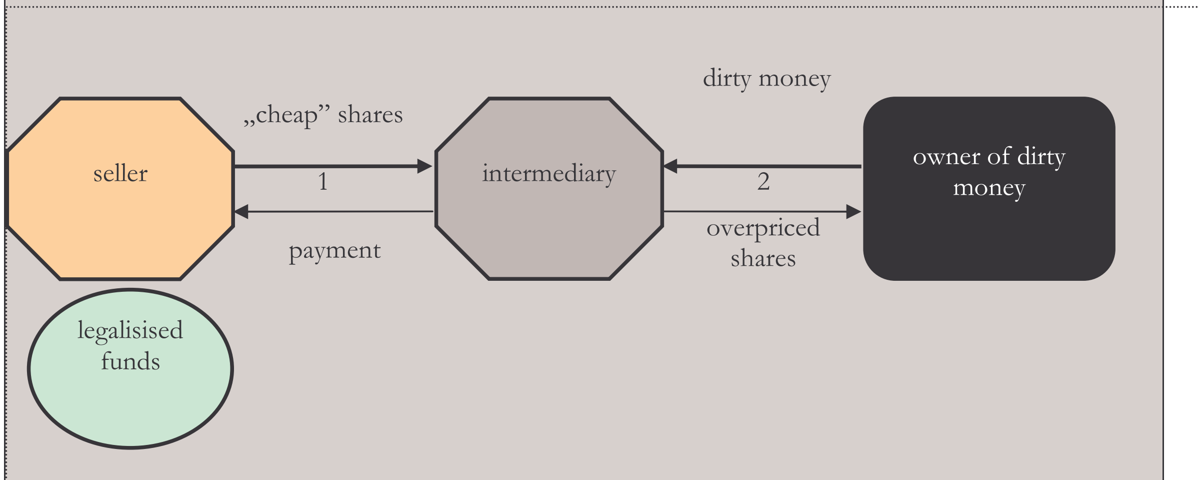
Overpricing/underpricing

Stage of ML – integration

Legalisation of the proceeds of crime is achieved through speculative trading with securities at off-market prices. A criminal associate purchases securities at a cheap price (1), and then resells them, in an agreed transaction via an intermediary, at an artificially inflated price, to the person holding illicit funds. The profit for sale of the shares then appears to have been legally obtained.

This methodology can be utilised for complex transaction structures with a number of buyers and sellers.

Such transactions can be detected if there is centralised transaction reporting with automated comparison of transactions to market prices.



Example
The money-launderer (subject A) sought to legalise financial assets derived from criminal activity. To achieve this he cooperated with another money-launderer (subject B). Futures contracts sold by subject B are purchased by subject A. In a short period of time a corresponding transaction was concluded, effectively reversing the transaction. All material elements of this transaction, such as the price, the volume and the date, were agreed between subject A and subject B. The agreement of all of the elements of the transactions was essential to ensure that transaction could be concluded between the two money-launderers.
Source: Poland

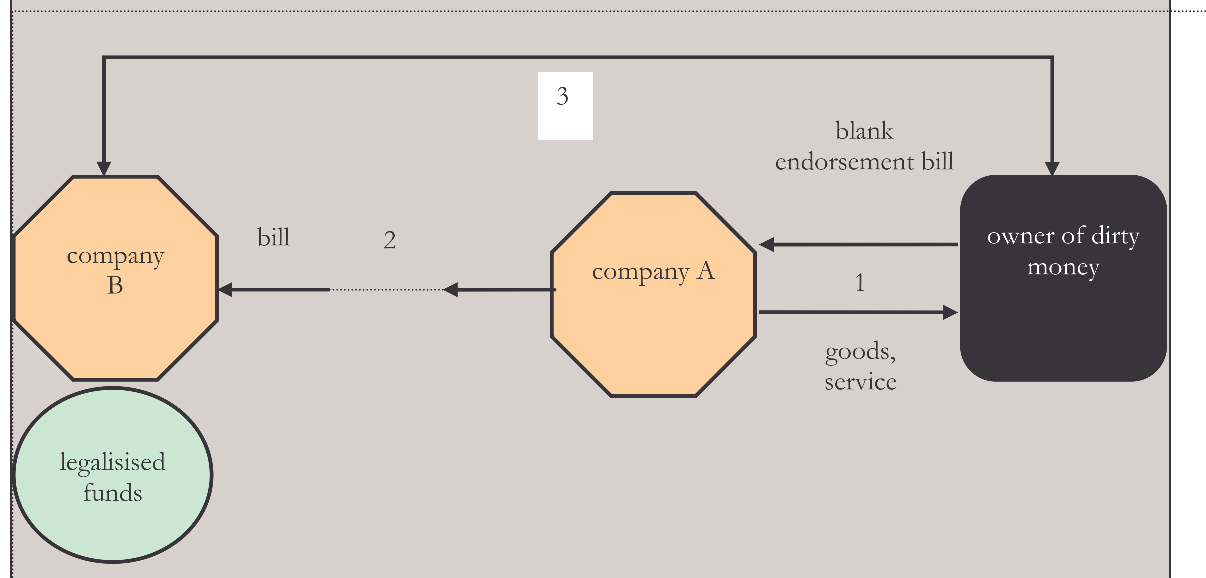
3.2 Breaking of the chain of ownership

“Break of chain” Transactions using bills of exchange

Stage of ML – layering,

The owner of illegal funds money makes out a bill of exchange with a blank endorsement in return for goods or services from company “A” (1). In the course of transactions company “B” receives this bill (2). Company B then presents it to the bill issuer for payment (3) and receives legalised money.

This scheme is frequently applied along with others in more complex money laundering schemes, and is intended to break the “break a chain of ownership” of documented transactions for money laundering.

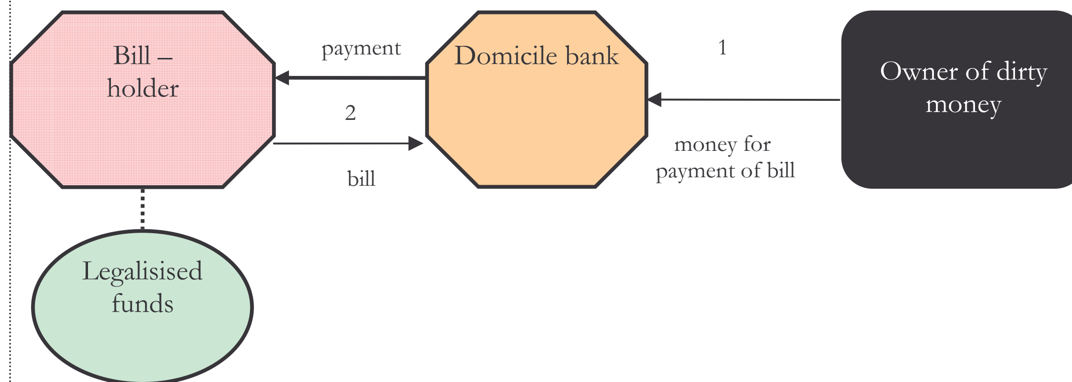


“Breaking the chain of ownership”. Transactions with domiciled bill[13]

Stage of ML – layering

The company concludes an agreement with a bank to issue a domiciled bill. Money is then paid to the bank as support for the bill account (1). The bank then pays the bill in accordance with its terms (2).

A variation on this scheme can be the use of a domiciled bill as a security for a natural person (including non-residents, who could present the domiciled bill at a bank for payment) to receive credit in a bank or pawn-shop. Domiciled bills are convenient as they provide security for transactions.



[13] Domiciled bill - bill payable in particular place, especially paid by designated bank.

3.3 Justification of money transfers

Fictitious transactions with securities to facilitate money transfers abroad

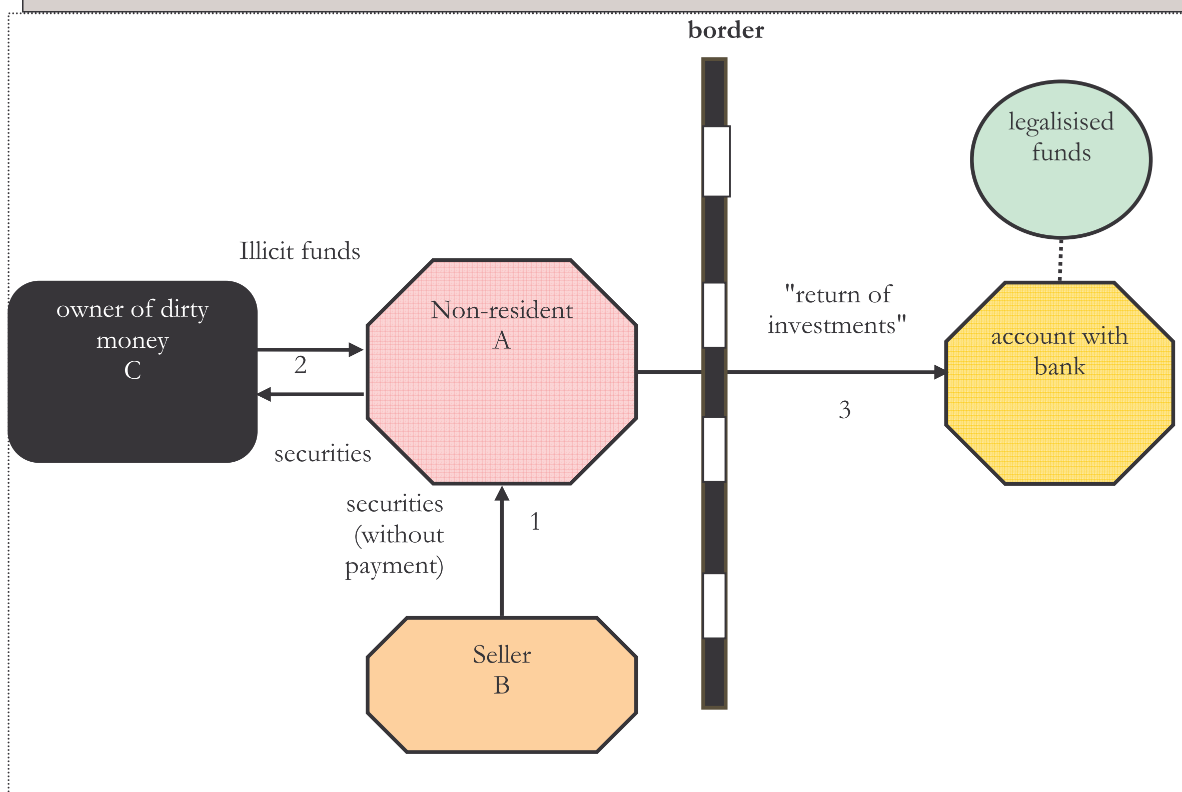
Stage of ML – layering

A Non-resident "A" concludes an agreement for purchase of securities and receives the securities from the seller "B" (normally a strawman). The non-resident "A" does not pay for the securities (1). These securities are then sold by the non-resident for illicit money "C" (2). The money is then transferred outside of the country to the account of the non-resident "A" under the guise of "return on investments" (3).

In a variation on this methodology, the non-resident "A" receives the securities and then the agreement is cancelled. The securities are not, however, returned.

Generally, this scheme is applied to mask the illegal origin of illicit funds and is utilised for the purpose of their further legalisation as part of a money laundering scheme.

In this methodology, the non-resident purchases and sells the securities at almost the same price (this is made to avoid taxing the investment proceeds of non-residents).



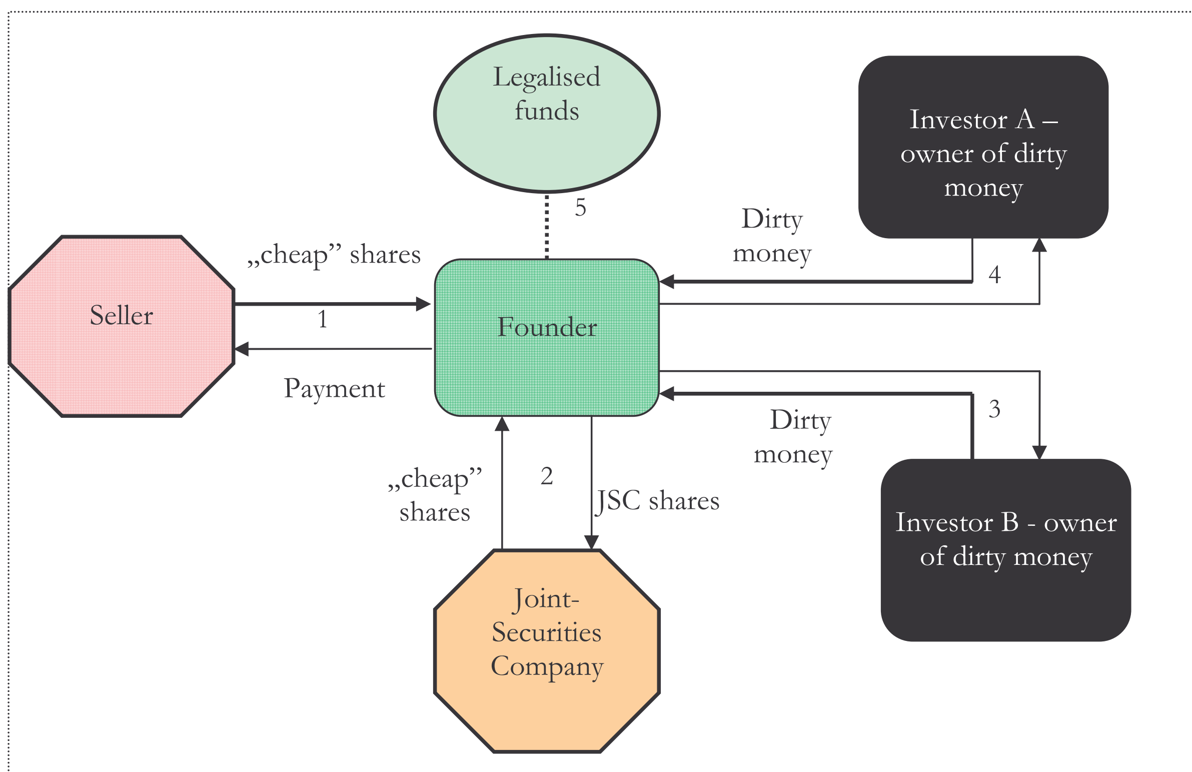
3.4 Issue of shares of newly formed company

Speculative transactions following the formation of a joint stock company (JSC) statutory fund

Stage of ML – integration

The legalisation of illicit funds may be achieved by means of the receipt of funds following the formation of a joint stock company. The shares of the newly formed company are issued to investors A & B at an inflated value (1, 2). Investors A & B purchase the shares using illicit funds. The founders of the company now appear to have acquired funds legally (5).

As a rule, there are no violations of legislation in the implementation of this scheme. Though, fraud is possible if over-priced shares are subsequently sold to unconnected investors.



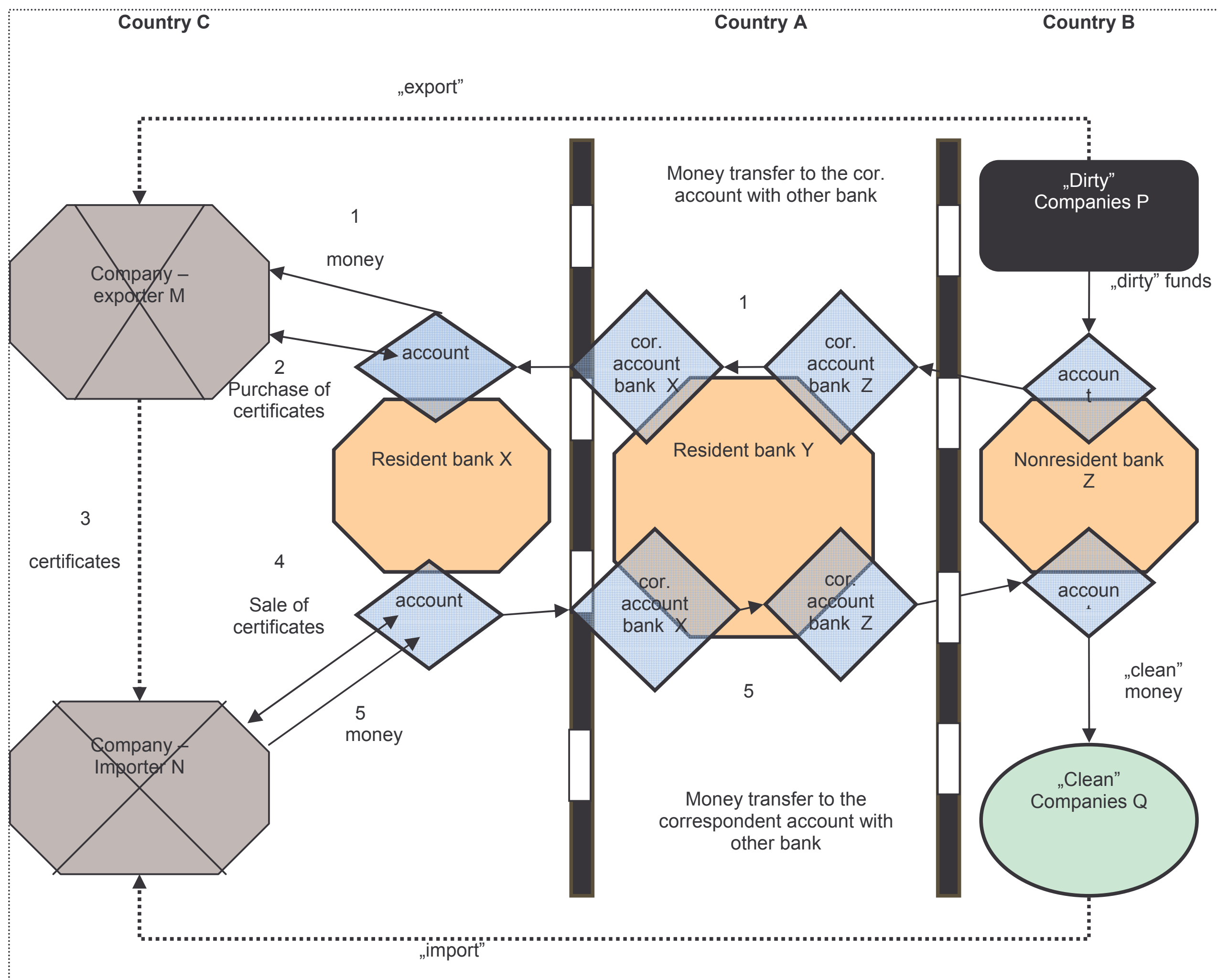
3.5 Carousel fraud

Money laundering transactions with the use of bearer deposit certificates issued in foreign currency

Stage of ML – layering ("break of chain"), integration

Exporting and importing companies have opened accounts with bank X in the country C. Bank X has a correspondent currency account with bank Y in country A. This account is mainly used for transactions in free convertible currencies that are not widely used for payments in international transactions and are not sold on the main world currency markets or are non-convertible currencies. Bank Z in country B has a correspondent account with bank Y for transactions in the same currencies. Country B is remote and banks are not cooperative on sharing customer information. Both legitimate and illegitimate companies hold accounts with Bank Z.

Exporter M receives currency proceeds from the "dirty" company P under an "export" contract (1). The same day it purchases bearer deposit certificates in currency from bank X (2). The certificates are then passed handed to importer N (3). The same day importer N presents the bearer deposit certificates for payment (4) and transfers money to the "clean" company Q under the "import" contract (5).



4 CASE STUDIES

167. Examples of money laundering typologies submitted by representatives of MONEYVAL countries set out below.

168. The examples submitted by Bosnia and Herzegovina, Bulgaria and Poland indicate that transactions with securities on the over-the-counter markets are often used by criminals in money laundering schemes.

169. Bosnia and Herzegovina, Bulgaria and Poland also reported instances where shares in companies were sold and the proceeds were reinvested in shares in other companies at prices significantly in excess of the prevailing market price.

Example

Purchase and sale of shares at off-market prices
The securities are purchased at a lower price than their market value. The seller then receives the balance of the purchase price through alternative means. The buyer, usually a middleman, now has securities with a value similar to the value of financial assets obtained by him from criminal activities. The securities are then sold at market price to investment funds registered in off-shore countries. Transactions are frequently conducted on unregulated or over-the-counter markets. The securities involved are the employees' shares of state-owned companies that are about to be privatised and quoted on the securities exchange.
Source: Poland

170. Bulgaria reported an incident where share dealing accounts were established where the account was funded from an overseas account and dealings appeared to be conducted with a linked account which was also funded from overseas.

171. Croatia and Poland have reported similar incidents with funds provided from overseas accounts.

Example
A certain Company X borrowed a large amount of money from abroad (mostly from companies which were set up in tax oases) which they then deposited with a Company C and continued to conclude further loan contracts with the same Company. Based on their contract, Company X converted their loan, in the total amount of €16,162,052, into shares of the Company C and thus became the major shareholder. It was noted that the annual accounts of Company C indicated the Company was operating at a loss. This raised the question of how the substantial loans entering the Company were to be utilised.
Source: Croatia

Example
The shares of a Company A, registered in European Country X, were purchased by non-residents (frequently either a company registered off-shore, or citisens of countries not complying with FATF Recommendations) at a price higher than the market price. The shares were purchased with the use of funds derived from criminal activity performed abroad or with the use of funds derived from criminal activity performed in European Country X, which had been previously transferred abroad. These are quite often fictitious transactions which are not accompanied by the movement of cash. In this case contracts submitted to the Revenue Service are the only proof of these transactions.
Source: Poland

172. Several additional examples of money laundering typologies are provided hereinafter :

Example I

In this money laundering methodology, securities are not purchased or sold. However the nature of the dealing account gives the appearance that the balance on the dealing account derives from investments made on the securities exchange market.

The dealing account is established to execute securities transactions but can also be debited or credited to reflect other non-cash transactions. In this circumstance, the initial (placement) stage of ML is conducted outside this account or the financial assets derived from the criminal activity are in the form of payment instruments located on other bank accounts, financial instruments or other securities which have been acquired elsewhere.

The account is operated in a manner to create the impression that financial assets on the securities dealing account are derived from legal investments on securities exchange. Therefore, the money-launderers execute a significant number of transactions of purchases or sales of securities, often without any economic reason.

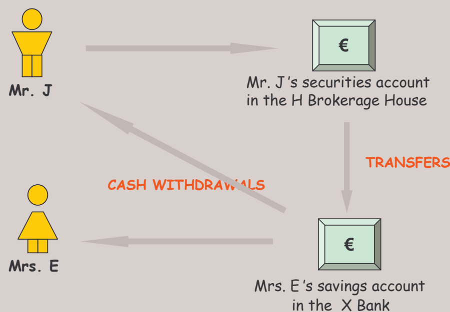
The possible losses from such transactions constitute costs of trying to legitimise the proceeds of crime. The aim of transactions on the securities dealing account is to disguise the origin of the funds involved and to hinder investigation by the authorities seeking to prove the illegal origin of the financial assets. To further facilitate this, purchased securities are transferred between securities accounts carried by the different securities companies.

This method of ML is often combined with the classical method of obtaining a bank credit or a loan. In this case the securities are purchased from the sources from bank or loans which are later paid back with the money derived from the criminal activities.

Source: Poland

Example II

Mr. J does not work and he is not employed. He established an investment account at H Brokerage House. Mr. J then granted his spouse, Mrs. E, authority to give instructions on his investment account. Two days later Mr. J paid €2,650 in cash into the account. During the next three months similar transactions with amounts varying from €1,320 to €2,650 were paid into the account. In aggregate, €91,400 was paid into the account although while Mr. J only purchased a small amount of shares in a joint-stock company for €1,000. The balance of the funds on the account, €88,700, was transferred to a savings account belonged to Mrs. E at Bank X. From this account the money were withdrawn in cash or credit card by Mrs. E and Mr. J.

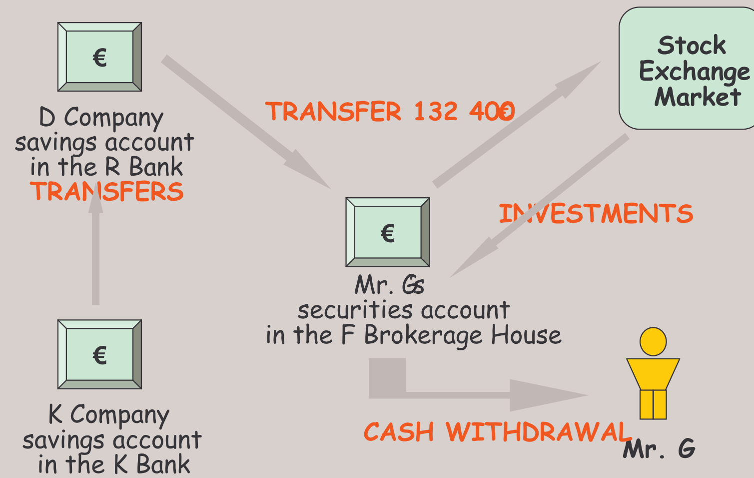


Source: Poland

Example III

Mr. G deposited €132,400 in an investment account at F brokerage house. The funds were transferred from an account at Bank R belonged to Company D. Company D was registered in off-shore country. The majority of the money, €124,500 was allocated to purchase shares. During a period of two days, Mr. G sold all acquired securities at close to their purchase price. Next Mr. G withdrawn the balance on the account in cash and closed the investment account.

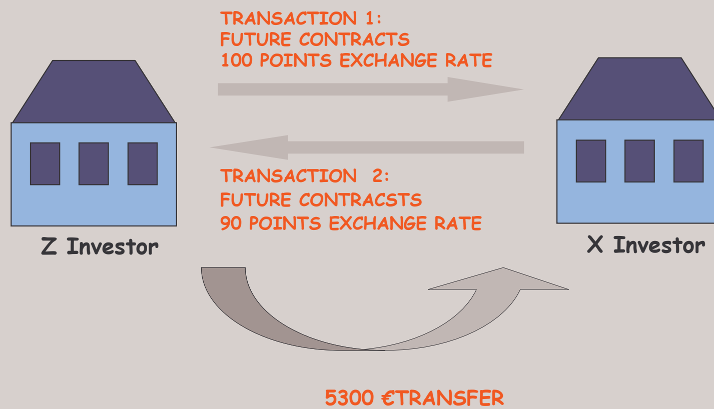
In accordance with the documents of Company D which were submitted to Bank R, the main shareholder of Company D is Company K. Company K's only shareholder is Mr. G. The bank account of Company D was funded by a transfer from K Company's account at Bank Z by way of "payment for marketing services".



Source: Poland

Example IV

Investor Z and investor X wanted to legitimise the source of their money. They entered into an agreement to transact of deposit contracts based on price of share W Company. Both had deposited sufficient funds in investment accounts to execute the transactions. According to the agreement investor X bought 200 deposit contracts for 100 points from investor Z. A similar transaction was carried out one hour later; but this time investor Z bought 200 deposit contracts for 90 points from investor X. The effect of these transactions was to transfer €5,300 from investor X to investor Z.

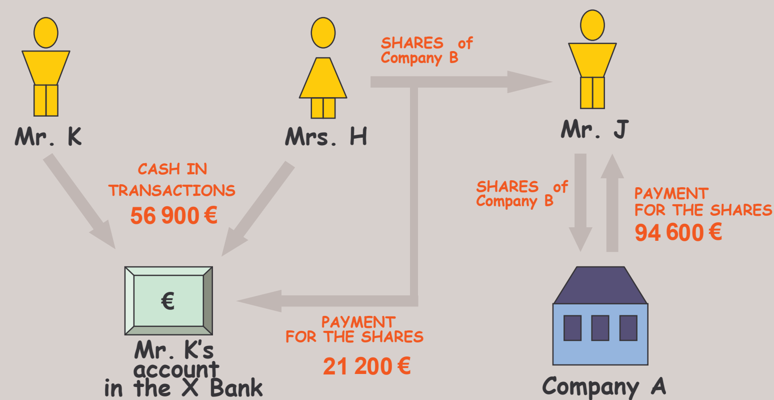


Source: Poland

Example V

In July Mr. J purchased 100% of the shares in Company B for €21,200 from Mr. K, although the nominal price of these shares was €59,600 and the underlying value of the company (taking into account the market value of property and equipment) was €84,200. The purchase price was paid in cash by Mr. J into Mr. K's account in X Bank. In the same month, during one week, numerous cash payments were made from Mr. K's account. These individual payments were all under the €15 thousand reporting limit although the aggregate sum of them was €56,900. The transactions were executed by Mr. K or his spouse Mrs. H.

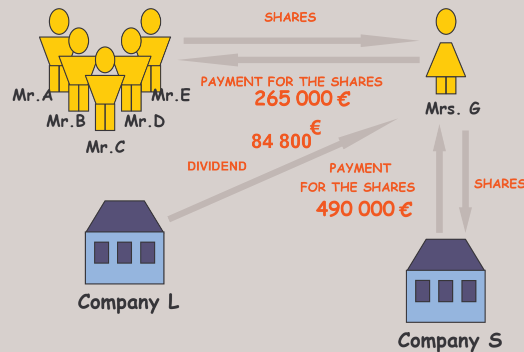
In August the same year Mr. J sold the shares of Company B to Company A for €94,600.



Source: Poland

Example VI

In April Mrs. G declared to the Internal Revenue that she had executed10 purchase transactions of shares in Company L from 5 its shareholders: Mr. A, B, C, D, E, F. In total, she bought 20 thousand shares, for €265,000. Three months later, Company L paid shareholders a dividend based on profits. Mrs. G received €84,800 as a result of this dividend. In August Mrs. G sold her shares in Company L to Company S for a total amount of €490,000€. The only shareholders of Company S were Mr A and Mr B.



Source: Poland

Example VII

Payment of dividends

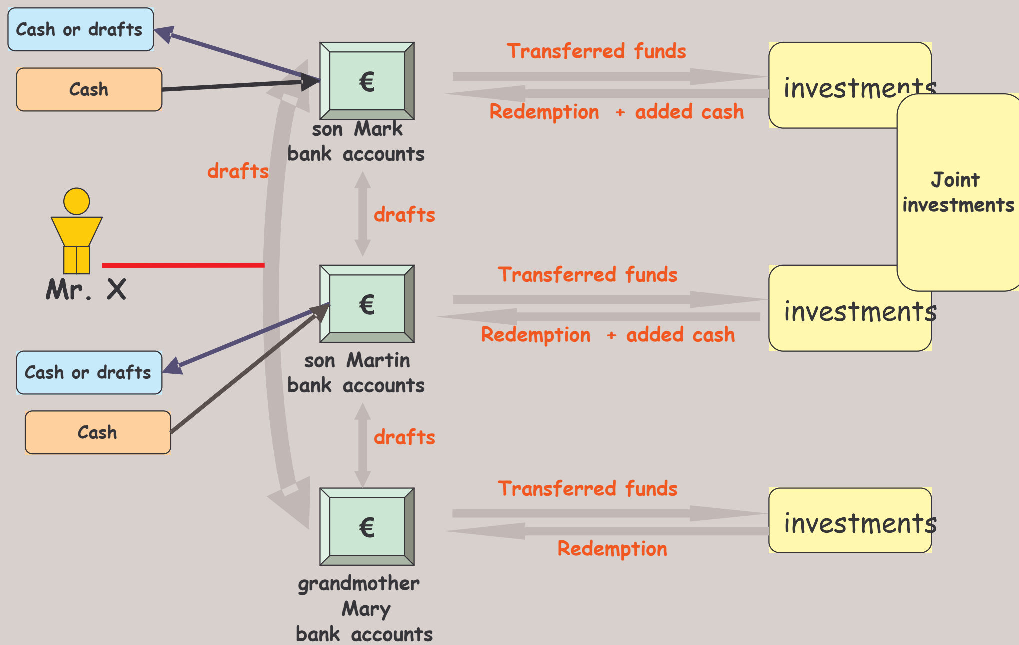
The shares of a company, which was about to pay out a dividend, were purchased using criminally derived funds. In this case the part of the "dirty money" used to purchase the securities was laundered in the form of dividend, which was paid out by the company. In this money laundering technique, shell companies are often set up to perform fictitious economic activity and to legalise financial assets derived from criminal activity. The financial assets derived from criminal activity are used to develop such companies by purchasing some fixed assets which "legitimise" the companies' activities and facilitate the sale of shares at overvalued prices.

Example VIII

An individual tried to open a bank account using a bank's draft from another bank as well as by adding a substantial amount in cash. He was introduced to the bank by Mr. X, who was his father and who also had power of attorney over other accounts opened by other family members. The applicant indicated that his father was to have power of attorney to his account.

The applicant claimed that the bankers draft emanated from a bank account that had been closed (which fact was verified and found to be correct), whilst the cash represented the proceeds of sale of some government securities (the redemption was not traced). He had no documents to prove the latter because he stated that he had destroyed his documents. This explanation triggered a suspicion. Analysis established that over a number of years the two young sons and the elderly mother of Mr. X had operated numerous bank accounts. These accounts were then closed and their funds were either taken as cash, had cash added to them to open new bank accounts, or were transferred to purchase securities. Funds from redeemed securities were either used to open new bank accounts and at times had additional cash added to it. Other redeemed securities were taken as cash.

It is suspected that Mr. X, who had power of attorney to many bank accounts of relatives (his two sons and his mother), was using these accounts in the placement stage with a view to evade tax. Cash was being regularly handed to him as his share of the family business. This cash was broken down and added to numerous bank drafts that were being organised by him through his relatives bank accounts (to which he had power of attorney) or added to the capital of closed bank accounts to open new accounts. As a consequence of his undeclared wealth, Mr. X was entitled to social security benefits since he unemployed due to being unfit to work.



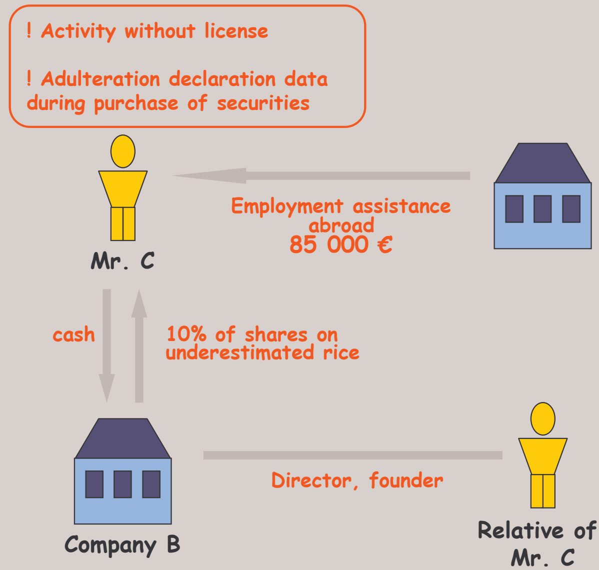
Source: Malta

Example IX

Mr C acted as an agent providing employment assistance for citizens of his country abroad, although he had not acquired the relevant license.

In the course of his activity, he accumulated profits in a European country of €85,000. In order to legalise these funds, Mr. C purchased 10% of the shares of a public corporation B at a discounted price of €32,000 (the real value was in excess of €126,000) at an auction. Payment for the shares was in cash.

Mr C supplied false information in the declaration annexed to the share purchase. Furthermore, it was revealed that director and founder of public corporation – Company B was a relative of Mr. C.



Source: Ukraine

Example X

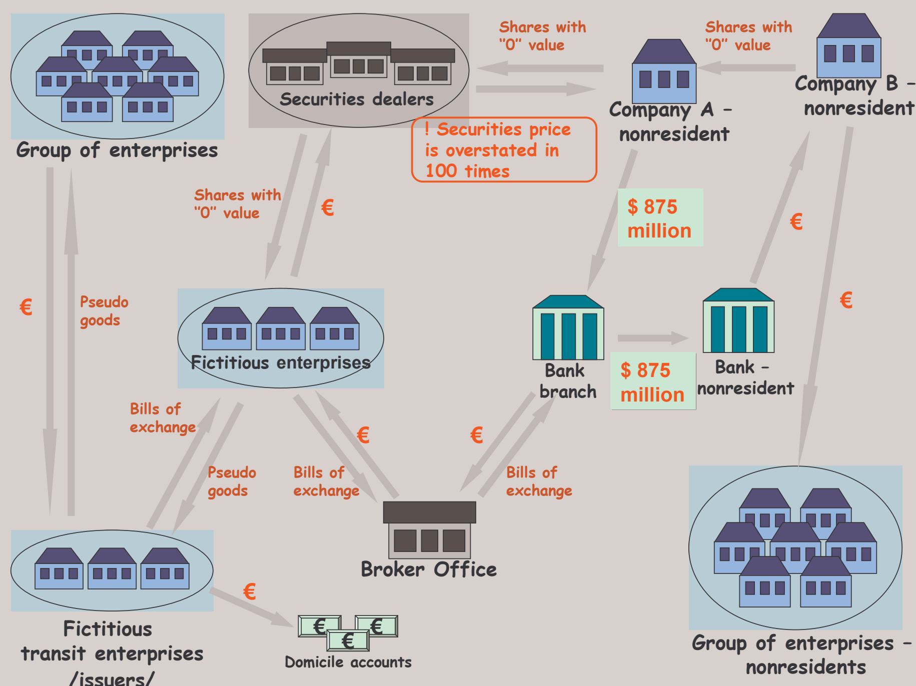
In order to legalisation the proceeds from criminal activities, a Group of companies, residents in European Country Z, transferred funds to fictitious companies, as payment for "pseudo-commodities". Promissory notes were issued to pay for the “pseudo-commodities” and funds were received against the guarantee of these promissory notes. The funds were transferred to the accounts of a domicile account, opened at a Branch of the Bank.

The promissory notes were then transferred as payment for the "pseudo-commodities" to the group of fictitious companies and were being held by a trader in a securities dealing company.

The Securities dealing company paid the group of fictitious companies for the promissory notes from funds from a domiciled account which presented the promissory notes for payment to the Branch of the Bank. The fictitious companies purchased securities of valueless securities of a foreign Company A at a significant multiple of their real value.

Company A had purchased the securities from Company B which was registered in the an American Country X.
The operation of this scheme allowed Company A to transfer $875 million, through the Branch of the Bank to its own accounts in a European bank with the justification that this was a return of portfolio investment.
Company A then transferred funds from its accounts at a bank in bank European Country Y to accounts of Company B at the same bank.

It was noted that, according to information provided by the competent authorities in the UK, Company A had not declared any investment activity. European country Y reported that a representative of Company A declared that he had never been involved in investment activity in European Country Z and had not been involved in currency transactions.



Source: Ukraine

Example XI

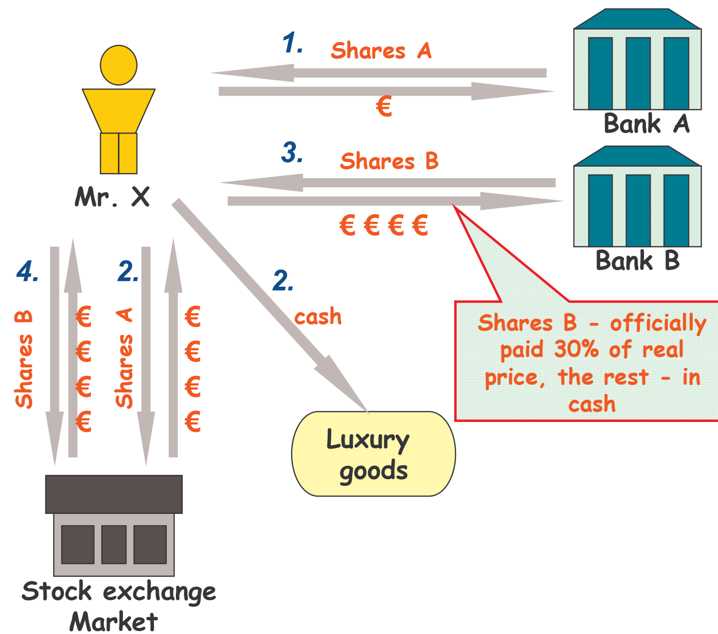
A high-ranked official (Mr. X from a supervisory agency, abused his official position in order to purchase shares of a commercial bank (Shares A).

He used his position to access the confidential information available on the national financial system. He presented false documents in courts and disguised the true identity of a number of dummy persons who were used for the purposes of these transactions.

Shares A were subsequently sold on the securities exchange and part of the proceeds were used to buy luxury goods, cars and real estate.

To legalise the rest of money Mr. X made an agreement with owners of another bank. He bought their shares (Shares B) on the over-the-counter market. Officially he paid only 30% of the market price of Shares B, the balance being paid in cash. Shares B were then sold at their true market value price on the securities exchange, and Mr. X obtained legalised money.

Source: Moldova



Example XII
Firm A received approximately €5.3 million from the State Budget as payment under a contract.
This 5.3 million € is distributed thus:
- about 2.9 million € - to firm B,
- about 2.37 million € - to firm C.

Firm B then turn transferred money to firm D.

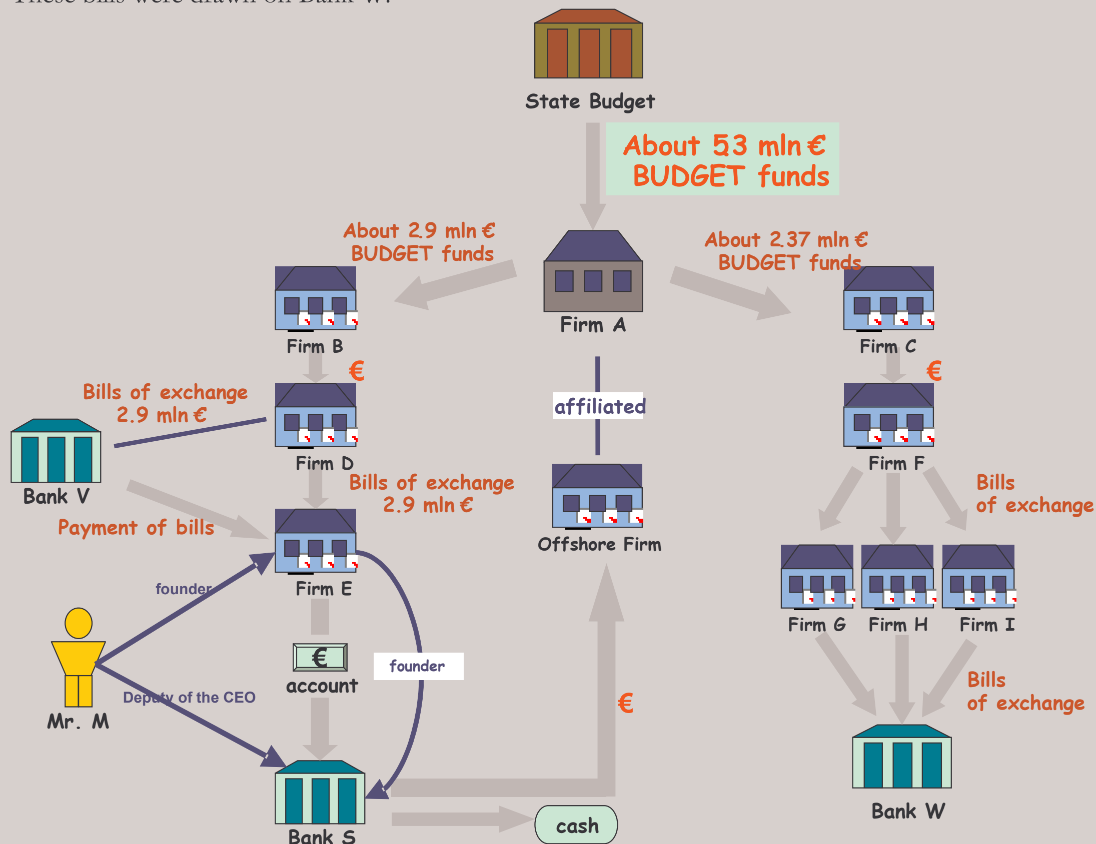
Firm D received bills of exchange for the same sum, €2.9 million. These bills of exchange were drawn on Bank V.

Firm D transferred €2.9 million and the bills of exchange to firm E.

Firm E then received full payment on the bills of exchange and transferred this money to its account at Bank S.

It subsequently became apparent that the founder of Firm E and the Deputy CEO of Bank S were the same person (Mr. M). And Firm E is also the founder of Bank S. Finally, Firm E then withdraws part of the funds as cash and transfers another part to an offshore firm which is affiliated to firm A.

Firm C transferred €2.37 million to firm F. Firm F then made out bills of exchange to firms G, H and I. These bills were drawn on Bank W.



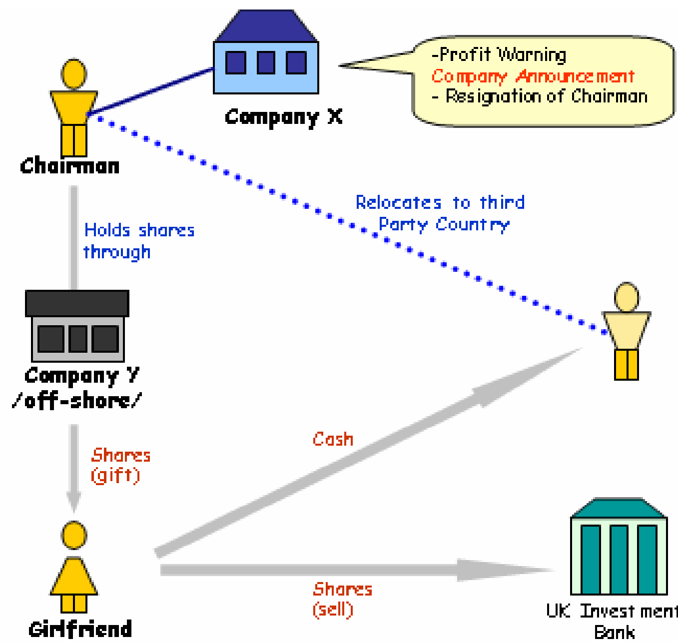
Source: Russian Federation

Example XIII
Insider dealing

Company x was listed on the London Stock Exchange. The company had experienced poor trading conditions and it was agreed that the company would issue a public profit warning which was likely to have a negative impact on the company's share price. Also, as a result of the poor trading results, it was agreed that the Chairman of the company would resign.

Prior to the public announcement, the Chairman gifted the whole of his shareholding in the company to his girlfriend. The beneficial ownership of the shares was further obscured by being registered in the name of an off-shore company. He then, on her behalf, negotiated a block sale of all of the shares, which was executed with a UK based investment bank, prior to the profits warning being announced. The Chairman then resigned and left the United Kingdom having given instructions for the sale proceeds to be transferred abroad.

Once the public announcement was made the share price dropped significantly. The Chairman was subsequently arrested upon return to the United Kingdom and was subsequently imprisoned.
Source: United Kingdom



CRIMINAL ACTIVITY LINKED TO MONEY LAUNDERING

173. Money laundering only becomes an offence if the money concerned is derived from an underlying predicate offence and it must be remembered that the overwhelming number of securities transactions are conducted for legitimate purposes. It is therefore necessary to understand the nature of the predicate offences that give rise to money laundering transactions.

174. Furthermore it may not always be clear what the underlying purpose of a suspicious transaction is. Some of the techniques for money laundering may themselves be utilised to commit financial fraud and money laundering transactions often coincide with transactions designed to commit fraud in the securities market.

175. One of the basic money laundering techniques on the securities market, execution of transactions at off-market prices, can be easily used for transfer pricing in order to:

- redistribute the tax burden between company branches in different countries;
- enhance financial reports of company branches.

176. The money laundering techniques described can also be used to disguise assets or justify 'unexpected' profits or losses in cases of:

- managers stealing money from their companies;
- public companies or financial institutions "enhancing" their balances before the report date;
- business partners hiding profits from each other;
- provident spouses hiding assets from their partners before divorce;
- hiding money from creditors;
- capital flight from a country.

177. The following activities are linked to money laundering in that they may either resources utilised to facilitate money laundering or may represent underlying predicate offences that rely on money laundering to legitimise the proceeds of the underlying predicate offences.

1 CONVERSION CENTRES

178. "Conversion centres" that provide facilities for the illegal conversion of assets into apparently legitimate assets, frequently to facilitate tax evasion, are found in a number of countries. The use of conversion centres that provide access to a range of nominee and fictitious companies is an important element legalisation of the proceeds of crime.

179. The primary "advantages" of use of conversion centres compared with other methods of tax evasion are:

- apparent legality;
- break in audit trail to criminal assets;
- universal character (conversion centres are able to provide facilities for apparently legitimate documentary evidence of financial and economic transactions covering a range of goods, services);
- complexity (range of ready to use, "turnkey", services which could include a selection of agreements with legitimate industrial and commercial enterprises including the transfer of converted cash to the directors of these enterprises, etc).

180. The following schemes are linked to the securities market.

The use of bearer saving certificates

181. Conversion centres widely electronic money transfers to move funds from the legitimate economy to the shadow economy through the purchase and sale of bearer saving certificates. The enterprise purchases bearer saving certificates from a bank, paying for these by wire transfer. At a later date, these certificates will be redeemed from the bank at face value. It is frequently the case that transactions on purchase and repayment of certificates are conducted directly the bank, and do not involve bogus companies officials or straw men.

182. The organisers of such conversion schemes frequently utilise the formal legal documents of bogus companies, and passport details of straw men.

The use of mechanism of currency purchase with the use of currency saving certificates

183. Conversion centres accumulate the funds from legitimate enterprises and transfer these to transit companies from where it is then transferred to the accounts of bogus companies. Simultaneously, currency saving certificates are bought from banks. The certificates are then sold through securities companies to bogus enterprises that, in their turn, pay illicitly acquired funds for them.

184. The bogus companies then present the currency saving certificates to the issuing bank to obtain apparently legitimately acquired funds, frequently in the form of currency deposits. This currency is transferred abroad as prepayment for goods or services that are never supplied. The funds are subsequently repatriated as cash, using unofficial transfer mechanisms, or are accumulated on accounts in offshore bank accounts.

2 VAT FRAUD

185. VAT fraud exploits the free movement of goods between countries. VAT rules concerning exports in many countries allow goods to be sold VAT free and duty free to and from other countries.

186. VAT fraud is split into two categories:

- **Acquisition fraud**

187. This is where goods are acquired VAT-free from another country and brought into the host country by a VAT registered trader, who then sells them to a buyer in the host country and the goods become available on the host country's market. The importer then goes missing without completing a VAT return or a compulsory declaration of movements of goods to or from other countries, and/or without paying the VAT due on his onward supply of the goods;

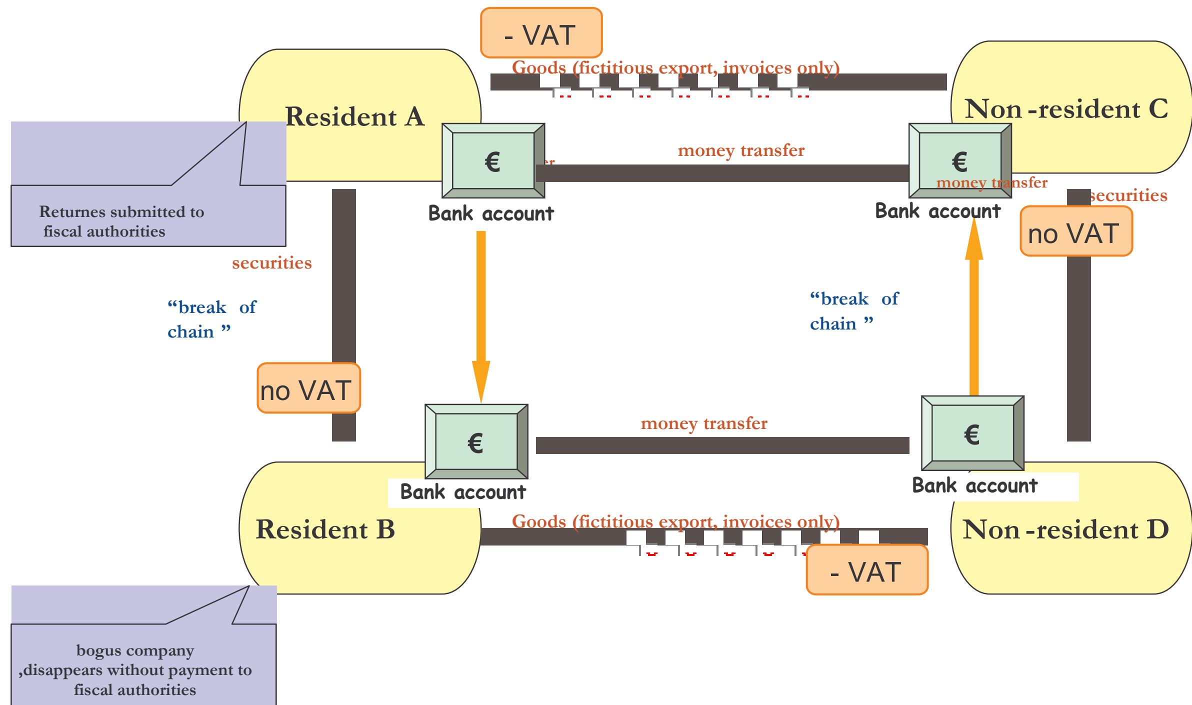
- **Carousel fraud**

188. This is similar to acquisition fraud in the early stages, but the goods are not sold for consumption in the host country. Instead, they are sold through a series of companies in the host country and then exported to another country, at which point the VAT is reclaimed. The goods may change hands between host country ‘buffer’ companies several times before a final ‘broker’ company sells them back to another country. The goods are then sold on in the other country and dispatched back to the host country where the process starts again. This type of fraud takes its name from the circular pattern or ’carousel‘.

189. Funds arising from VAT fraud are frequently moved through conversion centres using fictitious companies. Securities transactions, including bearer securities, are often used for the purpose of legitimising funds transferred from exporters to importers.

190. The use of securities is essential in VAT frauds for the following reasons:

- bearer securities may be used to 'break the chain' of the audit trail;
- over/under pricing of securities transactions is an easy way to move money abroad;
- the legitimate transaction that is subject to VAT (for goods) will frequently be balanced by another transaction, which is not subject to VAT (securities transactions are ideal for this purpose).



Example

This case study involves a number of speculative goods transactions with goods being frequently imported, sold and exported.

Goods, which had been previously exported, were returned to the country to a fictitious purchaser at a price that was 10 times lower than the export price. The goods were then sold at an overstated price through several fictitious and transit companies. Company A purchased the goods and sold them at an overstated price to company B. The same goods were then purchased by company C from company B at an overstated price. Companies A, B and C did not account for VAT on sales to the fiscal authorities. The goods were resold at the same price to company D and then imported by company E to country X. Finally, company F received the goods (through an export transaction with company Y). Subsequently, company D, which had arranged the export of the goods, claimed a VAT reimbursement from the fiscal authorities. A proportion of the funds thus obtained were converted into cash and divided among the participants of the scheme. The balance of the funds were transferred to the account of a foreign importer of goods.

The scheme was regularly duplicated (with the goods being returned to the country of production), involving several cycles of money laundering and VAT fraud.

Source: Ukraine

191. For further information, FATF has recently published a typologies report on VAT carousels[14].

[14] See Laundering The Proceeds of VAT Carousel Fraud, published February 2007

3 TAX EVASION

192. Business entities frequently use schemes with securities to avoid or minimise taxation payments. These schemes frequently involve transactions for the purchase or sale of securities in different tax periods, exploitation of differing taxation rules between different countries, etc.

193. One of the most popular schemes for tax evasion involving securities are regular transactions in bills of exchange presented as payment for goods or services performed with further presentation of such transactions as not subject to taxation.

194. It has been noted in Ukraine that there has been a move away from using bills of exchange for such transaction to utilising securities transactions.

195. In this example various fictitious companies are created. Such companies exist only on paper and do not conduct any financial or economic activity and do not have any permanent assets. Shares in the companies are sold and such shares are purchased by different securities market participants and financial institutions. The purchase of such shares, which would not normally represent an attractive investment opportunity, is made in order to realise tax losses, therefore minimising tax liabilities. This also has the effect of transferring funds to bogus companies.

196. It is noted that as securities trading strategies as well as the underlying securities products become more complex, detection and investigation becomes much more complicated.

Example
In the course of conducting tax audits, the fiscal authorities of Poland encountered several cases involving tax evasion or tax minimisation schemes which utilised securities or their derivates. The basis of these schemes was that the taxpayers failed to declare income resulting from the sale of shares in their tax returns. In some cases the companies concerned (mostly joint-stock and limited liability companies) arranged transactions in order to generate a loss and to reduce the taxable income arising from capital gains. They sold shares or outstanding debt obligations at arranged prices fixed at below the acquisition cost.
Source: Poland

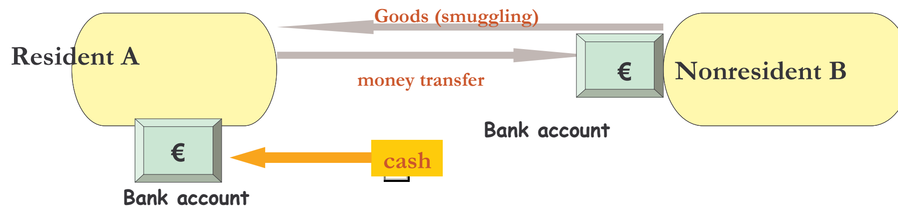
4 MONEY LAUNDERING SUPERMARKETS

197. Due to the national structure of government agencies, it is frequently the case that certain aspects of crime are the responsibility of individual agencies. For example market abuse will be investigated by the securities supervisory organisation whereas carousel fraud will be investigated by the fiscal authorities and money laundering may be investigated by the FIU. Criminals do not, however, observe such 'distinction of competences'. The same criminal group can be involved in all of the above mentioned activities (sometimes referred to as "money laundering supermarkets").

198. Moreover, some of the above mentioned crimes may generate opposing cash flows. Sophisticated organised crime groups will seek to balance such conflicting cash flows. This can significantly reduce the cost of transactions as well as reducing the vulnerability of abnormal or suspicious transactions being reported.

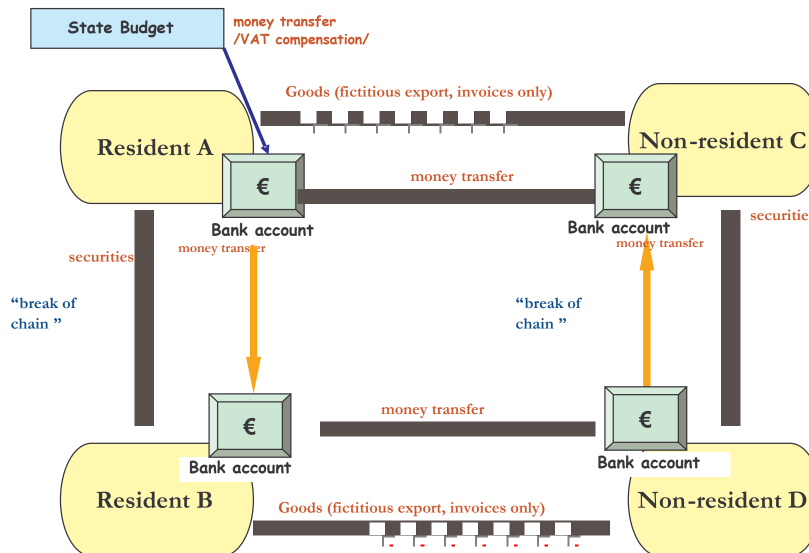
In order to illustrate this point, the following three schemes should be considered:

- ***Smuggling scheme***



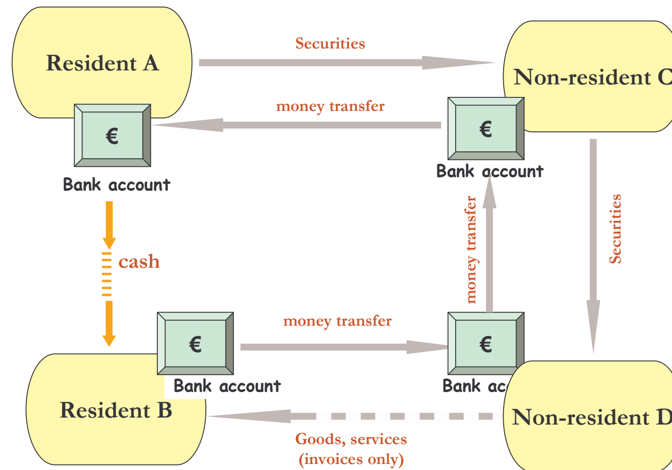
199. This is a very simple scheme – goods are smuggled into the country using a company B registered in another country. Locally domiciled A receives cash payments which are paid into its bank account and then transmitted to the account of company B.

- ***VAT fraud scheme***



200. In a typical VAT carousel fraud scheme, resident Company A makes a fictitious export of goods to foreign Company C and claims a VAT reimbursement from the fiscal authorities. However, as a precondition for the VAT claim company A has to receive payment for the "exported" goods from company C. In order to remit money back to Company C, funds are paid for securities to another Company B which sends them to the foreign Company D as consideration for a delivery of fictitious goods. Company D then pays money to Company C as consideration for the securities.

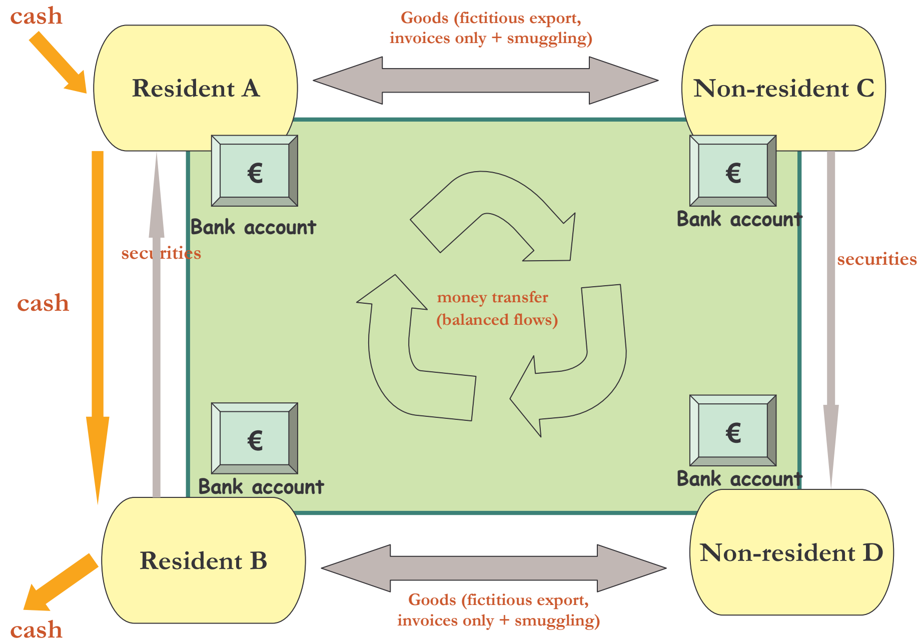
- ***Cash conversion scheme***



201. In this scheme Company B provides Company A with services for which it is remunerated in cash. Company B sends money for fictitious goods and services to foreign Company D and receives documents to support a tax deduction. Company A sells securities to Company C which in turn sells these to company D, the funds for which are remitted to Company A. Company D then sells the securities on the open market.

- ***Combined scheme***

202. If the three abovementioned schemes are combined, the criminals' organisation can minimise the number of transactions involved, saving on transaction costs and minimising the risk of detection of suspicious transactions.



203. In this combined scheme the use of bank services is minimised. Because of combining opposite cash flows (cash for smuggled goods gets in, unaccounted cash – out) there is no need to deposit/withdraw cash from accounts. Also money flows on accounts also go in opposite directions, so actual transfers can be done only for "balancing" payments.

5 CORRUPTION

204. Securities transactions can be utilised to make payments to corrupt officials and politically exposed persons. Securities transactions are particularly useful for payments to support corruption as:

- Significant sums of money are frequently involved with the problem of supplying an adequate explanation for the source of the funds. In many countries officials are required to provide an explanation for all sources of income. Due to the volatile nature of securities transactions dealing in securities can provide a suitable reason for significant cash flows.

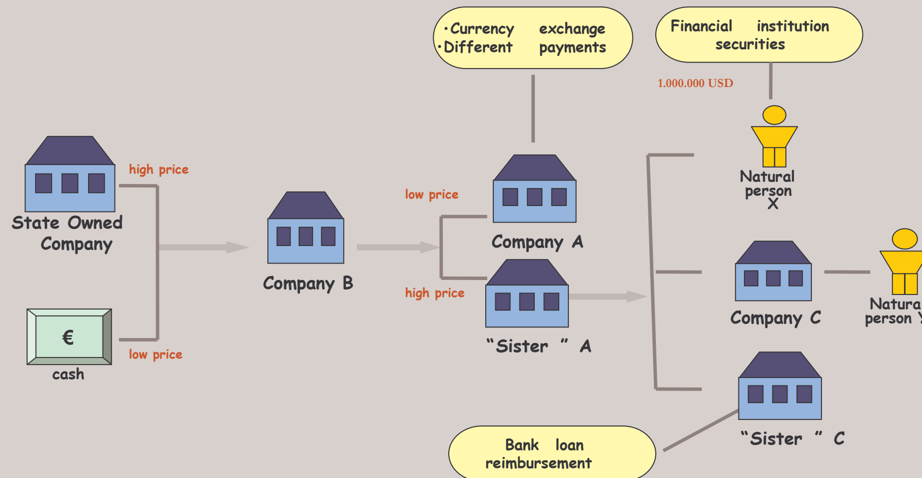
- Insider information may be supplied to PEPs as a means of rewarding them for services supplied.

- Transferring bearer securities which can either be sold or deposited as collateral for a loan or selling securities at off-market prices to PEPs represents a means of remunerating PEPs for corrupt services without leaving a cash-based audit trail.

Example
During a regular supervision visit it was discovered that a natural person, who was suspected of having been involved in criminal activities (including accepting bribes), had invested a considerable amount of money (€165,000) into acquiring shares. As these investments were not in line with his remuneration or lifestyle, supervisory agency contacted the FIU about its findings.
Source: Croatia

Example

A financial institution submitted a suspicious activity report concerning transactions in real estate where there was a significant difference between prices in successive real estate transactions.
The proceeds from these transactions was (in part) transferred to a financial institution and used to purchase securities. The transfer didn't raise any suspicions at the bank, as securities transactions were frequently made by business entities with surplus funds. The amount of money involved was US$1,000,000.
The methodology was that company A sold real estate properties at an agreed price to company B (the managers of the two companies were in collision). The next day company B sold the same properties to a state-owned company at price 5 times the purchase price. The original purchase price was significantly under-stated to avoid tax on the profit arising from the sale. The agreed sale price was over-stated in order to defraud the state-owned company. Company B was a shell company.
After receiving the sale proceeds from the state-owned company the following cashflow was identified:
- A sister company of A was incorporated by the same natural person that incorporated A, respectively Natural Person Y.
- Company C and a sister company of C were incorporated by the father of Natural person X.



Source: Romania

6 ORGANISED CRIME

205. With few exceptions, serious organised criminal activity is directly or indirectly concerned with making money. Most serious organised criminals, especially the more established and successful ones, are involved in more than one type of criminal activity. Serious organised criminals have an excellent and dynamic understanding of criminal markets and are quick to respond to threats from law enforcement measures or rivals and to seize and create money-making opportunities.

206. Profitability alone cannot explain the choices serious organised criminals make. They also look to manage risk by threatening and using violence; by transferring 'hands-on' risks to lower-level criminals or dupes; by corrupting law enforcement officers and others involved in the criminal justice process; and by using professionals to handle their affairs, especially to launder their criminal proceeds.

207. Most serious organised criminal activities require some measure of criminal collaboration and infrastructure, and this lies behind the formation of organised crime groups and networks. A wide range of structures exists. Some serious organised criminals belong to established groups with clear hierarchies and defined roles, but many are part of looser criminal networks and collaborate as necessary to carry out particular criminal ventures.

208. Serious organised criminals make use of 'specialists' who provide a service, often to a range of criminal groups. Services include transportation, money laundering, or the provision of false documentation (identity fraud underpins a wide variety of serious organised criminal activities). Various moneymaking activities have been facilitated through corrupt relationships with public and private sector employees, accountants and others in the financial field, plus a range of other professionals.

209. Cash remains a mainstay of serious organised criminal transactions. It has the obvious advantage that it leaves no audit trail, and is the most reliable form of payment as well as the most flexible. The initial stage of money laundering often involves moving cash out of the country in which criminal activities are being conducted through couriers or via various money transmission services. However, many serious organised criminals make use of financial and legal professionals to handle their financial affairs. This often involves using asset purchases (including securities) and legitimate or quasi-legitimate businesses, typically those with a high cash turnover, to launder criminal proceeds as well as to provide cover for the purchase, delivery and sale of illicit goods.

210. Serious organised criminals make use of the proceeds of crime in a number of ways:

- Pay local costs resulting from criminal activities, including payments to corrupt officials and criminal associates.
- Reinvest in further criminal activities, for example payments to bribe "insiders" in targeted organisations.
- Transfer funds abroad to pay for goods and services, such as counterfeit goods and drugs shipments, or merely to frustrate confiscation by law enforcement agencies.
- Invest in "legitimate" investments including securities and real estate in order to legitimise the proceeds of crime.
- Fund lifestyle.

7 CAPITAL FLIGHT

211. Capital flight occurs when both individuals and businesses attempt to transfer money and other assets to another country. This may be caused by concern about high taxes, economic instability, low level of investment opportunity etc. Such money and assets may have a legitimate origin although it is noted that a number of countries operate strict controls on the transfer of funds and assets abroad. In such circumstances, although the funds may be legitimately acquired, the act of

transferring them abroad, in contravention of restrictions on movement of funds, would constitute a criminal act.

212. Securities transactions have been utilized as a means of moving money to another country, in contravention of restrictions on movement of funds. The methodology which has been most regularly observed is the purchase and sale of securities at off-market prices. In this methodology, a person based in a foreign country purchases shares which have a low nominal value and then sells them to a connected person in the host country at a significantly inflated. The person in the host country then either holds the shares or sells the shares at market value thus realizing a loss (which may also be used to reduce their tax liability). Offshore companies in low-tax jurisdiction are frequently used for such schemes.

213. Similar schemes have been noted using savings certificates and bills of exchange to support capital flight transactions.

RED FLAGS & INDICATORS

214. The following warning red flags and indicators have been drawn from a number of sources. Many of these indicators may be found at various stages of the dealing cycle.

215. This list is not exclusive to the securities sector and similar indicators may be observed in other areas of the financial services industry. This list reflects current experiences and observations. It is not exhaustive and other methodologies may from time to time emerge.

216. The incidence of one or more of these warning signs will give an indication that the individual or organisation is acting in an abnormal manner. This does not necessarily mean that they are involved in money laundering or any other type of crime. It will, however, indicate that further investigation or enquiry should be undertaken.

1 WARNING SIGNS AT THE ACCOUNT OPENING STAGE

- The customer exhibits unusual concern regarding the firm's compliance with government reporting requirements and the firm's anti-money laundering policies, particularly with respect to his or her identity, type of business and assets, or is reluctant or refuses to reveal any information concerning business activities, or furnishes unusual or suspect identification or business documents.
- The information provided by the customer that identifies a legitimate source for funds is false, misleading, or substantially incorrect.
- Upon request, the customer refuses to identify or fails to indicate any legitimate source for his or her funds and other assets.
- The customer (or a person publicly associated with the customer) has a questionable background or is the subject of news reports indicating possible criminal, civil, or regulatory violations.
- The customer is an individual who has, or has had, a high political profile, or holds, or has held public office. This risk also extends to members of their immediate families and to known close associates.
- The customer is from, or has accounts in, a country identified as a country or territory that does not sufficiently comply with the Financial Action Task Force 40 plus 9 Recommendations or has a reputation for operating as a haven for criminal assets.
- The customer appears to be acting as an agent for an undisclosed principal, but declines or is reluctant, without legitimate commercial reasons, to provide information or is otherwise evasive regarding that person or entity.
- The customer has difficulty describing the nature of his or her business or lacks general knowledge of his or her industry.
- The customer maintains multiple accounts, or maintains accounts in the names of family members or corporate entities, for no apparent business purpose or other purpose.
- A wholesale customer who is unprofessional or naive in their approach to account opening.
- A wholesale customer who appears inexperienced in the wholesale markets and who does not have a proven track record.

2 WARNING SIGNS REGARDING FUNDS FOR INVESTMENT

- The customer attempts to make frequent or large deposits of currency.
- The customer settles in cash close to or at the settlement deadline.
- The customer insists on dealing only in cash equivalents, or asks for exemptions from the firm's policies relating to the deposit of cash and cash equivalents

- The customer deposits amounts of cash, below the mandatory reporting level, at various branches of the financial institution.
- The customer's account shows numerous currency or cashiers check transactions aggregating to significant sums.
- The customer's account has unexplained or sudden extensive electronic transfer activity, especially in accounts that had little or no previous activity.
- The customer's account has inflows of funds or other assets well beyond the known income or resources of the customer.
- Regular transfers of securities for sale from another securities company's account.

2.1 Warning signs when executing transactions

- The customer wishes to engage in transactions that lack business sense or apparent investment strategy, or are inconsistent with the customer's stated business strategy.
- The customer exhibits a lack of concern regarding risks, commissions, or other transaction costs.
- The customer attempts to make frequent or large deposits of currency, insists on dealing only in cash equivalents, or asks for exemptions from the firm's policies relating to the deposit of cash and cash equivalents.
- The customer engages in transactions involving cash or cash equivalents or other monetary instruments that appear to be structured to avoid the mandatory reporting requirements, especially if the cash or monetary instruments are in an amount just below reporting or recording thresholds.
- The customer requests that a transaction be processed in such a manner to avoid the firm's normal documentation requirements.
- The customer, for no apparent reason or in conjunction with other "triggers", engages in transactions involving certain types of securities, such as penny securities and bearer bonds, which although legitimate, have been used in connection with fraudulent schemes and money laundering activity.
- The customer's account shows an unexplained high level of account activity with very low levels of securities transactions.
- Corresponding sales and purchases on linked accounts.

2.2 Warning signs when settling transactions

- For no apparent reason, the customer has multiple accounts under a single name or multiple names, with a large number of inter-account or third-party transfers.
- Regular deposits and withdrawals of funds without or with minimal dealing activity on the account
- The customer's account has unexplained or sudden extensive electronic transfer activity, especially in accounts that had little or no previous activity.
- The customer's account has a large number of electronic transfers to unrelated third parties inconsistent with the customer's legitimate business purpose.
- The customer's account has electronic transfers that have no apparent business purpose to or from a country identified as a money laundering risk or a bank secrecy haven.
- The customer's account indicates large or frequent electronic transfers, immediately withdrawn from the account without any apparent business purpose.
- The customer makes a funds deposit followed by an immediate request that the money be wired out or transferred to a third party, or to another firm, without any apparent business purpose.

- The customer makes a funds deposit for the purpose of purchasing a long-term investment followed shortly thereafter by a request to liquidate the position and transfer of the proceeds out of the account.
- The customer engages in transfers between unrelated accounts without any apparent business purpose.
- Regular transfers of securities to another securities company's account following execution and settlement of transaction.

2.3 Warning signs relating to fictitious companies

- The absence of information on any legitimate activities of the company as a business entity (in the country of registration);
- Difficulty in define physical location of the staff and/or directors (proxies, representatives) or the type of activity of the company;
- Difficulty in obtaining identification information concerning directors, controllers and key members of staff;
- Inconsistency between the company's stated turnover in the statutory accounts and the amount of tax paid;
- One person combining the functions of the founder, chairman, chief executive/managing director and finance director;
- Registration of many companies by one person or at the same address;
- Registration of the organisation using lost or stolen passports
- Conclusion of insubstantial agreements by the company, which do not contain information on goods classification or list of services, terms of their execution and appropriate measures for non-performance or undue performance of the obligations.

FINANCIAL ANALYSIS AND INVESTIGATION TECHNIQUES

217. Traditionally, the investigation of instances of money laundering follows two routes:

- Following the audit trail of the proceeds of a specific crime
- Following the audit trail from a suspicious transaction report to establish the underlying predicate offence.

218. In the first case the FIU will receive reports from law enforcement agencies on specific crimes or on the activity of criminals and will need to have the analytic tools and data to identify all transactions related to the case.

219. In the second case the main problem is receive adequate information in the form of suspicious transaction reports and then to identify the underlying predicate offence. This can be achieved in two ways:

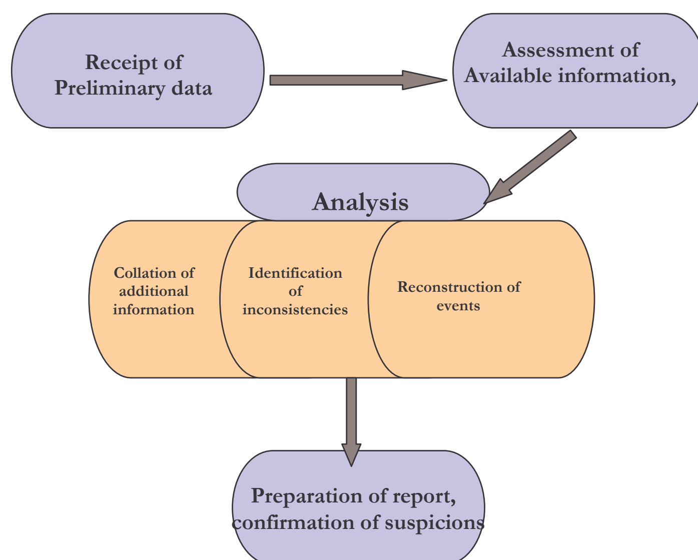
- A securities dealer identifies a suspicious transaction based on client due diligence or transaction monitoring and submits a suspicious transaction report;
- FIU or supervisor detects suspicious activity based on analysis of large number of threshold reports.

1 STAGES OF FINANCIAL ANALYSIS

220. The procedures adopted for the investigation of money laundering transactions in the securities market are similar those adopted for other criminal investigations.

221. The main stages for financial analysis are set out below:

1. Receipt of preliminary data;
2. Assessment of available information;
3. Analysis per se:
    3.1 collation of additional information;
    3.2 identification of inconsistencies;
    3.3 reconstruction of events and identification of perpetrators;
4. Preparation of report and confirmation of suspicions.



222. Each of the above stages of financial analysis will now be considered in detail, emphasizing specific features which are relevant to securities transactions.

1.1 Receipt of preliminary data

223. The main sources of preliminary data are:

- reports and intelligence received from state authorities which regulate and supervise the securities market and its participants;
- reports received direct from securities exchanges;
- suspicious transaction reports received from the participants in the securities market or from other financial institutions including banks and fund managers (reporting entities).

224. At this stage the receipt of reports on large transactions on the securities market by the FIU is useful. It is possible to receive such information through a requirement to report all transaction above a predetermined size or through obligatory reporting of specific types of transactions (e.g. the purchase of securities for cash).

225. It is also important that the FIU maintains a database of information including intelligence received from regulators, security exchanges and law enforcement agencies. The FIU should also have access to the databases of regulatory bodies and law enforcement agencies as well as having the ability of require that information be provided by financial institutions if required. The FIU should be able to identify who the underlying client is for specific transactions and search for additional transactions by that client.

Example

The Surveillance and Analysis Department of the CySEC is directly connected with the Securities Exchange's trading system. This allows for the continuous collection and analysis of trading information. Monitoring of trading is done daily and in real-time.
This market surveillance program:
a) processes and analyses the data received by the real-time database;
b) adds historical data to real-time database for analysis purposes;
c) sets different parameters per title or per group of titles; and
d) produces alerts and prepares alert reports.
The Surveillance and Analysis Department is also connected with the Central Depository and Central Registry of the Securities Exchange. This provides instant access to the identities of all investors. In the event of unusual and potentially improper trading, the CySEC contacts the Internal Auditor of the market intermediary and asks for explanations.

Source: Cyprus

226. The receipt of suspicious transaction reports is vital for the identification and monitoring of money laundering transactions. In order to facilitate the prompt identification of transactions which require further investigation it is important to ensure that the report contains sufficient information to ensure that time and resource is not wasted. The minimum information requirements to be included in an STR are set out below.

Elements in a Suspicious Transaction Report
Reporting entity
Name
Address
Telephone
Email address
Person to contact for further assistance
Subject details (individual)
Family name
Given name
Alias or nickname
Occupation
Date of Birth
Gender
Passport number
Other official document (e.g. identity card, tax reference number, etc.)
Address
Telephone
Email address
Subject details (legal person)
Name
Business name (if different from legal name)
Address
Telephone
Email address
Website
Registration number
Tax registration number
Country of registration
Type of business
Description of the transaction
Nominal value,
Date,
Method of payment (cash, internet banking, bank order etc.), and in case of bank payment, bank name
Type of securities subject of the reported transaction
Other operations performed by the subject (natural or legal) in the last 6-12 months
Reason for disclosure

1.2 Assessment of available information

227. Suspicious transactions may be identified by:

- analysis of one separate transaction which has been highlighted (e.g. through red flags, cross reference to black lists, etc.);
- information received either through STRs or intelligence reports. Such information could include suspicious behavior of client, investment activity which is inconsistent with the profile of the customer, provision of documents that appear to be forged or cloned, etc.;
- analysis of aggregated transactions: this may result form the analysis of a number of small and apparently inconsequential transactions, which when considered together, indicate a systemic attempt to launder money (e.g. smurfing through a number of financial institutions).

1.3 Analysis

Reconstruction of events and identification of perpetrators

228. It is important that FIUs have the facility to analyze significant volumes of information in order to form a judgment on the merits of a specific case. Once the initial analysis has been completed it may be necessary to reconstruct the series of transactions. To facilitate this analysis, the application of specific analytical software is useful in this process.

Example
The software used by the FIU allows it to rapidly analyze information stored on its database and to represent this information as a diagram. This diagram identifies the interrelationships between different subjects of the investigation. All elements of the stored data are reflected graphically and are built as diagrams that show both the subjects and relationships, that exist between them. The user then has the possibility to conduct a more detailed search of particular subjects, tracing the transactional history of connections identifies.
The software provides the functionality to :
- identify connections between specific persons, bank accounts, property and other types of subjects;
- create diagrams, which can contain large volume of data and connections among bank accounts and transactions.

Source: Ukraine

229. Initially, the analysis will seek to identify the facts of a case on the balance of possibilities in particular trying to identify the main participants and the underlying structure of the relevant transactions. It is noted that criminals frequently arrange a large number of securities transactions at the layering stage with the purpose of complicate the investigation and disguising the final destination of the laundered funds. It is therefore important to:

- identify the main participants in a series of transactions; and
- calculate their result (profit/loss) for the period analyzed.

230. This may help to identify the sources of funds and their destination, particularly where funds are at the final stage of integration into the financial system as legalised funds. Such method also provides the FIU with the opportunity to handle the situation which is frequently observed in securities market transactions of commingling both clean and dirty funds in transactions.

Collation of additional information

231. Once an investigation has been commenced further information that is required will be identified. It is therefore extremely important that the FIU has access to additional sources of information and that these are readily available.

232. The FIU will need to have access to information held by:

- financial services regulators;
- depositaries, custodians, registrars, securities exchanges and other financial institutions; and
- law enforcement agencies and other state authorities.

233. In addition it is noted that securities are actively used in the process of laundering through cross-border transactions. It is therefore important to develop arrangements for information from foreign FIUs.

Example
The FIU of Bosnia and Herzegovina has identified that the most important elements of information concerned details of buyers/sellers of securities, transaction details, details of foreign citizens who are dealing in securities and details of companies which have shares traded on the securities market. The most valuable sources of information were professional participants on the securities market (professional intermediaries, Registers of Securities, securities dealers and banks) and in addition, from law enforcement agencies.
Source: Bosnia and Herzegovina

Identification of inconsistencies

234. Information from regulators has proved to be particularly valuable when investigating studying of cases. The experience and technical expertise available can help to reveal and substantiate the criminal nature of transactions or identify the methodology underlying the transactions under investigation.

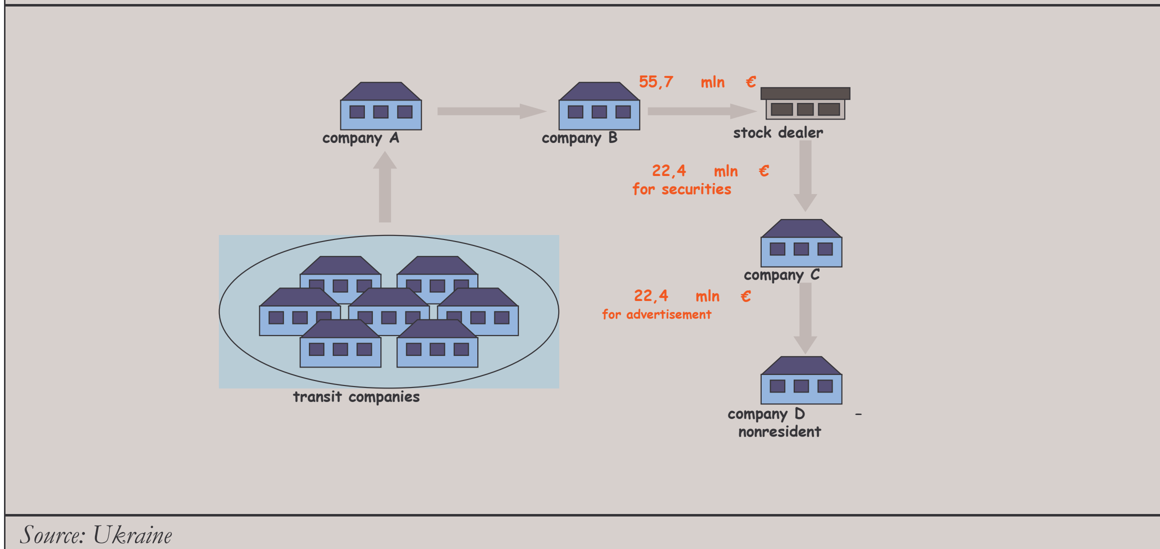
235. For example, such expertise is particularly valuable when investigating the laundering of criminal funds using securities transactions at off-market prices. In such schemes shell companies issues securities whose apparent market value is not backed up by the value of the underlying assets. Such share issues, which are normally conducted in accordance with the listing rules of the relevant securities market, are frequently used to facilitate money laundering transactions.

Example
1. The FIU received a report from a financial institution on a transaction which involved the securities dealer transferring €22.4 million to the foreign account of company C in European Country Z in order to conduct securities transactions.

2. The FIU analyzed the transaction against its database.
As a result of this analysis, the following chain of transactions was identified;
A number of transit companies had transferred significant sums of money in favor of company A. In its turn, company A had transferred €55.7 million in favor of a securities dealer through company B. Following on from this, €22.4 million was transferred in favor of company C to fund the purchase of securities. After the sale of the securities, company C paid €22.4 million to a non-resident company for "advertising services".
A search of the database of the FIU revealed the following information:
Resident company C was registered in small village. The company's statutory fund was only €176. The FIU prepared a report on this case. It was, however, concluded that in order to identify the complete scheme and to prove suspicions of money laundering, more information was required.

3. The FIU then sent a request for additional information to the reporting bank and to the FIU of European Country Z.
As a result of these requests, the following information was received.
The bank reported that:
In pursuance to the contract, company D from American Country W placed advertisements on international TV channels operated by company C (these arrangements appeared unusual for such a small company).

The director concerned from company C was not authorised to sign contracts.
The relevant bank account was opened within 14 days of the signing of the contract.
The FIU of European Country Z reported that:
Company D was not involved in advertising activity.
- On the day after the receipt of the funds, company D transferred funds to the accounts of 4 foreign companies.
- All the accounts of the foreign companies were opened at the same bank in European Country Z.
4. As a result of this analysis, the case was transferred to the law enforcement agency which had originally referred the case to the FIU.



Source: Ukraine

1.4 Preparation of report, confirmation of suspicions

236. Once the initial suspicions concerning the case have been identifies, the FIU would normally submit its findings and conclusions to the relevant law enforcement agencies.

237. Taking into account the complexity of money laundering transactions involving securities and in particular the large volume of information available concerning transactions, connections, etc. it is important that :

- law enforcement agencies have appropriate software for processing such volumes of information; and
- FIUs provide law enforcement authorities with graphical and diagrammatic representations of the relevant schemes of money laundering transactions.

Number of reports concerning money laundering utilising securities transactions, referred by FIUs to law enforcement authorities:

FIU/ Country	Period	Number of reports
Croatia	2006-2007	4
Malta	2006	1
Estonia	2006	2
Lithuania	2006	14
Poland	2006	16
Ukraine	2006	16
Bulgaria	2006	1

2 INVESTIGATION OF CASES BY LAW ENFORCEMENT AUTHORITIES

238. In money laundering investigations, it is essential to identify and prove the link between the underlying predicate offence and the assets of the criminals under investigation. This is particularly important where criminal funds are commingled with legitimate funds. It is therefore important to clearly identify those funds which have been derived from criminal activity.

239. In conducting investigations of money laundering cases, it may be necessary to utilise both overt and covert intelligence activities. With regard to covert intelligence activities these may include the use of special investigation means such as informants, whistleblowers etc.)

240. The commingling of legally and illegally acquired funds has presents serious difficulties in combating money laundering on the securities market. It is therefore important to utilise specialist software that facilitates the processing of large data volumes.

241. Direct proof of the illegal origin of assets obtained on securities market may become difficult in some cases and reversed burden of proof may fail in case of securities market because laundering schemes with overpriced securities may provide justification for profits obtained.

242. A number of countries utilise provisions that allow the confiscation of assets of value equal to the profits gained from crime until such time as the legitimate source of funds can be proved.

3 CO-OPERATION BETWEEN STATE AGENCIES

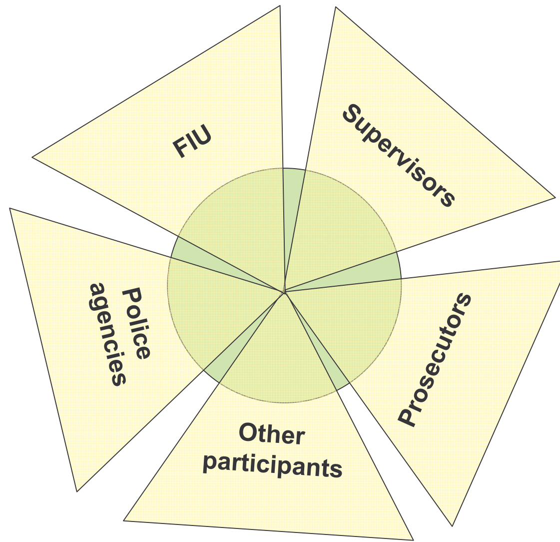
243. It is important that national legislation allows the exchange of information between law enforcement agencies, regulatory bodies and government departments where there are criminal or regulatory investigations taking place. If there are prohibitions on the exchange of such information then legislation should be introduced to remove such prohibitions. Depending on national legislation it may be necessary to implement a system of memorandum of understanding between the relevant organisations.

244. Such co-operation is important as individual agency may be considering one part of a criminal conspiracy relating to money laundering. It is only when all aspects of an investigation are considered together that the complete scheme of money laundering and related predicate offences can be appreciated.

245. It is therefore important that all law enforcement agencies and regulatory bodies within a jurisdiction are aware of any substantial investigations that are being conducted and that a mechanism exists for the sharing of relevant information.

246. It is useful to designate single points of contact with each law enforcement agency, regulatory body and government department who would be the recipient of any request for information. This will provide a number of benefits including ensuring that:

- the data requests to facilitate investigations are distributed effectively among the relevant agencies;
- The most appropriate enforcement powers (administrative, financial and criminal) are utilised to disrupt and prosecute the criminal groups under investigation. In this respect it is noted that in some circumstances the application of civil powers to remove authorisation to conduct business can be as effective a deterrent to crime as the application of criminal powers;
- Specialist skills and knowledge available properly utilised during an investigation.



Example of centralised coordination of exchange of information on economic crime

Example

For example, in the FSA of the United Kingdom there is a dedicated unit which coordinates the exchange of information on economic crime between over 100 law enforcement agencies, regulatory bodies and government departments and arranges meetings to discuss how to progress investigations making best use of the resources and legal powers available. This unit also maintains up-to-date details of all single points of contact.

In the Netherlands, the Financial Expertise Centre (FEC) is a cooperative effort between various investigative and enforcement agencies. The FEC comprises all the organisations with responsibilities relating to the financial sector including supervisory authorities, control, intelligence, and investigative institutions as well as prosecution authorities. These arrangements are the subject of an agreement together with related explanatory notes. The following bodies are members of the FEC:

- General Intelligence and Security Service (AIVD),
- Authority for the Financial Markets (AFM),
- Tax and Customs Administration,
- Central Bank (DNB),
- Fiscal Intelligence and Investigation Service-Economic Inspection and Investigation Service (FIOD-ECD),
- National Police Services Agency (KLPD),
- Public Prosecution Service (OM),
- Amsterdam-Amstelland Police Force.

4 SPECIALIST ASSISTANCE

247. One of the problems that hinders the effective investigation of money laundering offences involving securities transactions is the complexity of the transaction structures and underlying financial instruments. Frequently understanding such transactions requires technical expertise which is not available internally within the investigating body.

248. It is therefore important that FIUs and law enforcement agencies may consider the possibility of:

- specialisation of some employees in financial transactions;
- creation of separate subdivision which specialise in the investigation of complex financial transactions;
- allow the temporary transfer of experienced staff from financial institutions to provide technical assistance.

249. In order to solve this problem, in some jurisdictions, legislation does permit the hiring of specialists to work with law enforcement agencies.

Example
In Romania, within the Department for Investigating Organised Crime and Terrorism there are specialists with specific qualifications in the field of database processing, economics, finance, banking, customs, IT, capital markets, and other disciplines, for clarifying technical aspects in criminal investigations.
These specialists are appointed by order of the General Prosecutor attached to the High Court of Cassation and Justice at the proposal of the Chief Prosecutor of the Department for Investigating Organised Crime and Terrorism.
The specialists have the powers of public servants and carry out their activity within the central structure. The technically-scientific findings carried out by the specialists in accordance with written dispositions of the prosecutor may constitute evidence in accordance with the law. Investigations also may be carried out by other specialists or experts within public or private Romanian or foreign institutions, organised according to the law, as well by individual specialists or experts authorised or recognised according to the law.

5 FEEDBACK

250. The problem of FIUs providing relevant feedback to reporting entities on the relevance and outcome of STRs is an issue in almost all MONEYVAL member states.

251. In most countries it is the case that FIUs are prohibited from disclosing any information related to AML reports and analysis performed in their activity, except in certain prescribed circumstances, normally to law enforcement agencies and other FIUs.

252. It is, however, important that reporting entities receive some form of feedback from FIUs in order to improve the quality of reporting on AML/CFT activities. In this situation, where information on specific cases cannot be provided to reporting entities, other means of providing feedback need to be utilised. Such methods can include training programmes using sanitised case studies, regular publication of typologies and statistical reports.

253. Training on best practices can include presenting examples of correctly completed STRs, where all the important aspects of the case were revealed by the securities companies and included in the report. Also training should contain examples of incorrectly completed STRs where irrelevant details were included or important aspects of the case were ignored.

254. Another form of feedback provided by the FIU to securities companies could consist of money laundering typologies of cases related to capital market. The typologies could refer to money laundering using securities, laundering criminal proceeds initially received in the form of securities or any other forms of laundering related to capital market.

ABBREVIATIONS

AML	anti-money laundering
CDD	customer due diligence
CDO	collateralised debt obligation
CFT	combating the financing of terrorism
ETF	Exchange Traded Fund
EU	European Union
FX	Foreign exchange
ExO	execution-only
FATF	Financial Action Task Force
FIU	financial intelligence unit
IOSCO	International Organisation of Securities Commissions
IPO	initial public offering
MBS	mortgage-backed security
ML	money laundering
MTF	Multilateral Trading Facilities
OTC	'over-the-counter'
PEP	politically exposed person
SPV	special purpose vehicle
STR	Suspicious Transaction Report
VAT	Value added tax

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- The International Organisation of Securities Commissions http://www.iosco.org/

- Committee of European Securities Regulators http://www.cesr.eu/

GLOSSARY

asset-backed security	a type of bond or note that is based on pools of assets, or collateralised by the cash flows from a specified pool of underlying assets.
bearer bond	bond payable to holder; a bond payable only to the party that presents it
bearer securities	securities instruments in bearer form consist of bearer bonds and bearer securities certificates or "bearer shares". As with registered securities, both of these instruments are issued by a particular corporate entity in order to raise capital.
bill of exchange	an unconditional order issued by a person or business which directs the recipient to pay a fixed sum of money to a third party at a future date. The future date may be either fixed or negotiable. A bill of exchange must be in writing and signed and dated.
"black" company	criminal controlled company which may be registered using lost or stolen passports, passports of dead persons, homeless persons or mercenaries. The company is generally established for a short period of time and doesn't maintain proper books and records of account or account for taxes.
Bond	a security, in which the authorized issuer owes the holders a debt and is obliged to repay the principal and interest (the coupon) at a later date, termed maturity.
bond market (or the debt, credit, fixed income market)	a financial market where participants buy and sell debt securities, usually in the form of bonds.
"buffer" company	criminal controlled company created for consolidation of mechanism of money laundering or other criminal schemes. It is a false but "clean" company that participates in the schemes as an intermediary.
closed-ended investment fund	issues a limited number of shares (or units) in an initial public offering (or IPO). The shares are then traded on an exchange or directly through the fund manager to create a secondary market subject to market forces. If demand for the shares is high they may trade at a premium to net asset value. If demand is low they may trade at a discount to net asset value. Further share (or unit) offerings may be made by the scheme if demand is high although this may affect the share price.
collateralised debt obligations (CDOs)	a type of asset-backed security and structured credit product. CDOs gain exposure to the credit of a portfolio of fixed-income assets and divide the credit risk among different tranches: senior tranches (rated AAA), mezzanine tranches (AA to BB), and equity tranches (unrated).
corporate bond	a bond issued by a corporation. The term is usually applied to longer-term debt instruments, generally with a maturity date falling at least a year after their issue date.
Counterparty	a party to a contract. A counterparty is usually the entity with whom one negotiates on a given agreement, and the term can refer to either party or both, depending on context.

Coupon	the amount of interest paid per year expressed as a percentage of the face value of a bond.
credit derivative	a financial instrument or derivative whose price and value derives from the creditworthiness of the obligations of a third party, which is isolated and traded. Credit derivatives in their simplest form are bilateral contracts between a buyer and seller under which the seller sells protection against certain pre-agreed events occurring in relation to a third party (usually a corporate or sovereign) known as a reference entity; which affect the creditworthiness of that reference entity.
criminal controlled companies	use by criminals for illegal purposes, i.e. ML. The main types are: "black", "grey" and "buffer".
Debt security	see bond above
derivatives markets	the financial markets for derivatives. The market can be divided into two, that for exchange traded derivatives and that for over-the-counter derivatives. The legal nature of these products is very different as well as the way they are traded, though many market participants are active in both.
domiciled bill	a third party specified in a bill as the one obliged to pay the bill at the payer's place of residence (domicile) or in other specified place.
Electronic trading systems	a method of trading securities, foreign currency, and exchange traded derivatives electronically. It uses information technology to bring together buyers and sellers through electronic media to create a virtual market place.
Exchange-traded fund (or ETF)	an investment vehicle traded on stock exchanges, much like stocks. An ETF holds assets such as stocks or bonds and trades at approximately the same price as the net asset value of its underlying assets over the course of the trading day.
exchange-traded products	financial products that are traded on exchanges, which have standardised terms (e.g. amounts, delivery dates and terms) and settlement procedures and transparent pricing.
execution-only (ExO) securities companies	Carry out transactions in securities with regulated market counterparties, as agent for individual customers. ExO transactions are carried out only on the instructions of the customer.
Feeder fund	a structure which allows asset managers to capture the efficiencies of larger pools of assets, although fashioning investment funds to separate market niches. One or more investment vehicles pool their portfolio within another vehicle; there are normally several smaller feeders and one master to which they contribute.
financial market	a mechanism that allows people to easily buy and sell (trade) financial securities (such as securities and bonds), commodities (such as precious metals or agricultural goods), and other fungible items of value at low transaction costs and at prices that reflect the efficient market hypothesis.
forward contract	an agreement between two parties to buy or sell an asset (which can be of any kind) at a pre-agreed future point in time. The trade date and delivery date are separated. It is used to control and hedge risk (for example, currency exposure risk or commodity prices).

futures contract (or futures)	exchange traded derivatives; a standardised contract, traded on a futures exchange, to buy or sell a certain underlying instrument at a certain date in the future, at a specified price.
futures exchange	a central financial exchange where people can trade standardised futures contracts; that is, a contract to buy specific quantities of a commodity or financial instrument at a specified price with delivery set at a specified time in the future.
“grey” company	criminal controlled company which may be created to execute several transactions. Such company may have a dummy director and regularly provide reports to tax authorities and have invoices for illegal products.
government bond	a bond issued by a national government denominated in the country's own currency. Bonds issued by national governments in foreign currencies are normally referred to as sovereign bonds
hedge fund	a private investment fund charging a performance fee and typically open to only a limited range of qualified investors. As a hedge fund's investment activities are limited only by the contracts governing the particular fund, it can make greater use of complex investment strategies such as short selling, entering into futures, swaps and other derivative contracts and leverage.
high yield bond (non-investment grade bond, speculative grade bond or junk bond)	a bond that is rated below investment grade at the time of purchase. These bonds have a higher risk of default or other adverse credit events, but typically pay higher yields than better quality bonds in order to make them attractive to investors.
hybrid securities (or "hybrids")	a broad group of securities that combine the elements of the two broader groups of securities, debt and equity. Hybrid securities pay a predictable (fixed or floating) rate of return or dividend until a certain date, at which point the holder has a number of options including converting the securities into the underlying share.
institutional funds	authorised and unauthorised collective investment schemes and unitised life assurance funds that are dedicated to investment by institutional investors.
investment management	includes both discretionary and advisory management of segregated portfolios of assets (securities, derivatives, cash, property etc.) for the firm's customers.
investment trusts	are companies that invest in the shares of other companies for the purpose of acting as a collective investment. Investors' money is pooled together from the sale of a fixed number of shares which a trust issues when it launches. Investment trusts are traded on securities exchanges like other public companies.
market manipulation	a deliberate attempt to interfere with the free and fair operation of the market and create artificial, false or misleading appearances with respect to the price of, or market for, a stock. Examples of market manipulation - price manipulation, “marking the close”, wash trades and pre-arranged trading etc.
Margin	collateral that the holder of a position in securities, options, or futures contracts has to deposit to cover the credit risk of a counterparty.

mortgage-backed security (MBS)	an asset-backed security whose cash flows are backed by the principal and interest payments of a set of mortgage loans. Payments are typically made monthly over the lifetime of the underlying loans.
municipal bond	a bond issued by a state, city or other local government, or their agencies. Potential issuers of municipal bonds include cities, counties, redevelopment agencies, school districts, publicly owned airports and seaports, and any other governmental entity (or group of governments) below the state level.
open-ended investment fund	equitably divided into shares which vary in price in direct proportion to the variation in value of the funds net asset value. Each time money is invested, new shares or units are created to match the prevailing share price; each time shares are redeemed the assets sold match the prevailing share price. In this way there is no supply or demand created for shares and they remain a direct reflection of the underlying assets.
Option premium	the price the buyer of the options contract pays for the right to buy or sell a security at a specified price in the future.
options	financial instruments that convey the right, but not the obligation, to engage in a future transaction on some underlying security.
OTC products	bilateral agreements between two parties, or multilateral, depending on the settlement process, that are not traded or executed on an exchange.
over-the-counter (OTC) trading	trading with financial instruments such as securities, bonds, commodities or derivatives directly between two parties. It is contrasted with exchange trading, which occurs via corporate-owned facilities constructed for the purpose of trading (i.e., exchanges), such as futures exchanges or securities exchanges. OTC consist of investment banks who have traders who make markets in these derivatives, and clients such as hedge funds, commercial banks, government sponsored enterprises, etc.
participants in the securities market	range from small individual securities investors to large hedge fund traders, who can be based anywhere. Their orders usually end up with a professional at a securities exchange, who executes the order.
preferred stock (or preferred shares, preference shares)	is typically a higher ranking security than common stock, and its terms are negotiated between the corporation and the investor. They may or may not carry voting rights, and may have superior voting rights to common stock. They may carry a dividend that is paid out prior to any dividends to common stock holders. Preferred stock may have a convertibility feature into common stock.
retail investment funds	authorised unit trusts and open-ended investment companies (oeics).
retail securities market	includes wealth management, financial advisers, non-life providers of investment fund products, discretionary and advisory investment management and execution-only securities companies.
securities company	An organisation that buys and sells securities on behalf of investors. May also be known as a stock broker or securities trading company

securities derivative	any financial claim which has a value that is dependent on the price of the underlying securities. Futures and options are the main types of derivatives on securities.
securities exchange	an organisation that provides a marketplace for either physical or virtual trading shares, bonds and warrants and other financial products where investors (represented by securities companies) may buy and sell shares of a wide range of companies. A company will usually list its shares by meeting and maintaining the listing requirements of a particular securities exchange and the different. May also be known as a stock exchange
securities futures	contracts where the buyer, or long, takes on the obligation to buy on the contract maturity date, and the seller, or short takes on the obligation to sell. Securities index futures are generally not delivered in the usual manner, but by cash settlement.
securities option	a class of option. Specifically, a call option is the right (not obligation) to buy securities in the future at a fixed price and a put option is the right (not obligation) to sell securities in the future at a fixed price.
securities markets	organised exchanges plus over-the-counter markets in which securities are traded. Securities market refers to the system that enables the trading of company securities (collective shares), other securities, and derivatives. Bonds are still traditionally traded in an informal, over-the-counter market known as the bond market. Commodities are traded in commodities markets, and derivatives are traded in a variety of markets (but, like bonds, mostly 'over-the-counter').
securitisation transaction	the process of creating new financial instruments by pooling and combining existing financial assets, which are then marketed to investors.
Special purpose vehicle	a body corporate created to fulfill narrow, specific or temporary objectives, primarily to isolate financial risk, usually bankruptcy but sometimes a specific taxation or regulatory risk.
spot market (or cash market)	a commodities or securities market in which goods are sold for cash and delivered immediately. Contracts bought and sold on these markets are immediately effective. Spot markets can operate wherever the infrastructure exists to conduct the transaction. The spot market for most securities exists primarily on the internet.
Stock	A share (also referred to as equity shares) of stock represents a share of ownership in a corporation or company.
swap	a derivative in which two counterparties agree to exchange one stream of cash flows against another stream. The cash flows are calculated over a notional principal amount, which is usually not exchanged between counterparties.
unregulated fund	a vehicle established to hold and manage investments and assets, which is not subject to regulatory oversight. The fund usually has a stated purpose and/or set of investment objectives.

wealth management	the provision of banking and investment services in a closely managed relationship to high net worth clients who may be based in another country or may regularly travel between a number of countries.
wholesale securities market	includes private equity, corporate finance, wholesale markets, name passing securities companies in inter-professional markets and unregulated funds.

ANNEXES

1 ANNEX 1. INVESTMENT SERVICES AND FINANCIAL INSTRUMENTS AS SET OUT IN THE FINANCIAL MARKETS INSTRUMENTS DIRECTIVE

Section A – Investment service or activity

1. Reception and transmission of orders in relation to one or more financial instruments;

2. Execution of orders on behalf of clients;

3. Dealing on own account;

4. Portfolio management;

5. Investment advice;

6. Underwriting of financial instruments and/or placing of financial instruments on a firm commitment basis);

7. Placing of financial instruments without a firm commitment basis; and

8. Operation of Multilateral Trading Facilities (MTF).

Section B – Ancillary service

1. Safekeeping and administration of financial instruments for the account of clients, including custodianship and related services such as cash/collateral management;

2. Granting credits or loans to an investor to allow him to carry out a transaction in one or more financial instruments, where the firm granting the credit or loan is involved in the transaction;

3. Advice to undertakings on capital structure, industrial strategy and related matters and advice and services relating to mergers and the purchase of undertakings;

4. Foreign exchange services where these are connected to the provision of investment services;

5. Investment research and financial analysis or other forms of general recommendation relating to transactions in financial instruments; and the investment service of investment advice;

6. Services related to underwriting; and

7. Investment services and activities as well as ancillary services related to the underlying of the derivatives where these are connected to the provision of investment or ancillary services.

Section C – Financial instrument

1. Transferable securities;

2. Money-market instruments;

3. Units in collective investment undertakings; and

4. Options, futures, swaps, forward rate agreements and any other derivative contracts relating to securities, currencies, interest rates or yields, or other derivative instruments, financial indices or financial measures which may be settled physically or in cash;

5. Options, futures, swaps, forward rate agreements and any other derivative contracts relating to commodities that must be settled in cash or may be settled in cash at the option of one of the parties (otherwise than by reason of a default or other termination event);

6. Options, futures, swaps, and any other derivative contract relating to commodities that can be physically settled provided that they are traded on a regulated market and/or an MTF;

7. Options, futures, swaps, forwards and any other derivative contracts relating to commodities, that can be physically settled not otherwise mentioned in C 6 and not being for commercial purposes, which have the characteristics of other derivative financial instruments, having regard to whether, inter alia, they are cleared and settled through recognised clearing houses or are subject to regular margin calls;

8. Derivative instruments for the transfer of credit risk;

9. Financial contracts for differences;

10. Options, futures, swaps, forward rate agreements and any other derivative contracts relating to climatic variables, freight rates, emission allowances or inflation rates or other official economic statistics that must be settled in cash or may be settled in cash at the option of one of the parties (otherwise than by reason of a default or other termination event), as well as any other derivative contracts relating to assets, rights, obligations, indices and measures not otherwise mentioned in this Section, which have the characteristics of other derivative financial instruments, having regard to whether, inter alia, they are traded on a regulated market or an MTF, are cleared and settled through recognised clearing houses or are subject to regular margin calls.

2 ANNEX 2. DATA ON NATIONAL SECURITIES MARKETS

Name	Possibility of issue to bearer	Statistic data							
		Scope of issue (million. €)		Scope of deals (million €)		Securities market (million €)		Over-the-counter market (million €)	
Azerbaijan									
	2005-2006	**2005-2006**		**2005-2006**		**2005-2006**		**2005-2006**	
Shares[15]	+	506,12		188,84		163,88		102,14	
Corporative bonds	+	44,73		2,43					
Government bonds	-	1580,46		366,71					
Armenia									
	2005-2006	**2005-2006**		**2005-2006**		**2005-2006**		**2005-2006**	
Corporate securities	-	0,26		10,11		4,83		5,27	
Corporate bonds	+	0,35		2,49		0,88		1,61	
Estonia									
	2005-2006	2005-2006		2005-2006		2005-2006		2005-2006	
Shares	-	No data		5443,6		2580,0		2863,5	
Bonds	-	No data		46,6		3,4		43,2	
Malta									
	2005 **2006**	**2005**	**2006**	**2005**	**2006**	**2005**	**2006**	**2005**	**2006**
Sovereign Bonds	-	3,117	3,459	3,497	3,810	No data		No data	
Corporate Bonds	-	24	20	21	14				
Latvia									
	2005-2006	**2005**	**2006**	**2005**	**2006**	**2005**	**2006**	**2005**	**2006**
Shares	+	1745,556 (30.12.05)	1643,045 (29.12.06)	202,403	228,250	No data		No data	
Debt securities	+	689,412 (30.12.05)	655,239 (29.12.06)	4,281	4,281				
Lithuania									
	2005-2006	**2005-2006**		**2005-2006**		**2005-2006**		**2005-2006**	
Shares in companies	-	427,8		**2009**		No data		No data	
Bond market (government and companies)	-	2417,4		**931**		No data		No data	
Poland									
	2005-2006	**2005**	**2006**	**2005**	**2006**	**2005**	**2006**	**2005**	**2006**
Shares	+	5558,3	4904,6	18076,5	31645,6	No data		No data	
Bonds	+	1007,9	375,8	520,7	523,6				
Futures contracts	No data	No data		22515,7	35703,3				
Options	No data	No data		1093,1	1840,0				
Slovenia									
	2005-2006	**2005**	**2006**	**2005**	**2006**	**2005**	**2006**	**2005**	**2006**
Government securities - short term	+	1906,1	643,9	No data	No data	334,8	317,9	No data	No data
Government securities - long term	+	1571,3	950,8	No data	No data	422,7	426,3	No data	No data
Securities of other issuers (not banks)	+	0,0	18,3	No data	No data	No data	No data	No data	No data

[15] State Committee for Securities is going to come out with proposal to forbid issue shares to bearer.

Ukraine										
	2005	**2006**	**2005**	**2006**	**2005**	**2006**	**2005**	**2006**	**2005**	**2006**
Shares	+	-	3599,6	6315,9	26080,1	32731,9	501,1	959,3	25579,2	31772,6
Corporate shares of investment funds	-	-	121,4	221,9						
Corporate bonds	+	+	1849,2	3201,4	4732,5	9049,0	538,0	1013,9	4194,5	8035,1
Securities of local loan	+	+	50,8	12,1	322,9	414,1	86,7	90,5	236,3	323,6
Options	+	+	23,3	2,4	292,9	37,6	126,1	31,9	166,8	5,8
Investment certificates of share investment fund	+	+	3,3	2409,4	830,2	2065,0	9,5	16,7	820,7	2048,3
Certificates of fund of transactions with real estate	-	-	3,0	31,3	No data	16,5	No data	0,0	No data	16,5

3 ANNEX 3. CUSTOMER DUE DILIGENCE

Organisations providing securities dealing and intermediation services to customers (securities companies) should know the customers with whom they are dealing. A first step in setting up a system of customer due diligence (CDD) is to develop clear, written and risk based client acceptance policies and procedures, which among other things concern the types of products offered in combination with different client profiles. These policies and procedures should be built on the strategic policies of the board of directors of the security company, including policies on products, markets and clients.

The securities company's strategic policies will determine its exposure to risks such as dealing risk, reputational risk, operational risk, concentration risk and legal risk. After determining the strategic policies, client acceptance policies should be established, taking account of risk factors such as the background and geographical base of the customer and/or beneficial owner and the complexity of the business relationship. This is why – as indicated above – control measures and procedures with respect to AML/CFT should be an integral part of the overall customer due diligence.

Securities companies should be aware that, for example, they are more vulnerable to money laundering if they sell low value but high volume retail products to members of the public than if they sell sophisticated products to large financial institutions. The former are more sensitive to money laundering and therefore calls for more intensive checks on the background of the client and the origin of the funds than the latter. Securities companies should also be aware of requests for regular investment purchases slightly below any publicised limits for performing checks, such as checks on the source of wealth.

Customer due diligence measures that should be taken by securities companies include:

- identifying the customer and verifying that customer's identity using reliable, independent source documents, data or information;
- determining whether the customer is acting on behalf of another person, and then taking reasonable steps to obtain sufficient identification data to verify the identity of that other person;
- identifying the (ultimate) beneficial owner, and taking reasonable measures to verify the identity of the beneficial owner such that the securities company is satisfied that it knows who the beneficial owner is. For legal persons and arrangements securities company should take reasonable measures to understand the ownership and control structure of the customer;
- obtaining information on the purpose and intended nature of the business relationship and other relevant factors; and
- conducting ongoing due diligence on the business relationship and scrutiny of transactions undertaken throughout the course of that relationship to ensure that the transactions being conducted are consistent with the securities company's knowledge of the customer and/or beneficial owner, their business and risk profile, including, where necessary, the source of funds.

Risk Analysis

The extent and specific form of these measures may be determined following a risk analysis based upon relevant factors including the customer, the business relationship and the transaction(s). Enhanced due diligence is called for with respect to higher risk categories. Decisions taken on establishing relationships with higher risk customers and/or beneficial owners should be taken by senior management. Subject to national legal requirements securities companies may apply reduced or simplified measures in the case of low risk categories.

Prior to the establishment of a business relationship, the securities company should assess the characteristics of the required product, the purpose and nature of the business relationship and any other relevant factors in order to create and maintain a risk profile of the customer relationship. Based on this assessment, the securities company should decide whether or not to accept the business relationship. As a matter of principle, securities companies should not offer securities products to customers or for beneficiaries that obviously use fictitious names or whose identity is kept anonymous.
Factors to consider when creating a risk profile, which are not set out in any particular order of importance and which should not be considered exhaustive, include (where appropriate):

- type and background of customer and/or beneficial owner;
- the customer's and/or beneficial owner's geographical base;
- the geographical sphere of the activities of the customer and/or beneficial owner;
- the nature of the activities;
- the means of payment as well as the type of payment (cash, wire transfer, other means of payment);
- the source of funds;
- the source of wealth;
- the frequency and scale of activity;
- the type and complexity of the business relationship;
- whether or not payments will be made to third parties;
- whether a business relationship is dormant;
- any bearer arrangements; and
- suspicion or knowledge of money laundering, financing of terrorism or other crime.

The requirements for CDD should apply to all new customers as well as − on the basis of materiality and risk − to existing customers and/or beneficial owners. As to the latter the securities company should conduct due diligence at appropriate times. In some derivative, options and futures transactions, various transactions or 'trigger events' may occur after the contract date and indicate where due diligence may be applicable. These trigger events include margin calls, exercise of options and closing out of positions.

The requirement for a securities company to pay special attention to all complex, unusually large transactions, and all unusual patterns of transactions, which have no apparent economic or visible lawful purpose is essential to both the establishment of a business relationship and to ongoing due diligence. The background and purpose of such transactions should, as far as possible, be examined, the findings established in writing, and be available to help competent authorities and auditors. In this respect "transactions" should be interpreted in a broad sense, meaning inquiries and applications for a securities product, settlement, exercise of options, closing out of positions, etc.

In the event of failure to complete verification of any relevant verification subject or to obtain information on the purpose and intended nature of the business relationship, the securities company should not execute the transaction, or should terminate the business relationship. The securities company should also consider making a suspicious transaction report to the financial intelligence unit (FIU).

Establishing a business relationship

Identifying a customer is a two-part process. The securities company first identifies the customer, by obtaining a range of information from him. The second part – the verification – consists of the securities company verifying some of this information through the use of reliable, independent source documents, data or information.

The securities company will need to carefully assess the specific background, and other conditions and needs of the customer to satisfy local know your customer rules. To achieve this, the securities company will collect relevant information, for example details of source of funds, income, employment, family situation, etc. This will lead to a customer profile which could serve as a reference to establish the purpose of the relationship and to monitor subsequent transactions and events.

The securities company should realise that creating a customer profile is also of importance for AML/CFT purposes and therefore for the protection of the integrity of the securities company and its business.

In addition, the beneficial owner should also be identified and verified. For the purposes of this guidance paper the expression beneficial owner applies to the owner/controller of the securities acquired.

When the identity of customers and beneficial owners with respect to the securities dealing account has been established the securities company is able to assess the risk to its business by checking customers and beneficial owners against internal and external information on known fraudsters or money launderers (possibly available from industry databases) and on known or suspected terrorists (publicly available on sanctions lists such as those published by the United Nations). It is recommended that securities companies use available sources of information when considering whether or not to act on behalf of a customer. Identification and subsequent verification will also prevent anonymity of policyholders or beneficiaries and the use of fictitious names.

Timing of identification and verification

In principle identification and verification of customers and beneficial owners should take place when the business relationship with that person is established. This means that (the owner / controller of) the customer needs to be identified and their identity verified before, or at the moment when, the securities transaction is concluded. Valid exceptions are mentioned in the following paragraphs.

Where a customer is permitted to utilise the business relationship prior to verification, financial institutions should be required to adopt risk management procedures concerning the conditions under which this may occur. These procedures should include measures such as a limitation of the number, types and/or amount of transactions that can be performed and the monitoring of large or complex transactions being carried out outside the expected norms for that type of relationship. Where the securities company has already commenced the business relationship and is unable to comply with the verification requirements it should terminate the business relationship and consider making a suspicious transaction report.

Examples of situations where a business relationship could be used prior to verification are:

- tax authority approved individual investment and saving schemes;
- purchase and sale of securities for minimal amounts (less than limit set by law);
- internet accounts; and
- non-face-to-face customers

In addition, in the case of non-face-to-face business verification may be allowed after establishing the business relationship. However, securities companies must have policies and procedures in place to address the specific risks associated with non-face-to-face business relationships and transactions.

Transactions and events in the course of the business relationship

The securities company should perform ongoing due diligence on the business relationship. In general the securities company should pay attention to all requested changes to settlement and delivery instructions. It should assess if the change/transaction does not fit the profile of the customer and/or beneficial owner or is for some other reason unusual or suspicious. Enhanced due diligence is required with respect to higher risk categories. The CDD program should be established in such a way that the securities company is able to adequately gather and analyse information.

Occurrence of these transactions and events does not imply that (full) customer due diligence needs to be applied. If identification and verification have already been performed, the securities company is entitled to rely on this unless doubts arise about the veracity of the information it holds. As an example, doubts might arise if sale proceeds from one customer's account are used to fund the payments on an unrelated account.

Methods of identification and verification

This guidance paper does not seek to specify what, in any particular case, may or may not be sufficient evidence to complete verification. It does set out what, as a matter of good practice, may reasonably be expected of securities companies. Since, however, this guidance paper is neither mandatory nor exhaustive, there may be cases where a securities company has properly satisfied itself that verification has

been achieved by other means which it can justify to the appropriate authorities as reasonable in the circumstances.

The best possible identification documentation should be obtained from each verification subject. "Best possible" means that which is the most difficult to replicate or acquire unlawfully because of its reputable and/or official origin.

Individuals

The following personal information should be considered:
- full name(s) used;
- date and place of birth;
- nationality;
- current permanent address including postcode/zipcode;
- occupation and name of employer (if self-employed, the nature of the self-employment); and
- specimen signature of the individual.

It is recognised that different jurisdictions have different identification documents. In order to establish identity it is suggested that the following documents may be considered to be the best possible, in descending order of acceptability:
- current valid passport; or
- national identity card.

However, some jurisdictions do not have national identity cards and many individuals do not possess passports. Where appropriate the FIU or security industry supervisors should compile their own list of acceptable documents in accordance with local conditions.

Original documents should be signed by the individual and if the individual is met face-to-face, the documents should preferably bear a photograph of the individual. Where copies of documents are provided, appropriate authorities and professionals may certify the authenticity of the copies.

Documents which are easily obtained in any name should not be accepted uncritically. These documents include birth certificates, an identity card issued by the employer of the applicant even if bearing a photograph, credit cards, business cards, driving licences (not bearing a photograph), provisional driving licences and student union cards.

Legal persons, companies, partnerships and other institutions/ arrangements

The types of measures normally needed to perform CDD on legal persons, companies, partnerships and other institutions/arrangements satisfactorily require identification of the natural persons with a controlling interest and the natural persons who comprise the mind and management of the legal person or arrangement. Where the customer or the owner of the controlling interest is a public company that is subject to regulatory disclosure requirements, it is not necessary to identify and verify the identity of any shareholder of that company.

FATF Recommendation 5 requires, where customers and/or beneficial owners are legal persons or legal arrangements, the securities company to:
- verify that any person purporting to act on behalf of the customer and/or beneficial owner is so authorised and identify and verify the identity of that person;
- verify the legal status of the legal person or legal arrangement, e.g. by obtaining proof of incorporation or similar evidence of establishment or existence; and
- form an understanding of the ownership and control structure of the customer and/or beneficial owner.

Where trusts or similar arrangements are used, particular care should be taken in understanding the substance and form of the entity. Where the customer is a trust, the securities company should verify the identity of the trustees, any other person exercising effective control over the trust property, the settlors and the beneficiaries. Transactions should not be entered into until full CDD has been completed on all identified parties.

When dealing with the identification and verification of companies, trust and other legal entities the securities company should be aware of vehicles, corporate or otherwise, that are known to be misused for illicit purposes.

Sufficient verification should be undertaken to ensure that the individuals purporting to act on behalf of an entity are authorised to do so.

The following documents or their equivalent should be considered:

- certificate of incorporation;
- the name(s) and address(es) of the beneficial owner(s) and/or the person(s) on whose instructions the signatories of the customer are empowered to act;
- constitutional documents e.g. memorandum and articles of association, partnership agreements; and
- copies of powers of attorney or other authorities given by the entity.

In all transactions undertaken on behalf of an employer-sponsored pension or savings scheme the securities company should, at a minimum, undertake verification of the principal employer and the trustees of the scheme (if any).

Verification of the principal employer should be conducted by the securities company in accordance with the procedures for verification of institutional applicants for business. Verification of any trustees of the scheme will generally consist of an inspection of the relevant documentation, which may include:

- the trust deed and/or instrument and any supplementary documentation;
- a memorandum of the names and addresses of current trustees (if any);
- extracts from public registers; and
- references from professional advisers or investment managers.

As legal controls vary between jurisdictions, particular attention may need to be given to the place of origin of such documentation and the background against which it is produced.

Enhanced measures with respect to higher risk customers and non-cooperative countries and territories

Enhanced CDD measures should apply to all higher risk business relationships, clients and transactions. This includes both high risk business relationships assessed by the securities company, based on the customer's individual risk situation, and the types of business relationships mentioned in the following paragraphs.

With regard to enhanced due diligence, in general the securities company should consider which of the following, or possible additional measures, are appropriate:

- certification by appropriate authorities and professionals of documents presented;
- requisition of additional documents to complement those which are otherwise required;
- performance of due diligence on identity and background of the customer and/or beneficial owner, including the structure in the event of a corporate customer;
- performance of due diligence on source of funds and wealth;
- obtaining senior management approval for establishing business relationship; and
- conducting enhanced ongoing monitoring of the business relationship.

Bearer securities

Securities instruments in bearer form consist of bearer bonds and bearer securities certificates or "bearer shares". As with registered securities, both of these instruments are issued by a particular corporate entity in order to raise capital. The difference between registered securities and securities in bearer form, among other things, is the method of transfer. In the case of registered securities, the instrument is issued to a particular individual, and the "owner" is recorded in a register maintained by the issuing entity. In the case of securities in bearer form, the instrument is issued; however, the owner is not recorded in a register. When registered securities are transferred to a new owner, the new owner must be recorded in order for the transfer to be valid. When bearer securities are transferred, since there is no register of owners, the transfer takes place by the physical handing over of the bond or share certificate.

Share certificates, whether in registered or bearer form represent equity within a corporate entity, that is, they represent shareholdings or ownership of a particular corporate entity. The number of shares owned by a person determines the degree of control that such an individual may have over the legal entity that issued the shares. In the case of registered shares, determining ownership is relatively straightforward, as the record of ownership is maintained in the share register of the issuing entity. Determining the ownership of bearer shares, in contrast, is not so easy since it depends on who possesses or has physical control of the share certificates. The obstacles to determining easily the ownership of bearer shares (and thus the ultimate owner of the corporate entity that has issued such instruments) are a factor that has been exploited by launderers to conceal or disguise true ownership of entities used in some money laundering schemes.

Politically exposed persons

The FATF Recommendations require additional due diligence measures in relation to PEPs. For this purpose securities companies should:

- have appropriate risk management systems to determine whether the customer is a PEP. The board of directors of the securities company must establish a client acceptance policy with regard to PEPs, taking account of the reputational and other relevant risks involved;
- obtain senior management approval for establishing business relationships with such customers;
- take reasonable measures to establish the source of wealth and source of funds; and
- conduct enhanced ongoing monitoring of the business relationship.

New or developing technologies

New or developing technologies can be used to market securities products. E-commerce or sales through the internet is an example of this. Although for this type of non-face-to-face business verification may be allowed after establishing the business relationship, the securities company should nevertheless complete verification.

Although a non-face-to-face customer can produce the same documentation as a face-to-face customer, it is more difficult to verify their identity. Therefore, in accepting business from non-face-to-face customers a securities company should use equally effective identification procedures as those available for face-to-face customer acceptance, supplemented with specific and adequate measures to mitigate the higher risk.

Examples of such risk mitigating measures are:

- certification by appropriate authorities and professionals of the documents provided;
- requisition of additional documents to complement those which are required for face-to-face customers;
- independent contact with the customer by the securities company;
- third party introduction, e.g. by an intermediary subject to the criteria established in the section on Reliance on intermediaries and third parties below; and
- requiring the first payment to be carried out through an account in the customer's name with a bank subject to similar CDD standards.

Non-cooperative countries and territories

Compliance by jurisdictions with the FATF Recommendations is periodically assessed by international bodies. Jurisdictions that do not sufficiently apply the FATF Recommendations could be listed by the FATF as Non-cooperative countries and territories. In specific circumstances, jurisdictions may be asked to impose appropriate countermeasures. Securities companies should give special attention to business originating from jurisdictions which do not sufficiently apply the FATF Recommendations.

Simplified customer due diligence

In general, the full range of CDD measures should be applied to the business relationship. However, if the risk of money laundering or the financing of terrorism is lower (based on the securities company's own assessment), and if information on the identity of the customer and the beneficial owner is publicly available, or adequate checks and controls exist elsewhere in national systems it could be reasonable for securities companies to apply, subject to national legislation, simplified or reduced CDD measures when identifying and verifying the identity of the customer, the beneficial owner and other parties to the business relationship.

Securities companies should bear in mind that the FATF lists the following examples of customers where simplified or reduced measures could apply:

- financial institutions – where they are subject to requirements to combat money laundering and the financing of terrorism consistent with the FATF Recommendations, and are supervised for compliance with those controls;
- public companies that are subject to regulatory disclosure requirements;
- government administrations or enterprises.

Reliance on intermediaries and third parties

Depending on the legislation of the jurisdictions in which the securities company operates, it may be allowed to rely on intermediaries and third parties to perform the following CDD elements:

- identifying the customer and verifying that customer's identity using reliable, independent source documents, data or information;
- identifying the beneficial owner, and taking reasonable measures to verify the identity of the beneficial owner to the extent the intermediary or third party is satisfied that they know who the beneficial owner is, including taking reasonable measures to understand the ownership and control structure of the customer; and
- obtaining information on the purpose and intended nature of the business relationship.

Where such reliance is permitted, the following criteria should be met:

- the securities company should immediately obtain the necessary information concerning the above mentioned elements. Securities companies should take adequate steps to satisfy themselves that copies of identification data and other relevant documentation relating to the CDD requirements will be made available from the intermediaries and third parties upon request without delay. Securities companies should be satisfied with the quality of the due diligence undertaken by the intermediaries and third parties.
- the securities company should satisfy itself that the intermediaries and third parties are regulated and supervised, and have measures in place to comply with CDD requirements in line with FATF Recommendations 5 and 10.

Where such reliance is permitted, the ultimate responsibility for customer and/or beneficial owner identification and verification remains with the securities company relying on the intermediaries or third parties. The checks by the securities company as indicated in the previous paragraph do not have to consist of a check of every individual transaction by the intermediary or third party. The securities company should be satisfied that the AML and CFT measures are implemented and operating adequately.

Securities companies should satisfy the above provisions by including specific clauses in the agreements with intermediaries/third parties or by any other appropriate means. These clauses should include commitments for the intermediaries/third parties to perform the necessary CDD measures, granting access to client files and sending (copies of) files to the securities company upon request without delay. The agreement could also include other compliance issues such as reporting to the FIU and the securities company in the case of a suspicious transaction. It is recommended that securities companies use application forms to be filled out by the customers and/or intermediaries/third parties that include information on identification of the customer and/or beneficial owner as well as the method used to verify their identity.

Each jurisdiction should determine in which jurisdictions the intermediaries and third parties that meet the conditions can be based. Securities companies should inform themselves as to which jurisdictions are considered suitable taking into account information available on whether those jurisdictions adequately apply the FATF Recommendations.

The securities company should undertake and complete its own verification of the customer and beneficial owner if it has any doubts about the ability of the intermediary or the third party to undertake appropriate due diligence.

4 ANNEX 4. TRAINING OF STAFF

All staff of security companies should receive initial and ongoing training on relevant AML/CFT legislation, regulations, guidance and the security company's own AML/CFT policies and procedures.

Decisions on how to meet training needs should be made by each security company in accordance with its legal, regulatory and commercial requirements.

Such training programmes however should at a minimum include:

- Explanatory information on obligations contained in the relevant laws;
- Explanatory information on the securities company dealers' AML/CFT policy and systems, including specific information on verification and recognition of suspicious customers, suspicious transactions and reporting obligations of such suspicions to the compliance officer.
- A description of the nature and processes of laundering and terrorist financing, including new developments and current money laundering and terrorist financing techniques, methods and trends;

Certain categories of employees need more specific training. That is the case in particular with staff dealing with new business and the acceptance (either directly or via intermediaries) of new customers, such as sales persons; and with the settlement of transactions. These staff should be made aware of their legal responsibilities and the AML/CFT policies and procedures of the security company, in particular the client acceptance policies and all other relevant policies and procedures, the requirements of verification and records, the recognition and reporting of suspicious customers/transactions and suspicion of the financing of terrorism. They also need to be aware that suspicions should be reported to the compliance officer in accordance with AML/CFT systems.

Furthermore, directors and senior management with the responsibility for supervising or managing staff, and for auditing the system should also receive training covering all aspects of AML/CFT policy and procedure, and in particular on their responsibility regarding AML/CFT policies and procedures, relevant laws including the offences and sanctions applicable; procedures relating to the service of production and restraint orders (to stop writing business), internal reporting procedures; and on legal requirements for verification and record keeping.

Besides, the compliance officer should receive in-depth training concerning all aspects of all relevant legislation and guidance and AML/CFT policies and procedures. The compliance officer will require extensive initial and continuing instruction on the validation and reporting of suspicious customers/transactions and freezing assets in accordance with legislation.