

**MONEYVAL**

**Report submitted to Moneyval by  
Cyprus on progress in respect of the  
Special Assessment Of The  
Effectiveness Of Customer Due  
Diligence Measures In The Banking  
Sector In Cyprus**

8 December 2015

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# CYPRUS

## Written Report

### Submitted to MONEYVAL

#### **1. *Brief Secretariat Note on the Progress Made in Respect of the Special Assessment of the Effectiveness of Customer Due Diligence Measures in the Banking Sector in Cyprus***

1. At the 43<sup>rd</sup> Plenary, on 10 December 2013, the Plenary adopted the first report on Cyprus's progress in respect of the implementation of the recommendations in the report 'Special Assessment of the Effectiveness of Customer Due Diligence Measures in the Banking Sector in Cyprus' dated 24 April 2013 (the Special Assessment Report)<sup>1</sup>. At the time, while it was acknowledged that in the period since the special assessment the focus of the CBC's efforts had been on strengthening the financial system in Cyprus, it was clear that much work still needed to be done to ensure that the recommendations made by the special assessment team were implemented. The plenary therefore determined that Cyprus was to provide an interim report at the 44<sup>th</sup> Plenary and a fuller report at the 45<sup>th</sup> Plenary.
2. The interim report was presented and adopted at the 44<sup>th</sup> Plenary on 31 March 2014. The Plenary, after having considered the analysis of the Secretariat, determined that sufficient progress had been made by the authorities in the period since the 43<sup>rd</sup> Plenary to ensure that the banks had implemented the recommendations made in the special assessment report. It was reiterated that Cyprus should provide a fuller report on the progress made at the 45<sup>th</sup> Plenary. In particular, Cyprus was requested to provide information on the findings of the on-site inspections which were due to be carried out by the Central Bank of Cyprus (CBC) and provide further updates on the ongoing developments within the CBC, the Cyprus Securities and Exchange Commission (CySEC)<sup>2</sup>, the Cypriot Bar Association (CBA)<sup>3</sup>, the Institute of Certified Public Accountants of Cyprus (ICPAC)<sup>4</sup> and the Company Registry.
3. At the 45<sup>th</sup> Plenary, on 15 September 2014, the Plenary adopted the second report on Cyprus's progress. The Plenary was satisfied that the Cypriot authorities had taken further meaningful steps to ensure that banks implement the recommendations made in the Special Assessment Report. In particular, it was noted that the CBC had shifted its focus to on-site monitoring to verify that the updated policies and procedures of banks were being adequately implemented in practice and ensure that the concerns raised by the special assessment team were being properly addressed. However, a number of recommendations were made and Cyprus was requested to provide a report at the 48<sup>th</sup> Plenary in September 2015 on further progress made in relation to the Special Assessment Report.
4. Those recommendations were the following:
  - The CBC should continue implementing its on-site monitoring programme, particularly by undertaking further comprehensive on-site examinations. Priority should be given to those banks visited by the special assessment team, insofar as this is consistent with the CBC's risk-based supervisory programme. The CBC should also consider conducting a focussed inspection at those banks which have not yet received a visit.

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<sup>1</sup> [http://www.coe.int/t/dghl/monitoring/moneyval/Evaluations/CY\\_eurogroup\\_rep2013.pdf](http://www.coe.int/t/dghl/monitoring/moneyval/Evaluations/CY_eurogroup_rep2013.pdf)

<sup>2</sup> AML/CFT supervisor for Administrative Service Providers (TCSPs)

<sup>3</sup> AML/CFT supervisor for lawyers

<sup>4</sup> AML/CFT supervisor for accountants

- The CBC should follow-up on the action taken by banks in relation to deficiencies identified during comprehensive on-site examinations. Clear and definite time-frames should be established for addressing the identified deficiencies. Effective, proportionate and dissuasive sanctions should be imposed by the CBC for any serious breaches, where this is considered appropriate. The CBC should also continuing monitoring action taken by the banks which have received a focused visit, to ensure that the measures recommended by the CBC will be implemented.
5. On 16 November 2015, the Cypriot authorities submitted a report on the measures taken since the 45<sup>th</sup> Plenary in September 2014 (Section 2). The report should be read in conjunction with the Special Assessment Report, the two progress reports, adopted at the 43<sup>rd</sup> and 45<sup>th</sup> Plenaries respectively, and the interim report adopted at the 44<sup>th</sup> Plenary.
  6. In its most recent report, Cyprus confirmed that the 13 credit institutions which had been visited by the special assessment team in April 2013 have been subject to an anti-money laundering/counter financing of terrorism (AML/CFT) on-site inspection in the period from 2014 to 2015. In this period, the CBC conducted a total of 24 AML/CFT on-site inspections and one is still in process (11 in 2014 and 13 in 2015, with one further on-site inspection scheduled to take place in December<sup>5</sup>). The examination programme utilised by the CBC during its on-site inspections has been tailored specifically to focus on the measures arising from the recommendations made in the Special Assessment.
  7. The on-site monitoring programme for 2015 was developed on the basis of information gathered through the off-site monitoring tool established with the assistance of the International Monetary Fund (referred to in the previous progress reports). Off-site monitoring entails a detailed review by the AML/CFT Unit of the CBC of the Annual Reports of the Money Laundering Compliance Officers and the Annual Reports on AML/CFT Risk Assessment submitted by credit institutions to the CBC. The purpose of these reports is to assist the CBC in understanding each credit institution's inherent money laundering/financing of terrorism (ML/FT) risks, assess the internal control environment of the institution to mitigate risks and to develop institutional risk profiles. As a result of this off-site review, in 2015 the CBC focussed its (on-site) resources on those credit institutions which pose higher ML/FT risks, in addition to those credit institutions visited during the Special Assessment. Those credit institutions which were not included in the 2015 annual inspection programme were subject to off-site monitoring. It is planned that these credit institutions will be subject to an on-site inspection in 2016.
  8. Based on the on-site inspections conducted in 2014 and 2015, the CBC determined that all inspected credit institutions have adequate policies and procedures in place which are in line with the regulatory framework and appropriate to the nature and size of their business. In particular, credit institutions have policies and procedures which identify the categories of higher risk customers and the circumstances which could lead to a (re)classification of the risk-grading of the customer. Additionally, the CBC indicated that the policies and procedures recognise that the accumulation of risks in complex business in itself presents an overarching risk, set out enhanced measures which need to be applied to mitigate those risks, set out customer acceptance policies and specify the cases where it is appropriate to reject or terminate a client relationship on the basis of the assessed risk. Credit institutions also presented cases to the CBC where, in line with the updated policies and procedures, direct meetings were held by the institution with beneficial owners of existing customers.

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<sup>5</sup> In addition to the 14 inspection of 2015, the CBC has conducted on-site inspections at four Payment Institutions and one E-money institution.

9. Reference was made to other examples where in the course of the on-site inspections conducted by the CBC it was concluded that the recommendations made in the Special Assessment were being implemented by credit institutions. For instance, it was noted that those credit institutions which relied on business introducers reassessed existing business relationships with third parties and terminated those relationships which did not conform to the criteria concerning third parties introduced in November 2014 (referred to in the previous progress reports). It was verified that prospective business relationships which pose a higher risk had not established as a result of input provided by the Money Laundering Compliance Officer. It was found that a number of credit institutions had strengthened their AML/CFT Compliance Unit by increasing the staff complement and implementing software to facilitate the review of transactions. Most credit institutions which were inspected were found to have implemented measures to determine whether an existing customer (or beneficial owner) has become or is subsequently found to be a politically exposed person. Information on the purpose of the business relationship was found to have been updated in accordance with the risk profile of the customer. Measures were being taken to update customer due diligence information of existing customers, based on the nature, size and complexity of the business of the credit institution. It was noted that suspicions of ML related to tax evasion had been reported to the financial intelligence unit.
10. The Secretariat was informed that the follow-up process of the on-site inspections (which includes issuing an on-site inspection report containing corrective measures and a period of time within which credit institutions are permitted to provide submissions) is still underway. Therefore, no further information could be provided to the Secretariat on the breaches which were identified and the sanctions which the CBC intends to impose.
11. The authorities referred to other measures undertaken since September 2014. The CBC continued to strengthen its AML/CFT supervisory framework. The AML/CFT Unit, which was set up in May 2013, is comprised of a head of unit and seven additional staff members. It is expected that an additional person will join the unit in the future. The on-site inspections in 2014 and 2015 were carried out by the AML/CFT Unit with the assistance of external auditors. Awareness-raising and training programmes continued to be organised by the CBC on preventive measures. The Secretariat was informed that the external assessment of the Company Registry had been completed. It is worth noting that the backlog of amendments to company registration documents (comprising of approximately 40,000 documents) was processed successfully. More than 37,000 companies which were not compliant with their filing obligations were struck off the register. As a result of a compliance campaign, more than 314,000 overdue annual returns were submitted in 2015. It is expected that by mid-2016 the register will be completely updated and contain accurate and current information on all legal persons in Cyprus.
12. In light of the progress made by Cyprus, especially the fact that all credit institutions that had been inspected by the special assessment team in 2013 have now been subject to an on-site inspection and are currently discussing any necessary corrective measures with the CBC, the Plenary decided that Cyprus should not be requested to provide any further progress reports in relation to the Special Assessment. However, Cyprus should continue informing the Plenary, through the *tour de table* procedure, on any sanctions or other administrative actions imposed on credit institutions as a result of the on-site inspections carried out by the CBC. It should be noted that Cyprus's fifth round evaluation process is expected to start in May 2016, with the on-site element of the evaluation scheduled for May 2017. The effective application of customer due diligence (together with all other preventive measures) in the banking sector of Cyprus will therefore be subject to greater scrutiny in the context of the upcoming evaluation.

MONEYVAL Secretariat

December 2015

## **2. *Report submitted by Cyprus***

COUNCIL OF EUROPE



CONSEIL DE L'EUROPE

**COMMITTEE OF EXPERTS  
ON THE EVALUATION OF ANTI-MONEY LAUNDERING MEASURES  
AND THE FINANCING OF TERRORISM**

**Report on the Special Assessment of the Effectiveness of Customer Due Diligence Measures in the  
Banking Sector in Cyprus**

**16 November 2015**

## **Measures that have been adopted to implement the recommendations made in the Special Assessment of the Effectiveness of CDD Measures in the Banking Sector in Cyprus (24 April 2013)**

### **Background information**

It is recalled that the Special Assessment of how effectively Customer Due Diligence (CDD) measures are implemented within the Cypriot banking sector was conducted between 19 and 29 March 2013, when the prevailing economic environment was experiencing unforeseen turbulence which led to the adoption of a fully-fledged Economic Adjustment Programme ('EAP') by the Cypriot authorities with the European Commission, the European Central Bank and the International Monetary Fund.

Amongst the events that followed suit were an unprecedented financial sector restructuring (including the bail-in of uninsured depositors), resolution, restructuring and recapitalisation of the two biggest financial institutions of household posture within the Cypriot financial sector, the restructuring of the credit cooperative sector all using EAP funds. Additionally, another systemic bank was recapitalised with private funds. It is also worth mentioning the imposition of extensive capital controls in an effort to protect the then fragile banking system which lasted for about one year and were within the course of this period gradually relaxed.

As part of the EAP, Cypriot authorities undertook to reengineer the regulatory and supervisory AML/CFT framework taking into consideration the FATF framework. This effort included the issuance of revised Directives for AML/CFT issues to supervised persons, the redesign of onsite and offsite supervisory tools and the investment in manpower, systems and training .

For the banking sector in particular, the Central Bank of Cyprus ('CBC') overhauled its approach to the regulation and supervision of AML/CFT issues through a revised Directive on the basis of the relevant AML Law ('The Prevention and Suppression of Money Laundering and Terrorist Financing Laws of 2007-2014), a set of Guidelines, to assist credit institutions in effectively implementing their legal and regulatory obligations and further the goal to mitigate money laundering and terrorist financing (ML/TF) risks, so as to prevent the exploitation of the institutions for criminal purposes, the development with technical assistance by the IMF of specialised off-site tools and on-site inspection programs and the initiation of an intensive and demanding cycle of on-site inspections.

It should also be noted that the implementation of the EAP by the Cypriot authorities was closely monitored by its program counterparts by means of regular on-site quarterly visits, with the last visit taking place in the first half of November 2015. The program is expected to be completed by March 2016. It is worth noting that not all funds made available through the program will be drawn by the Cypriot government which has, on the basis of the progress achieved since March 2013, resorted to drawing funds from capital markets directly. More specifically, on AML/CFT issues, Cypriot authorities have achieved since the inception of the program compliance with the goals set notwithstanding the fact that the on-site inspection cycle is still under implementation.

As part of the efforts exerted by Cyprus to reinforce the fight against the use of the financial sector for money laundering and terrorist financing and in line with the international standards set by the Financial Action Task Force (FATF) and Moneyval, but also the relevant European directives and especially the 4th Directive of the European Parliament and of the Council on the prevention of the use of the financial system for the purposes of money laundering or terrorist financing, the CBC, in collaboration and coordination with the other regulatory authorities have decided to conduct an assessment of the related risks on a national level, with the assistance of the World Bank. This exercise, on the basis of the internationally accepted and recognised methodology of the World Bank, will allow for the identification of any deficiencies in the regulatory framework currently in place for combating money laundering and terrorist financing, but also in the effectiveness of the procedures followed by all stakeholders involved in this effort, aiming at taking corrective action. This will contribute significantly towards the reinstatement of Cyprus as a reputable international financial centre and will facilitate substantially the various assessments of the country that are carried out from time to time. The risk assessment is expected to be completed by July 2016.

Finally, as regards the issue of FBME Bank Ltd, to protect the integrity of the financial sector, the CBC took swift action to put the local branch of FBME Bank Ltd under resolution following the measures taken by its correspondent banks after its designation by the US authorities as a financial institution of primary money laundering concern. The CBC is in the final stage of taking the necessary measures, following the July 2014 on-site inspection for AML/CFT issues as well as other supervisory matters.

The following address the various recommendations derived by the assessors during their 2013 assignment and provide the current state of play.

1. ***Each bank should combine all of its risk analyses into an overall AML/CFT risk policy document, for Board approval, based on a thorough and meaningful consideration which should include in particular any risk areas that might not previously have received sufficient attention. This analysis should be updated on a regular basis. Concretely, banks should as part of their overall risk policy:***
  - i. ***Recognise that the accumulation of risks in complex business in itself presents overarching risk;***
  - ii. ***Determine their appetite for such complex business bearing in mind whether the bank is in a position to effectively monitor and control the cumulative risks sufficiently to mitigate the possibility of abuse for purposes of ML (including in respect of tax crimes) and FT;***
  - iii. ***Set out the enhanced measures which need to be taken to mitigate these overarching risks;***
  - iv. ***Specify cases where it is appropriate based on an assessment of the risks to reject or terminate a client relationship.***

***[High priority – 6 months and ongoing]***

***Response of the authorities:***

Measures taken by the Central Bank:

The Prevention and Suppression of Money Laundering and Terrorist Financing Law (“the AML Law”) was last amended in December 2014. A revised version of the Central Bank of Cyprus (“CBC”) Directive issued to credit institutions on the prevention of money laundering and terrorist financing (4<sup>th</sup> issue) (“the CBC Directive”), which was issued on 4 December 2013, now includes all the measures recommended by the Moneyval assessment team.

- A) Article 58 of the AML Law provides, inter-alia, that any person carrying out financial or other business activities, is obliged to apply adequate and appropriate systems and procedures in relation to internal controls, risk assessment and risk management in order to prevent money laundering and terrorist financing.

Section 3 of the CBC Directive imposes the requirement on the Money Laundering Compliance Officer to identify, record and evaluate all potential risks, with the full commitment and support of Senior Management and the active co-operation of the business units of the credit institution. Once a credit institution has identified the risks it faces then it must design and implement the appropriate systems and controls for their management and mitigation in accordance with the procedures prescribed in the CBC Directive. In addition, credit institutions need to have suitable means of assessing, on a regular basis, whether their risk mitigation procedures and controls are working effectively. Systems and controls should be kept under regular review so that risks resulting from changes in the characteristics of existing customers, new customers, products and services are managed and countered effectively. In view of the above, a credit institution should

keep its risk assessment report fully updated. It is, therefore, required that a credit institution revisits its assessment at least annually.

In this respect, it is required to submit the risk assessment report on an annual basis to the Board of Directors through the Senior Management for consideration and approval. A copy of the said approved report, together with the Money Laundering Compliance Officer's Annual Report, should be submitted to the CBC.

Following the said risk assessment, according to section 2 of the CBC Directive, credit institutions are required to develop and establish a clear policy and procedures in line with the provisions of the AML Law and the requirements of the CBC Directive.

The Money Laundering Compliance Officer is obliged to prepare the customer acceptance policy and submit it through the credit institution's Senior Management to the Board of Directors for consideration and approval. Once it has been approved, the said policy is communicated to the staff.

The said policy should set, in an explicit manner, the criteria for (i) accepting new customers, (ii) the types of customers who do not meet the said criteria and are not, therefore, acceptable for entering into a business relationship and (iii) should prescribe the categories of customers that should be designated as being of high risk. The customer acceptance policy and related procedures should provide for enhanced due diligence for the categories of high risk customers as prescribed in the AML Law, and the CBC Directive (Section 4.14.2) as well as those customers that the credit institution itself has classified as high risk on the basis of its adopted policy.

In addition, the CBC Directive requires credit institutions to expand their customer acceptance policy to recognize that the accumulation of risks in complex business in itself presents overarching risk and to determine their appetite for such complex business bearing together with the enhanced measures needed to effectively monitor and control the cumulative risks sufficiently to mitigate the possibility of abuse for purposes of ML (including in respect of tax crimes) and FT. Credit Institutions should also specify cases where it is appropriate based on an assessment of the risks to terminate a client relationship.

- B) On 19 June 2013, the CBC (AML Unit) held a meeting with the Money Laundering Compliance Officers of all credit institutions, where it presented and explained the findings of the Moneyval and Deloitte special assessments. The CBC requested the Money Laundering Compliance Officers of all credit institutions to analyse the findings of both reports and to take corrective measures based on the recommendations of each assessment. The CBC also held individual meetings with the Money Laundering Compliance Officers of the six credit institutions assessed by the independent auditors and distributed a copy of the findings relating specifically to their credit institution. During these meetings the findings of both assessments were discussed in detail. On 2 December 2013, the CBC invited again the Money Laundering Compliance Officers of all credit institutions to reiterate the importance of the application of CDD measures, monitoring of transactions and submission of suspicious activity reports.
- C) On 3 February 2014, the CBC issued a set of Guidelines to the Chief Executive Officers/General Managers of all credit institutions, to assist credit institutions in effectively implementing their legal and regulatory obligations and further the goal to mitigate money laundering and terrorist financing (ML/TF) risks, so as to prevent the exploitation of the institution for criminal purposes. The said Guidelines cover the following major areas:
- (i) Sound and effective risk management systems to identify and understand ML/TF risks (Appendix 1);
  - (ii) Customer Due Diligence and construction of customer's business/risk profile (Appendix 2);
  - (iii) Enhanced Due Diligence measures in relation to Politically Exposed Persons ("PEPs")

(Appendix 3);

(iv) Ongoing Monitoring of business relationships and transactions (Appendix 4);

(v) Education and Training to staff in relation to money laundering and terrorist financing (Appendix 5);

(vi) Fraudulent tax crimes as a predicate offence (Appendix 6).

D) In addition to the above, the Chief Executive Officers/General Managers of all credit institutions were requested to ensure the implementation of the requirements of the AML Law and the CBC Directive for the effective management of the risks emanating from money laundering or terrorist financing activities, commensurate to the nature, size and complexity of their credit institution's operations. Particularly, they were requested to ensure that:

(i) Their credit institution has sound and effective risk management systems in place to identify and understand ML/TF risks with respect to their customers, products and services, geographical locations/areas, and delivery channels. Their credit institution's risk management systems include an overall policy for identifying and understanding, measuring, controlling, and monitoring ML/TF risks. The said risk management policy, procedures and measures is submitted to the Management Body (Board of Directors) for approval, and reviewed on a regular basis.

(ii) Adequate and appropriate customer identification and due diligence measures are applied and the business/economic and risk profiles of their customers are properly constructed, determined and assigned;

(iii) Enhanced due diligence measures are applied to politically exposed persons and particularly the source of wealth of PEPs, is adequately identified and established. Also they were requested to strengthen the implementation of due diligence procedures when seeking to identify 'family members' and 'close associates' of PEPs, and institute systems and procedures to identify customers and persons related to customers, who subsequently become PEPs;

(iv) Their credit institution has sound and effective systems and measures in place to demonstrate ongoing monitoring of the business relationships and particularly for higher risk clients, including PEPs;

(v) Their credit institution's training programmes are reviewed to include information on current ML/TF techniques, methods and trends, and clear explanations of all aspects of the AML/CFT laws and regulations. Moreover, they were requested to ensure that training programmes include requirements concerning customer due diligence, suspicious transaction reporting and sanctions for non-compliance;

(vi) Their credit institution implements appropriate systems and procedures so as to detect and prevent the laundering of proceeds from fraudulent, serious tax crimes from the financial system; and

(vii) Their credit institution employs adequate human and other resources to comprehensively implement the requirements and provisions as stipulated in the Prevention and Suppression of Money Laundering Activities Laws of 2007-2013 and the Central Bank of Cyprus Directive on the prevention of money laundering and terrorist financing issued in December 2013.

E) The CBC conducted an information gathering exercise to assess the progress made by credit institutions in the implementation, inter-alia, of the recommendations of the Moneyval Special Assessment as well as any additional measures taken with respect to any weaknesses/problems they have identified. Particularly, on 13 February 2014, a Circular Letter was issued to the Money Laundering Compliance Officers of all credit institutions requesting them to provide their confirmation/attestation on specific measures taken by them and/or their institution, together with the relevant supporting information and/or documentation. In addition, and in accordance to

Sections 2 and 3 of the CBC Directive, on 28 February 2014, the Money Laundering Compliance Officers of all credit institutions submitted to the CBC copies of their Annual Report and the Risk Assessment Report, both of which were submitted to their Board of Directors for consideration and approval.

F) Relevant seminars were organised for the Money Laundering Compliance Officers of all credit institutions

- On 18 March 2014, the CBC organised a seminar for the financial sector with the assistance of an external financial expert, to address issues such as EDD, the construction of business profile, monitoring of transactions, and reliance on business introducers.
- On 28 March 2014, the CBC in collaboration with MOKAS and an external firm organised a seminar for the Money Laundering Compliance Officers of all credit institutions. This seminar covered the recent changes to the legal and regulatory framework (including the AML Law and Regulations), tax crimes, construction and submission of SARs, and Risk Management Systems.
- On 19 May 2014 the CBC in cooperation with the Cyprus Institute of Financial Services organised a seminar which covered highlights from the Moneyval and Deloitte special assessments, PEPs and their regulatory framework and tax crime as a predicate offence for ML purposes. In particular during that session the regulatory framework on tax crimes was explained as well as examples on legal tax structures/business structures likely to be used for legitimate tax planning purposes in Cyprus.
- On 16 December 2014 the CBC in collaboration with an audit firm and with the assistance of two external financial experts organised a Seminar on Risk Assessment. This seminar covered examples of methodology that can be used and the drafting of Risk Assessment Reports.
- On 16 & 17 February 2015, the CBC in cooperation with the Cyprus Institute of Financial Services and Global Training organised a two-day seminar which covered topics such as AML/CFT Compliance, Tax crime, Trusts, Foundations, Funds and Fraud.
- In addition, the Head of the AML/CFT Unit has delivered key note addresses at various seminars in the period 2014-2015, whereby the expectations and measures to address the various deficiencies are analysed, as well as the progress made on the road to recovery.

G) Onsite and offsite examinations

The comprehensive on-site inspections carried out in 2014/2015 included all those credit institutions which had been visited by the special assessment team of Moneyval in 2013.

During 2014, CBC examiners, through a tailored examination programme, obtained evidence, inter-alia, of implemented measures stemming from the recommendations made by Moneyval following its Special Assessment.

Moreover, during 2014 the CBC performed comprehensive AML/CFT on-site inspections in 11 credit institutions, covering inter-alia the effectiveness of their risk management systems.

During 2015, the CBC used the off-site tools mentioned in the Background Information section of this report to develop an on-site inspection plan for the year. Priority was given to those credit institutions which presented characteristics which were perceived as attracting higher risks insofar as AML/CFT issues are concerned. For those credit institutions that were not included in the audit plan for 2015, it was deemed acceptable given the risk comparison with their peers. Nevertheless, they will be included in the audit plan for 2016 and in particular for on-site visits in the first half of the year. It needs to be emphasized that the CBC has kept those institutions that were not submitted under a comprehensive audit in either 2014 or 2015 in close monitoring through the off-site tools, the review of the Annual Reports of the Money Laundering Compliance Officers of all licensed credit institutions addressed to the BoD through the Senior Management and copied to the CBC, the review of the AML/CFT risk report addressed to the BoD through the Senior Management and copied to the CBC and the attendance of meetings held in the presence of senior management and the internal auditors.

By November 2015, the CBC has completed comprehensive on-site inspections in thirteen credit institutions (including 4 cooperative societies) as planned and one more on-site inspection will be conducted at the beginning of December 2015.

In line with the new risk-based supervisory approach adopted by the CBC, the AML Unit of the CBC analyses the Money Laundering Compliance Officers' Annual Reports and Risk Assessment Reports submitted by the institutions, together with additional data that are submitted on a six monthly basis, so as to understand each institution's inherent ML/TF risks, assess the internal control environment they have in place to mitigate and/or control the inherent ML/TF risks, as well as build the institutional risk profiles. In carrying out this analysis, it liaises with the responsible prudential supervisory team and the institutions external auditors, as required.

Finally, the process of the on-site inspection is followed by an exit meeting which senior management, the internal auditor, the MLCO and other officials from the credit institutions, as necessary, are required to attend. During this meeting, which timewise takes place shortly after the completion of the on-site inspection, all findings are presented so as to allow the credit institution to start taking corrective measures promptly. An examination report for internal use by the CBC is also prepared, with reference to all matters reviewed during the on-site inspection. An examination letter addressed to the credit institution is then sent, inviting the institution to give its position within 14 days. On the basis of the reply of the credit institution, a second letter is then addressed either to impose an administrative fine or to give written warning for the assumption of specific corrective measures within a specified time period.

The CBC follows a policy of publishing on its website any administrative fines imposed on credit institutions for AML/CFT infringements.

For the on-site inspections of 2014/2015, the process of the issuance of examination reports and letters is still on-going and hence no indication may be given as to the possible outcome.

#### Measures taken by the credit institutions:

In March 2014, the Money Laundering Compliance Officers of all credit institutions confirmed that their respective institutions had in place a Risk Assessment methodology to identify and understand ML/TF risks within their customer, products, services, geographical locations/areas and delivery channels. According to information and documentation collected from all credit institutions, they have amended their policies and procedures to be in line with the revised legal and regulatory framework. The said policies and procedures, together with the Money Laundering Compliance Officer's Annual Report and the Risk Assessment Report were submitted to the Board of Directors of each institution for consideration and approval (a copy of the said documents and reports was also submitted to the CBC).

In February 2015 all credit institutions submitted to the CBC a copy of the Money Laundering Compliance Officer's Annual Report and the Risk Assessment Report for 2014, together with the minutes of the Board of Directors. This process is repeated annually.

During CBC onsite examinations of 2014 and 2015, it was established that all credit institutions' policies and procedures are in line with the current regulatory framework and appropriate to the nature and size of their business.

It was also established that their policies and procedures determine the categories of high risk customers as well as those attributes/circumstances which, if prevailing, will lead to the (re)classification of customers into the high risk category. In this respect, it was established that banks' policies and procedures recognise that the accumulation of risks in complex business in itself presents an overarching risk. In addition, it was established that banks' policies and procedures set out the enhanced measures which need to be taken to mitigate these overarching risks as well as the criteria for accepting customers and specify cases where it is appropriate based on an assessment of the risks to reject or terminate a client relationship.

Furthermore, the Risk Assessment System is evaluated through the performance of the Risk

- 2. In cases involving an accumulation of high risks, particularly where emanating from the use of complex structures combined with introduced business, banks should strengthen their current procedures in line with their updated risk policy and consistently implement the highest level of enhanced due diligence. This could include (as indicated by some banks in Cyprus as already their practice in high risk cases) direct contact with the ultimate beneficial owner in a larger number of cases. [High priority – 6 months and ongoing]**

**Response of the authorities:**

Measures taken by the Central Bank:

- A) Article 61(2) of the AML Law requires persons carrying on financial or other business activities to apply the customer identification and due diligence procedures set out in the Law but permits persons carrying out financial or other business activities to determine the extent of such measures on a risk sensitive basis depending on the type of customer, business relationship, product or transaction. It is highlighted that, according to the AML Law, persons carrying on financial or other business must be able to demonstrate to the competent authorities that the extent of the measures is appropriate in view of the risks of money laundering and terrorist financing.

In addition to the above, Article 64(2) of the AML Law requires persons carrying out financial or other business activities to apply enhanced and additional customer due diligence measures in all instances which due to their nature entail a higher risk of money laundering or terrorist financing.

Section 4.14 of the CBC Directive requires, inter-alia, that for high risk products, accounts or customers, credit institutions should take additional measures for verifying their customers' identity, creating their business profile and ascertaining the source of assets i.e. how they have been acquired and their origin as well as monitor the movement of their transactions on a regular basis. Moreover, it is required that in cases where there is an accumulation of high risks and particularly emanating from the use of complex structures combined with introduced business, credit institutions' enhanced due diligence measures should entail a direct contact with the natural person who ultimately owns or exercises control over a customer. For this purpose, minutes should be prepared following every meeting and kept in the customer's file.

Section 4.12 of the CBC Directive provides that credit institutions may rely on third parties for the implementation of customer identification and due diligence procedures, only at the outset of establishing a business relationship for the purpose of ascertaining and verifying the identity of their customers. According to the degree of risk, any additional data and information for the purpose of updating the customer's business profile during the operation of the account or for the purpose of examining unusual transactions executed through the account, should be obtained from the natural persons (directors, beneficial owners) who control and manage the activities of the customer and have the ultimate responsibility of decision making as regards management of funds and assets.

- B) Please refer to the CBC's response to Question 1 above. Points B to G are relevant.

Measures taken by the credit institutions:

In March 2014, the Money Laundering Compliance Officers confirmed that their AML/CFT policy, the Customer Acceptance Policy as well as their AML/CFT procedures were amended to reflect the nature, size and complexity of their respective credit institution's operations. In this connection, they confirmed that their policies and procedures are in line with the requirements of

the CBC Directive and set in an explicit manner the categories of high risk customers, the categories of customers involving accumulation of high risks, the criteria for accepting customers as well as those types of customers who are not acceptable or should be rejected. In addition, their procedures provide, inter-alia, for enhanced due diligence measures to mitigate any ML/TF risk.

As already mentioned under question 1, during onsite examinations of 2014 and 2015 carried out at twenty four credit institutions, it was established that policies and procedures determine the categories of high risk customers as well as those attributes/circumstances which, if present, can lead to the classification of a customer into the high risk category. In this respect, it was established that credit institutions' policies and procedures recognise that the accumulation of risks in complex business in itself presents overarching risk. In addition, it was established that credit institutions' policies and procedures set out the enhanced measures which need to be taken to mitigate these overarching risks. Moreover, it was noted that all credit institutions' policies and procedures describe the circumstances under which their officials should meet directly with the person who ultimately owns or exercises control over the customer. In this connection, the credit institutions were requested to present to the CBC examiners cases of customers with which, as a result of the implementation of their policies, the credit institution had direct meetings with them, including evidence thereof.

- 3. Banks should implement stricter controls on the use of business introducers to ensure not only that the introducer is regulated but also that the introducer's AML/CFT procedures are reviewed on an ongoing basis. In accordance with best practice reported to the assessors by several credit institutions, where concerns arise on the reliability of CDD conducted by a particular business introducer, or a significant number of SARs relate to customers they introduce, credit institutions should always consider terminating business relations with the introducer. [High priority – 6 months and ongoing]**

**Response of the authorities:**

Measures taken by the Central Bank:

- A) Article 67 of the AML Law permits persons carrying on financial or other business to rely on third parties for the implementation of customer identification and due diligence procedures, as these are prescribed in article 61(1)(a),(b),(c) of the AML Law, provided that the said persons are (i) subject to mandatory professional registration, recognized by law and (ii) are subject to supervision with regard to their compliance with the requirements of the European Union Directive. Moreover, the AML Law explicitly provides that the ultimate responsibility for performing the above mentioned measures and procedures remains with the credit institutions or the other person who carries on the financial or other business which relies on the third person. Consequently, the obligation to apply customer identification and due diligence procedures cannot be delegated to a third person.

The CBC has taken steps to expand its regulation on credit institutions that rely on third parties in recognition of the unique role and risks posed by such entities in the anti-money laundering framework. Particularly, section 4.12 of the CBC Directive requires credit institutions, prior to accepting the customer identification data verified by the said third person, to apply the following additional measures/procedures:

- (i). Obtain a copy of the policy and procedures applied by the third person.
- (ii). Ascertain and evaluate the systems and procedures applied by the third person for the prevention of money laundering and terrorist financing. The said assessment should be performed by the credit institution's Money Laundering Compliance Officer.
- (iii). Collect data and information on the person appointed as a Compliance Officer in accordance with Article 69(1) of the AML Law,

- (iv). As a result of the above mentioned assessment, the credit institution should be satisfied that the third person implements customer identification, due diligence and record keeping systems and procedures which are in line with the requirements of the AML Law and the CBC Directive.
- (v). The Money Laundering Compliance Officer maintains a separate file for every third person where it keeps the assessment report and other relevant information (identification details, records of meetings, evidence of professional registration in accordance with the appropriate law etc).
- (vi). The Money Laundering Compliance Officer reviews on an annual basis the business relationship with the third person.
- (vii). The Money Laundering Compliance Officer keeps a register with data/information (e.g. name, address, work, professional area, supervisory authority, cooperation start date, last date of evaluation, next evaluation date, evaluation grade) on third persons with whom the Bank has entered into cooperation. A copy of the said register should be forwarded to the Central Bank of Cyprus along with the Money Laundering Compliance Officer's Annual Report.
- (viii). The Money Laundering Compliance Officer gives her/his approval for the commencement of the cooperation with the third person.

The CBC in cooperation with representatives of credit institutions and the Association of Cyprus Banks have developed (i) a questionnaire which will assist them to assess third parties at the onset of the business relationship and (ii) specific criteria (a scorecard) that will be used by the Money Laundering Compliance Officers at the onset and in the course of the business relationship with them. The said questionnaire and scorecard was forwarded to all credit institutions by the Association of Cyprus Banks in May 2014.

To ensure a level playing field and regulatory compliance by all credit institutions, on 10 July 2014, the CBC forwarded the said two documents to all credit institutions obliging them to make use of them in case their institution's policy allows them to rely on third parties for customer identification purposes. In this connection, each credit institution should arrange for the said new questionnaire to be completed for all third parties with whom it has a business relationship and to reassess them in accordance with the requirements of the Law and the CBC Directive.

In addition to the above, credit institutions were requested to make use of the scorecard during the application of the review procedure and assign a score to each third party which will determine the continuation or termination of the relationship, accordingly. The said process was completed in November 2014.

Initially, it was proposed to set up a registry populated with those third parties who do not fulfill the above obligations. Such third parties were to be recorded in the registry by the credit institutions themselves. The CBC developed the required IT infrastructure to assist in this project. Subsequent discussions with all parties concerned raised a number of legal and administrative issues which led to the shelving of the project, at least for the time being. Notwithstanding this development, the CBC during its on-site inspection addresses the issue of third persons by means of a specialized audit program and assessment which could lead to sanctioning of the credit institution if the latter's procedures are found to be deficient or contravene the provisions of the CBC AML directive regarding the issue of third persons.

C) Please refer to the CBC's response to Question 1 above. Points B to G are relevant.

Measures taken by the credit institutions:

In March 2014, the Money Laundering Compliance Officers confirmed that credit institutions

amended and enhanced their AML/CFT policies and procedures to be in line with the legal and regulatory framework. It should also be noted that 13 credit institutions confirmed that, according to their institution's policies, they do not rely on third parties for customer identification and due diligence procedures.

During the onsite examinations carried out in twenty four credit institutions since the beginning of 2014, it was established that credit institutions' policies and procedures have indeed been amended and enhanced in order to be in line with the regulatory framework.

In addition, it was established that those credit institutions which rely on business introducers have reassessed existing business relationships with third parties on the basis of the regulatory requirements mentioned above utilising a specialised questionnaire and scorecard. Moreover, it was noted that credit institutions terminated business relationships which did not meet the aforementioned criteria.

The above provide sufficient comfort to the CBC that, despite the non-implementation of the disqualified third persons' register, credit institutions have indeed taken on board the regulatory requirements and the prevailing new stride of reliance on third parties. Needless to say that compliance with these requirements will continue to form part of the CBC's on-site inspection, under a dedicated inspection program.

**4. When accepting higher risk customers, banks should ensure, where not already the case, that ML/FT risk issues are taken fully into account, with the process involving the expertise of the compliance function in an enhanced advisory role. [High priority – 6 months and ongoing]**

**Response of the authorities:**

Measures taken by the Central Bank:

- A) Article 61(2) of the AML Law requires persons carrying on financial or other business activities to apply the customer identification and due diligence procedures set out in the AML Law but permits persons carrying out financial or other business activities to determine the extent of such measures on a risk sensitive basis depending on the type of customer, business relationship, product or transaction.

In addition to the above, Article 64(2) of the AML Law requires persons carrying out financial or other business activities to apply enhanced and additional customer due diligence measures in all instances which due to their nature entail a higher risk of money laundering or terrorist financing.

In this connection, the CBC Directive requires that the Customer Acceptance Policy of each credit institution should define the categories of high risk customers, as these are defined in the AML Law, the CBC Directive (Section 4.14.2) as well as the clients that the credit institution itself has classified as high risk on the basis of the risk assessment and policy it has established.

Furthermore, Section 4.14 of the CBC Directive provides that, in order to determine what constitutes sufficient customer identification, one should take into account each customer's perceived risk associated with money laundering and terrorist financing. The extent and the number of checks that must be carried out for customer identification may vary depending on the perceived risk of the customer's country of origin or the type of service, product or account requested by the customer, or the customer's background and professional or business activities as well as the level of the expected turnover and transactions. Information on the source of funds, i.e. how payments will be made, from where and by whom, should be recorded so as to facilitate future transaction checks.

However, for high risk products, accounts or customers, credit institutions should take additional

measures for verifying their customers' identity, creating their business profile and ascertaining the source of assets i.e. how they have been acquired and their origin as well as monitor the movement of their accounts/transactions on a regular basis.

It is emphasised that a credit institution should be in a position to prove to the Central Bank of Cyprus, if so requested in the context of the latter's supervisory function, that the extent of customer identification and due diligence measures implemented is proportional to the money laundering and terrorist financing risks faced.

In addition to the above, the CBC Directive provides that the Money Laundering Compliance Officer should become aware of the prospective high risk customers the credit institution intends to accept, and he/she should act as an advisor before the credit institution establishes a business relationship. For existing high risk customers, the above said process should be implemented during the updating procedure. Moreover, for the reclassification of high risk customers to a lower risk level, the approval of the Money Laundering Compliance Officer is required.

B) Please refer to the CBC's response to Question 1 above. Points B to G are relevant

Measures taken by the credit institutions:

In March 2014, the Money Laundering Compliance Officers confirmed that all credit institutions' AML/CFT policies and procedures have been amended to be in line with the above mentioned regulatory requirements.

During onsite examinations carried out in twenty four credit institutions, it was established that credit institutions' policies and procedures provide that the Money Laundering Compliance Officer should become aware of the prospective high risk customers the credit institution intends to accept, and he/she should act as an advisor before the credit institution establishes a business relationship. Policies and procedures of some credit institutions go beyond the CBC requirements, requiring the Money Laundering Compliance Officer's opinion for all customers, irrespective of risk categorisation.

In addition, it was verified that for all new business relationships established with high risk customers, the Money Laundering Compliance Officer's opinion had been obtained. Furthermore, it was verified that for existing high risk customers the above said process is indeed implemented during the updating procedure. It is worth noting, that in some cases the on-boarding of certain prospective customers was terminated in view of the negative opinion given by the Money Laundering Compliance Officer.

**5. Banks should review the resources allocated to the monitoring of high risk international business and where necessary increase resources of compliance departments to fully investigate and properly review all the alerts raised on high risk accounts. Any banks not already conducting such transaction checking thoroughly across the full range of their higher- risk business should be required to improve the effectiveness of their implementation. [High priority - ongoing]**

***Response of the authorities:***

Measures taken by the Central Bank:

A) Article 61(1) (d) of the AML Law requires persons engaged in financial or other business to conduct ongoing monitoring of the business relationship including scrutiny of transactions undertaken throughout the course of that relationship to ensure that the transactions being conducted are consistent with data and information maintained by the person who carries on financial or other business in respect of the customer, the business and the risk profile of the customer, including the source of funds as well as ensuring that the documents, data or information held are kept up-to-date.

Article 58(e) of the AML Law requires credit institutions, inter alia, to examine in detail any transaction which by its nature may be associated with money laundering or terrorist financing and in particular those complex or unusually large transactions and all unusual patterns of transactions which have no apparent economic or visible lawful purpose.

Section 4.15 of the CBC AML Directive requires credit institutions to perform on-going monitoring of customers' accounts and transactions for effective money laundering and terrorist financing preventive procedures. Credit institutions are required to have a full understanding of normal and reasonable account activity of their customers as well as of their business profile and have the means of identifying transactions which fall outside the regular pattern of an account's activity or to identify complex or unusual transactions or transactions without obvious economic purpose or clear legitimate reason. The procedures and intensity of monitoring accounts and examining transactions should be risk sensitive.

In order to accomplish the above, credit institutions are required to have in place adequate automated/ electronic management information systems which will be capable of supplying, on a timely basis, all the valid and necessary information for the identification, analysis and effective monitoring of customer accounts and transactions to Management, the Money Laundering Compliance Officer and other responsible officials based on the assessed risk of these accounts and transactions in relation to money laundering or terrorist financing purposes.

Finally, Appendix 3 of the Directive of the Central Bank of Cyprus entitled 'The Governance and Management Arrangements Directive' (July 2014), defines the "Principles for a sound and an effective operation of information technology systems in the context of managing a credit institution's operational risk" and imposes detailed and specific requirements on credit institutions in relation to the secure, effective and efficient operation of systems.

B) Please refer to CBC's response to Question 1 above. Points B to G are relevant.

Measures taken by the credit institutions:

In March 2014, the Money Laundering Compliance Officers confirmed that their institutions have reviewed the resources allocated to the Money laundering compliance units and to the units monitoring transactions, and measures have been taken where needed.

During the onsite examinations carried out in 2014/2015, it was noted that eleven institutions have strengthened their resources by hiring more staff in compliance units. Thirteen credit institutions reviewed their staff resources allocated to their AML Unit and concluded that there was no need to increase the staff.

Additionally, banks have reviewed and some have invested in IT platforms which allow for a detailed review of the transactions by the relevant staff. The CBC reviews these tools as part of its on-site inspections, with the assistance of IT specialists from the Supervision Department. The review covers, inter-alia, AML IT systems security and adequacy, alert systems, scenario analysis, UN/EU sanctioned persons, client lists et al. Any weaknesses identified from this review are reported as findings of the on-site inspection.

- 6. Banks should strengthen the implementation of due diligence procedures in relation to PEPs, particularly when seeking to identify 'family members' and 'close associates' of PEPs, ascertaining source of wealth, and identifying customers who subsequently become PEPs. These issues may point to a need for the competent authorities to issue further guidance on establishing sources of wealth. [Medium priority – 12 months]**

**Response of the authorities:**

Measures taken by the Central Bank:

- A) Section 64(1)(c) of the AML Law has been amended to strengthen the implementation of due diligence procedures in relation to politically exposed persons (PEPs). Particularly, the said requirements do not limit, any more, the scope of the PEP requirements to individuals who have their place of residence in another country. Therefore, the said requirements equally apply to local as well as foreign PEPs. Also, the AML Law requires that persons providing financial and other activities to have appropriate risk based procedures to determine whether the customer or the beneficial owner is a politically exposed person (family member or PEP's associate). Moreover, it is an obligation imposed by the AML Law on credit institutions to address the situations where an existing customer becomes or is subsequently found to be a PEP and to obtain the Senior Management's approval for the continuation of relationships between the credit institution and such persons.
- B) Please refer to CBC's response to Question 1 above. Points B to G are relevant.

Measures taken by the credit institutions:

In March 2014, the Money Laundering Compliance Officers confirmed that credit institutions amended their AML/CFT policies and procedures to be in line with the above mentioned legal and regulatory requirements. In addition to the above, the majority of credit institutions confirmed that they amended their Account Opening Forms and introduced specific self declaration questions regarding PEPs, family members and/or PEPs' associates. It should be noted that all credit institutions are subscribers to relevant commercial databases for screening their customers and in cases of legal entities, the natural persons (i.e. UBOs, authorised signatories and Directors) connected with them.

In relation to local PEPs, the CBC has established through its on-site inspections that credit institutions identified, reviewed and reassessed such business relationships, where they existed.

In relation to the requirement to have systems and procedures in place to address the situations where an existing customer or the beneficial becomes or is subsequently found to be a PEP, the CBC has established as part of the on-site inspections carried out in 2014/2015 that twenty credit institutions have implemented the necessary procedures and systems to comply with the above requirement. Any weaknesses identified in relation to PEPs during the on-site examinations of 2014/2015 will be duly reported to the credit institutions concerned in the examination letters which will be sent.

- 7. Banks should ensure that the purpose of the business relationship is identified and recorded in all cases and that the economic and business profile of high risk customers is detailed, meaningful, accurate and regularly updated, where this has not already been done. [Medium priority – 6-12 months, risk prioritised]**

**Response of the authorities:**

Measures taken by the Central Bank:

- A) Section 4 of the CBC Directive covers in detail the customer identification and due diligence measures needed to be applied by credit institutions in order to construct a detailed, meaningful and accurate customer business and economic profile.
- B) Please refer to the CBC's response to Question 1 above. Points B to G are relevant.

Measures taken by the credit institutions:

In March 2014, the Money Laundering Compliance Officers confirmed that their policies and procedures provide for the collection of adequate information which is detailed, meaningful, accurate and regularly updated. For high risk customers additional/enhanced due diligence measures are applied. Following the Moneyval and Deloitte Special Assessments, and having in

mind the weaknesses identified, credit institutions informed us that they have taken a number of steps/measures to ensure that their institution is compliant with the corresponding legal and regulatory requirements. Examples of measures taken by credit institutions were the following:

- Policies and procedures have been reviewed, amended and/or enhanced where needed.
- Customers' files were reviewed to ensure that in all cases the construction of business profiles is adequate and meaningful.
- A KYC Unit was established for reviewing customer files and transactions.
- Money Laundering Compliance Officer reviews and approves high risk customers.
- Identification and assessment/evaluation of business relationships with local PEPs.
- The Internal Auditor and the Compliance Department or the Money Laundering Compliance Officer intensified their audits (regular and/or ad hoc reviews) to ensure effective implementation of policies and procedures.
- Enhanced/upgraded IT systems to maintain customer business profiles electronically and/or identify cases of customers where documents/information is missing and/or generate reports/statistics which facilitate the review/update process.
- High risk customers visited or contacted directly by credit institution officials.

During the onsite examinations of 2014 and 2015, it was established that credit institutions' policies and procedures are in line with the AML regulatory framework requiring credit institutions' officials to collect adequate information which is detailed, meaningful, accurate and regularly updated. For high risk customers additional/enhanced due diligence measures are applied.

Moreover, one of the objectives of the CBC examiners during the onsite examinations of 2014 and 2015, was to assess the level of compliance of each credit institution in relation to the effective implementation of customer due diligence procedures, emphasising high risk customers. In this connection, an appropriate sample of existing and new customers was selected in order to test all aspects of CDD procedures including the updating of business and risk profiles of all customers. In this respect, it has been evidenced that credit institutions have indeed put a great effort and improved their AML procedures so as to be commensurate with the risks they are facing, the purpose of the business relationship was identified and recorded in many cases and that the economic and business profile of high risk customers is detailed, and meaningful. Any weaknesses that were identified during the on-site inspections on CDD issues will be duly reported in the examination letters to be addressed to the credit institutions.

**8. Banks should update any remaining outstanding CDD in relation to existing customers without further delay. [Medium priority – 6-24 months, risk prioritised]**

**Response of the authorities:**

Measures taken by the Central Bank:

- As per Moneyval's Special Assessment report, a few credit institutions indicated that projects to update verification documentation for customers existing at the time of the material upgrading of the Cypriot AML/CFT requirements in 2007/8 were, to some extent, still in progress. The credit institutions concerned informed the assessors that the outstanding work related to retail business and the omissions were mainly technical in nature (e.g. no copy of utility bill, out-of-date identification document) but may also include incomplete customer profile to provide the base line for ongoing due diligence. In general, most of the customer base, including larger, riskier, and corporate customers appeared to have been addressed at this stage.
- Article 60(d) of the Law requires persons carrying out financial or other business activities to apply customer identification and due diligence measures when there are doubts about the veracity or adequacy of previously obtained customer identification documents, data or information.

Furthermore, article 62(6) of the Law requires the application of customer identification and due diligence procedures not only to new customers but also at appropriate intervals to existing customers, depending on the level of risk of being involved in money laundering or terrorist financing activities.

- Section 4.5 of the CBC Directive, requires credit institutions to ensure that their customer identification records as well as the information that form their business/economic profile remain completely updated throughout the business relationship. In this respect, credit institutions must examine and check on a regular basis the validity and adequacy of the customer identification data and information they maintain, especially those concerning high-risk customers.
- Despite the above and taking into account the level of risk, if at any time during the business relationship with an existing customer, a credit institution becomes aware that reliable or adequate data and information are missing from the identity and the business/economic profile of the customer, then the credit institution is expected to take all necessary action, by applying the customer identification and due diligence procedures, to collect the missing data and information, the soonest possible, so as to update and complete the customer's business/economic profile. The CBC monitors this process as part of its on-site inspections through the dedicated CDD/KYC audit program.
- Please refer to CBC's response to Question 1 above. Points B to G are relevant.

Measures taken by the credit institutions:

In March 2014, the Money Laundering Compliance Officers confirmed that their policies and procedures in relation to the update and review of customers' files and transactions have been reviewed and amended where it was needed, so as to be in line with the requirements of the CBC Directive.

A number of credit institutions confirmed that following the two special assessments their customers' files have been reviewed. One credit institution informed the CBC that it has established a KYC update unit within the compliance department that is assigned with the task of reviewing and updating the KYC data for high risk customers or whenever certain trigger events occur. A great number of credit institutions informed the CBC that they have amended or they plan to amend their IT systems so as to monitor and ensure that the review process is performed electronically. The CBC response to Question 7 is also relevant.

The larger credit institutions have adopted a structured program aimed at completing the review of all customers over the medium term, on a risk basis and are in the habit of keeping the CBC updated as to the progress achieved.

In this respect, during the on-site inspections of 2014/2015, it was established that credit institutions' policies and procedures are in line with the AML regulatory framework. In addition, it was evidenced that, based on the nature, size and complexity of credit institutions' business, different measures, systems and procedures are implemented to deal with this specific issue. For example, three major credit institutions established a dedicated team within the compliance unit for reviewing and updating the KYC data. Some institutions have upgraded their AML IT systems accordingly and some are in the process of calibrating their AML IT systems and monitoring procedures to ensure that these are in line with the risks identified during their Risk Assessment.

- 9. Banks should review their current staff training arrangements, both for client-facing staff and for the compliance function, and enhance the training where necessary to reflect best practice, taking into account in particular the types of higher-risk business that staff are liable to encounter. All banks should focus training, inter alia, on the importance of creating and regularly updating economic and business profiles of customers, ongoing monitoring,**

**and the identification of suspicion (particularly in the international business context).  
[Medium priority – 12 months and ongoing]**

**Response of the authorities:**

Measures taken by the Central Bank:

A) Article 58 of the AML Law requires persons carrying on financial or other business to establish adequate and appropriate systems and procedures to make their employees aware with regard to:

- (i) systems and procedures for the prevention of money laundering and terrorist financing,
- (ii) the AML Law,
- (iii) the Directives issued by the competent Supervisory Authority,
- (iv) the European Union's Directives with regard the prevention of the use of the financial system for the purpose of money laundering and terrorist financing.

Furthermore, Article 58(e) of the AML Law requires the regular training of staff to recognise and handle transactions and activities suspected to be related with money laundering or terrorist financing activities.

In addition section 8 of the CBC Directive requires of the Money Laundering Compliance Officer, in cooperation with other competent units of the credit institution (i.e. the Personnel and Training departments etc), to prepare and implement, on an annual basis, an education and training program for the staff as required by the AML Law and the CBC Directive. It is emphasized that the training programme should have a different structure for new staff, customer service staff, compliance staff, staff moving from one department to another or staff dealing with the attraction of new customers. The Money Laundering Compliance Officer is required to evaluate the adequacy of the seminars and the training provided to the staff and to maintain detailed records regarding the seminars/programs carried out.

B) Please refer to CBC's response to Question 1 above. Points B to G are relevant.

C) Seminars organized:

- On 18 March 2014, the CBC organized a seminar for the financial sector with the assistance of an external financial expert, to address issues such as EDD, the construction of business profile, monitoring of transactions, and reliance on business introducers.
- On 28 March 2014, the CBC in collaboration with MOKAS and an external firm organized a seminar to the Money Laundering Compliance Officers of all credit institutions. This seminar covered the recent changes to the legal and regulatory framework, tax crimes, construction and submission of SARs, and risk management systems.
- On 19 May 2014 the CBC in cooperation with the Cyprus Institute of Financial Services organized a seminar which covered highlights from the Moneyval and Deloitte special assessments, PEPs and their regulatory framework and tax crime as a predicate offence for ML purposes. In particular during that session the regulatory framework on tax crimes was explained as well as examples on legal tax structures/ business structures likely to be used for legitimate tax planning purposes in Cyprus.
- On 16 December 2014 the CBC in collaboration with an audit firm and with the assistance of

two external financial experts organised a Seminar on Risk Assessment. This seminar covered examples of methodology that can be used and the drafting of Risk Assessment Reports.

- On 16 & 17 February 2015, the CBC in cooperation with the Cyprus Institute of Financial Services and Global Training organised a two-day seminar which covered topics such as AML/CFT Compliance, Tax crimes, Trusts, Foundations, Funds and Fraud.
- On 28 & 29 September 2015, the CBC was a co-organizer of the Regional Alliance against Money Laundering and Terrorist Financing seminar of the World Union of Arab Bankers.

Measures taken by the credit institutions:

In March 2014, the Money Laundering Compliance Officers confirmed that they organised in-house seminars to their staff covering inter-alia, the weaknesses identified during the two special assessments. Moreover, the majority of them confirmed that they and/or the compliance staff attended seminars in Cyprus or abroad.

In addition, most credit institutions delivered seminars to their staff in relation to the new legal and regulatory requirements and on the latest developments in AML/CFT matters.

It should be noted that detailed information on training courses/seminars attended by the Money Laundering Compliance Officer, his/her assistants and the staff, whether in-house or external, are included in the Money Laundering Compliance Officer's Annual Report and are reviewed by the responsible officers.

During onsite examinations carried out in 2014 and 2015, it was established that tailored in-house seminars were organised in various credit institutions. In addition, it was established that Money Laundering Compliance Officers and compliance staff attended specialised seminars in Cyprus and/or abroad. As part of the on-site inspections, the CBC monitors the training activities of credit institutions through a dedicated audit program.

*The following supplemental recommendations are included as they are directly relevant to placing the banks in a position to implement effective CDD measures:*

- 10. The competent authorities should amend their directives to explain the new provisions on tax crimes (including tax evasion) as predicate offences to ML. Careful guidance needs to be given on the assessment of risk in this context, including on business structures likely to be used for tax evasion purposes. Guidance should also be given on the identification of suspicious activities related to domestic and foreign tax evasion [Medium priority – 6-12 months]**

***Response of the authorities:***

Measures taken by the authorities:

- Please refer to CBC's response to Question 1 above. Points B to E are relevant.
- All supervisory authorities from the financial and non-financial sector issued Guidelines to their supervisory entities, explaining the new provisions on tax crimes as predicate offences to money laundering. It should be noted that the said Guidelines issued by the other supervisory authorities are along the same lines with the one issued by the CBC.
- The following seminars have taken place during 2014 and 2015 in the financial and non-financial sector by each supervisory authority and in cooperation with the Cyprus FIU, MOKAS, in order to explain, inter-alia, the new provision of the law in relation to tax crimes.

- MOKAS in collaboration the CBC and an external firm organised a seminar to the MLCOs of all credit institutions on 28 March 2014. This seminar covered the recent changes to the legal and regulatory framework, tax crimes, construction and submission of SARs, and risk management systems.
- MOKAS in cooperation with CYSEC, the CBA and other organisations has organised two seminars on 9/5/2014 in Nicosia and on 26/7/2014 in Limassol which covered the AML Legislation and among other the requirements to report SARs, including the duty to report issues relating to tax crimes. Members of ICPAC were also invited and participated in the above seminars.
- The CBC in cooperation with the Cyprus Institute of Financial Services organised a seminar on 19 May 2014 which covered highlights from the Moneyval and Deloitte special assessments, PEPs and their regulatory framework, and tax crime as a predicate offence for ML purposes. In particular during that session the regulatory framework on tax crimes was explained as well as examples of legal tax structures as well as business structures likely to be used for legitimate tax planning purposes in Cyprus.
- MOKAS has delivered a seminar to the staff of Deloitte, one of the big audit firms, upon invitation on 16 June 2014. The seminar covered amongst others the AML Law, and the requirements to report STRs, including the duty to report issues relating to tax crimes.
- On 16 December 2014 the CBC in collaboration with an audit firm and with the assistance of two external financial experts organised a Seminar on Risk Assessment. This seminar covered examples of methodology that can be used and the drafting of Risk Assessment Reports.
- On 16 & 17 February 2015, the CBC in cooperation with the Cyprus Institute of Financial Services and Global Training organised a two-day seminar which covered topics such as AML/CFT Compliance, Tax, Trusts, Foundations, Funds and Fraud.
- On 28 & 29 September 2015, the CBC was a co-organizer of the Regional Alliance against Money Laundering and Terrorist Financing seminar of the World Union of Arab Bankers.

During CBC's onsite examinations it was established that several SARs were submitted to MOKAS whereby a suspicion of "tax crime" was raised. It is evident that the guidance provided to the financial sector through the Guidelines and various seminars raised the awareness of staff on the identification of suspicious activities related to tax crime.

**11. The accumulation of high risks has implications for the CBC's supervisory work, in particular in relation to those banks most exposed to such risks. The CBC should take these considerations into account and incorporate them appropriately when updating the CBC Directive. [Medium priority – 12 months]**

**Response of the authorities:**

Measures taken by the Central Bank:

- The CBC has strengthened and continues to strengthen its resources, especially within the supervision department. A separate AML/CFT Unit was set up in May 2013 to undertake AML/CFT supervision of credit institutions. Initially, this unit consisted of five persons plus the Head of the Unit and was reinforced with another person in October 2014, who joined on a fixed term contract. In March 2015 another person joined the unit to act as group leader and coordinator. The AML/CFT Unit requires to be strengthened by one more expert. The strengthening of staff arrangements of the AML/CFT Unit would assist in the timely completion of outstanding matters and facilitate the smoother organisation of the Unit's tasks for the short and medium term period.

- As already mentioned above, the CBC, with the technical assistance of the IMF, has designed and developed a risk-based assessment methodology and tools for offsite and onsite supervision, which are tailored to the business model adopted in Cyprus and particularly address the high risks inherent in this model.
  - In relation to offsite supervision, the CBC designed, developed, and adopted, a risk assessment methodology and tools that provide for:
    - a comprehensive analysis of inherent ML/TF risks within the following risk factors: customers, products & services, geographic locations/areas, and delivery channels;
    - an assessment of the internal control environment that should be in place to mitigate and/or control the inherent ML/TF risks, as identified and measured;
    - institutional risk profiles;
    - specific AML/CFT supervisory strategies (adapted to institutional risk profiles).
  - In relation to onsite supervision, during 2014, the CBC conducted on-site inspections at 11 credit institutions, utilising the aforementioned methodology. The inspections were carried out by CBC AML/CFT Unit whose capacity and expertise was complemented by the use of external auditors selected via a tender procedure together with the assistance of financial experts from abroad. So far, during 2015, the CBC conducted on-site inspections of 13 credit institutions and is scheduled to complete this cycle with an additional on-site inspection in December 2015. The 2015 inspections were also carried out with assistance from external audit firms selected via a tender procedure. The scope of the audit firms' work was limited to CDD/KYC measures, under the full control of CBC, while all other audit programs were conducted by the CBC AML Unit's staff.
  - In addition to the above, during 2015 the CBC has conducted on-site inspections at four Payment Institutions and one E-Money institution.
  - The on-site inspection cycle will continue for 2016 in the same mode as for 2015. The tender process for the selection of the audit firms which will complement the work of the CBC has been initiated.
- Finally, the on-site inspection process is closely monitored as part of the quarterly Troika review.

**12. The Company Registry should be provided with the staff and other resources necessary to remove the backlog of amendments to company registration documents and to follow up unsubmitted annual returns and financial statements. [Medium priority – 12 months]**

**Response of the authorities:**

Measures taken by the Company Registry:

On the initiative of the Cyprus' authorities, a full third party assessment of the Department of the Registrar of Companies and Official Receiver (DRCOR) took place from September – December 2013, by the National School of Government International UK, Companies House UK and the Insolvency Service UK in collaboration with the authorities. The scope of the assessment was to assess, according to best practice, the processes and methods of the Department, its information and technology systems, its staffing and organisation and also to address the issue of the backlog and unsubmitted annual returns and financial statements.

Based on this work, an action plan was formulated for the reformation of the DRCOR, which was approved by the Council of Ministers on the 30.4.2014 aiming to restructure the Department according to best international practice with a specific timeframe for its implementation.

A Project Team, including a project manager, was assigned to this project, with the responsibility to design and promote all necessary actions regarding the implementation of the reformative measures.

Regarding the above recommendation, the following have been achieved.

- a. With additional staffing all backlog of amendments to company registration, comprising of approximately 40.000 documents, have been processed, while subsequent respective documents have been immediately processed so as not to create future backlogs.
- b. A team consisting of DRCOR staff has been set up to process all submitted annual returns while a procedure for striking off non-compliant companies on the Register, was initiated in September 2014. This was preceded by an awareness campaign through the media and service providers. Since the beginning of year 2014, 37.308 companies have been struck off the Register, while currently around 94.000 companies are in the final stage of the 3month notice for strike off, after publication in the Government Gazette. As a result of the compliance campaign, more than 314.000 overdue annual returns have been submitted at the DRCOR over the last year. It is expected that by the end of the first half of 2016, DRCOR will have a fully cleansed Register, providing accurate and current ownership information on all types of legal persons registered in Cyprus. In addition to this 'cleansing' process, a new policy and process are being developed for striking off companies that do not comply with their filing obligations. The new process includes the automatic generation of reminder letters, the imposition of fines where non-compliance persists, and the initiation of the strike off procedure after one year of non-compliance. This process is expected to be fully operational in 2016.
- c. Since the 20.2.2015, the online submission of the annual returns and financial statements has become mandatory.
- d. Amending legislation to the Companies Law has been formulated and enacted on the 19.6.2015, that has streamlined the registration, filing and strike-off processes for companies.

It should further be noted that the implementation of this action plan, is closely monitored as part of the quarterly Troika review.

**13. The supervisory regime for ASPs should be brought fully into effect as quickly as possible and the AML/CFT supervision of lawyers and accountants, in their role as business introducers, should be further strengthened. [Medium priority – 12 months and ongoing]**

**Response of the authorities:**

Measures taken by the authorities:

The supervisory authorities have enhanced their AML monitoring capacity by restructuring the supervisory department (Cyprus Securities and Exchange Commission), increasing the human resources (Cyprus Securities and Exchange Commission, Cyprus Bar Association and Institute of Certified Public Accountants of Cyprus). At the same time, all supervisors are working with specialised consultants towards the development of risk-based supervisory tools for offsite and onsite surveillance.

**CYSEC**

The supervisory regime for ASPs has come into full effect. CySEC is examining on an ongoing basis applications for authorisation – the application deadline for companies already offering those services was in July 2013.

A special section on the CySEC's website addresses frequently asked questions, which help interested parties in the application of the ASP Law. In the same context CySEC announcements are published on a regular basis to give guidelines on the Law or codify a procedure that needs to be followed. CySEC has been the guest speaker in seminars and meetings presenting and explaining the said Law. Competent Authorities have enhanced and strengthened their cooperation and are regularly meeting or communicating regarding common supervision principles and exchange of information, knowledge and knowhow. Following the enactment of the ASP Law, business introducers - for

banking purposes - can only be lawyers and accountants regulated by their respective Competent Authority or an ASP regulated by CySEC. CySEC has implemented its Risk Based Supervision Framework on ASPs and has already started carrying out onsite inspections of ASPs that have already received their CySEC authorisation. In addition, the CySEC decided on 5 October 2015 to assign the carrying out of AML/CFT on-site inspections of 16 TCSPs to two major audit firms.

### **ICPAC**

The AML/CFT Laws, as amended by Law no. 192(I)/2012 and Law no.: 101(I)/2013, redefine the definition of the accountancy profession, in order to capture all the activities of accountants and auditors.

Pursuant to these amendments, ICPAC, in its capacity as Supervisory Authority for the professional activities of members of ICPAC (including trust and company services to third parties) or general partnerships or limited partnerships or limited liability companies, whose general partners or shareholders and directors are members of the ICPAC, as well as any subsidiary company of such companies, has taken all appropriate measures to fulfill its task effectively.

To this end, the Institute of Certified Public Accountants for Cyprus (ICPAC) has engaged in the following actions:

- a. The AML Directive to the members of the Institute has been revised in September 2013 to accommodate all the latest relevant updates
- b. The Regulations of the Institute were also revised to take into account new provisions regarding the monitoring, supervision and disciplinary proceedings of the members
- c. ICPAC has outsourced the onsite inspection of its members to ACCA UK, which performs the AML audits on its behalf. The procedure and the staffing of this function has been enhanced.
- d. ICPAC set up a specific committee to handle the everyday affairs and business issues of its members that provide administrative services.
- e. After the enactment of the ASP Law, ICPAC issues separate practising certificates to individual and firms for the provision of administrative services. Each member who wishes to provide such services or act as a business introducer must hold such a certificate.
- f. A register of the members and of the firms providing administrative services is kept by the Institute, which is also available on its website. Registers are also maintained of the subsidiary companies of ASPs and of the persons employed by them.
- g. A number of training activities have been carried out in 2013/2014 and scheduled for the remainder of 2014 regarding AML and the provisions of administrative services. In 2013, the new ASP law, the revised AML Directive, the AML Law and aspects of suspicious transactions were presented in seminars; whilst in 2014 similar updated activities are being pursued, for the benefit of the members.
- h. The Institute has developed and finalised a risk based offsite surveillance tool for all its licensed firms.
- i. ICPAC is up-to-date with the requirements of the AML Action Plan imposed by Troika.

### **CBA**

Pursuant to the amendments to the AML/CFT Laws (L.192 (I)/2012 and L.101 (I)/2013) the CBA has been appointed as the competent authority for the supervision of trust and company services provided by CBA members.

To this end, the CBA has proceeded as follows:

- a. has strengthened its AML department which now consists of five (5) supervisors, who have received training on the newly developed onsite RBA methodology and attended several seminars as part of their training. For further details on staff training, as well as CBA members' training, please refer to Table 7.

- b. has revised its AML Directive accordingly and has issued a Directive which regulates the registration and supervision of Administrative Service Providers”, (edition: February 2013), revised in January 2015.
- c. has created a separate registry for ASPs regulated by the CBA which is posted on the CBA’s website. Also, CBA issues certificates to its members for the provision of administrative services.
- d. has developed and finalised a risk based offsite and onsite surveillance tools for all its members
- e. Is up-to-date with the requirements of the AML Action Plan imposed by Troika.

A detailed action plan, duly adhered to by the authorities, is part of the Memorandum of Understanding on Specific Economic Policy Conditionality for Cyprus (Annex 2 - [http://ec.europa.eu/economy\\_finance/publications/eeip/pdf/ip009\\_en.pdf](http://ec.europa.eu/economy_finance/publications/eeip/pdf/ip009_en.pdf) page 106 of the EC Report) in which specific enhancements to the AML framework are stipulated. In this specific action plan, various measures are stipulated with deadlines for implementation. These measures include amongst other, a) the development of a risk based approach in supervision by all competent authorities (on-site and off-site), b) the reviewing by the Central Bank of Cyprus of the framework relating to the use of introducers/third parties c) the on-going quarterly monitoring of the implementation of adequate AML supervision by the competent supervisory authorities. Subsequently, this process is closely monitored as part of the quarterly Troika review.