

ANTI - MONEY LAUNDERING

BACKGROUND

Pursuant to the recommendations made by the Financial Action Task Force (FATF) on anti-money laundering standards. SEBI vide its Circular Ref No.: ISD/CIR/RR/AML/1/06 dated January 18, 2006 laid down broad guidelines on Anti Money Laundering Standards. As per the Circular, all the intermediaries registered with SEBI under Section 12 of the SEBI Act were advised to ensure that a proper policy framework on anti-money laundering measures was put into place.

WHAT IS MONEY LAUNDERING

Money Laundering can be defined as engaging in any financial transaction or series of transactions that involve income derived from criminal activity, transaction designed to conceal the nature or source of proceeds derived from illegal activities including drug trafficking, smuggling, terrorism, arms dealing, fraud, forgery and many other crimes.

Money laundering is a major threat to financial institutions and the economic stability of entire countries. Governments worldwide have introduced legislation to prevent it, including specific money laundering offenses and legally imposed requirements on institutions operating in their jurisdictions.

Money laundering is the process of moving illegally acquired cash through financial systems so that it appears to be legally acquired. When a criminal activity generates substantial profits, the individual or group involved in such activity route the funds to safe heavens by disguising the sources, changing the form, or moving the funds to a place where they are less likely to attract attention.

The adoption of this policy is aimed at increasing awareness of money laundering activity and its ill effects. Typically a person with dirty money has millions of ways of integrating the same with the white money in the Indian context. If he sets up a hotel, he can show as much sales as he wishes. However all this money has to come into financial assets at some stage. What the AML Act is trying to do is to reduce the menace. It is like putting the signals in place. The violators can at least be recognized and fined. It will not eliminate accidents, but one can hope for some discipline

THE MONEY LAUNDERING PROCESS

Money can be obtained illegally from various criminal activities like drug trafficking, terrorism, organized crime and fraud. As criminals attempt to conceal the true origin and ownership of the proceeds of their criminal activities and provide a legitimate cover for their source of income they usually follow three stages:

Placement - This is where the criminal proceeds are first-injected into the system. It is also the stage where those who are educated, briefed and alert to the process of money laundering, have the best chance of detecting what is happening and are thus best able to thwart and disrupt the process at the outset. At this stage, very often larger amounts of money are divided and distributed into smaller amounts to avoid suspicion and then paid into a series of bank accounts, arose to purchase securities, or life policies or other assets, sometimes many kinds of assets, all to achieve the prime purpose of being able to inject the tainted money or value into the legitimate mainstream financial/business system. Eg: A criminal having huge crime proceeds in form of cash, can deposit this cash in bank accounts maintained with difference banks, in the name of his relatives, friends and associates, in small amounts.

Layering - After the injection has taken place and the tainted money or value has entered and become mixed up in the main mass of money or value in the financial system, it is spun around different accounts, different names, different ownerships, plus different instruments and investments.

All these movements are designed to disguise the origins of the money or value and thus confuse those who might be attempting to trace the money or value back to the root, criminal source. Facilitated by the birth of electronic funds transfer technology the fast movement of funds through multiple jurisdictions often with different laws, creates major problems for investigators of identification, access and ultimately achieving successful prosecutions.

Integration - Placing the laundered proceeds back into the economy in such a way that they re-enter the financial system as apparently legitimate funds.

Integration means the reinvestment of those funds in an apparently legitimate business so that no suspicion of its origin remains and to give the appearance of legitimizing the proceeds

ANTI MONEY LAUNDERING ACT

In India, the Anti Money Laundering (AML) / Combating Financing of Terrorism (CFT) measures are controlled through the Prevention of Money Laundering Act, 2002 which was brought in force with effect from 1st July 2005. RBI, SEBI and IRDA have been brought under the PML Act, and therefore it will be applicable to all financial institutions, banks, mutual funds, insurance companies, and their financial intermediaries. The agency monitoring the AML activities in India is called Financial Intelligence Unit (FIU IND) and compliance is required by all financial intermediaries.

Further in terms of rules made under the Act, all intermediaries shall maintain a record of:

- All cash transactions of the value of more than rupees ten lakhs or its equivalent in foreign currency;
- All series of cash transactions integrally connected to each other which have been valued below rupees ten lakhs or its equivalent in foreign currency where such series of transactions have taken place within a month;
- all cash transaction where forged or counterfeit currency notes or bank notes have been used as genuine and where any forgery of a valuable security has taken place;
- All suspicious transactions whether or not made in cash;

NEED FOR A MONEY LAUNDERING POLICY

The purpose of this policy is to set out the prevention of money laundering commitments and obligations for Kapila Securities Pvt. Ltd. (hereinafter referred to as 'Company')

- This policy is based on the provision of the "Prevention of Money Laundering Act, 2002 and circular issued by SEBI and exchanges thereof".
- This internal policy sets out and establishes governing principles, broad guidelines and standards to be adopted by the Companies in order to protect the Companies from being used by any person to launder money.
- The purpose of this policy is to establish the general frame work for the fight against money laundering, terrorism, financial crimes and corruption,

The main aspect of this policy is "**customer due diligence process**" which mean.

- Obtaining sufficient information in order to identify persons who beneficially own or control securities account.
- Verify the customer's identity using reliable, independent source documents, data or information;
- Conduct ongoing due diligence and scrutiny of the transactions and account throughout the course of the business relationship to ensure that the transactions being conducted are consistent with the client risk profile/ financial status/ background

Client Due Diligence Process includes three specific parameters

- Policy for acceptance of clients
- Procedure for identifying the clients
- Suspicious Transactions identification & Reporting

CUSTOMER ACCEPTANCE POLICY

The following Customer Acceptance Policy indicating the criteria for acceptance of client shall be followed in the Company.

- No account should be opened in anonymous or fictitious/benami name(s) i.e. to say that anonymous or fictitious/benami customers shall not be accepted.
- No account should be opened or transactions conducted in the name of or on behalf of banned/suspended individuals, organizations, entities, etc. For the purpose, necessary cross checks must be made to ensure that the identity of a customer does not match with any person with known criminal background or with banned/ suspended
- No account should be opened if appropriate due diligence measures cannot be applied to a customer for want of verifiable documents on account of non co-operation of the customer or non-reliability of the data/information furnished to company

- Be Careful while accepting clients of special category- Such clients include the following Non Resident Clients, High Net worth Clients, Trusts, charities, NGOs and organizations receiving donations, Companies having close family shareholding or beneficial ownership, Clients in high risk countries (where existence / effectiveness of money laundering controls is suspect to be highly prevalent, Politically Exposed Persons (PEP), person of foreign origin, Companies offering foreign exchange offerings, Non-face to face clients, and, Current / Former Head of State, Current or Former Senior High profile politicians , Those with dubious reputation as per public information available, etc.

CUSTOMER IDENTIFICATION PROCEDURE

Customer identification means identifying the person and verifying his/her identity by using reliable, independent source documents, data or information. The Company need to obtain sufficient information necessary to establish, **to their satisfaction**, the identity of each new client, whether regular or occasional

- Verify its genuineness with website and verify the pan card copy with original and put “verified with original” stamp as a proof of verification.
- Check original documents before accepting a copy.

An indicative list of the nature and type of documents/information that may be relied for client identification are given below, Documents that may be obtained and verified from Clients

Client	Documents
Individual	
Proof of Identity	<ul style="list-style-type: none"> ➤ Passport ➤ PAN card ➤ Voter’s Identity Card ➤ Driving licence ➤ Government/ Bank/ PSU issued Photo Identity card
Proof of Address	<ul style="list-style-type: none"> ➤ Passport ➤ PAN card ➤ Voter’s Identity Card ➤ Driving licence ➤ Telephone bill (Not more then 3 months old) ➤ Bank account statement(Not more then 3 months old) ➤ Electricity Bill (Not more then 3 months old) ➤ Rent Agreement ➤ Flat Maintenance Bill ➤ Insurance Policy ➤ Ration Card
Corporate	<ul style="list-style-type: none"> ➤ Pan card copy of company ➤ Address proof of company ➤ Copy of Certificate of incorporation ➤ Memorandum and Articles of Association ➤ Shareholding pattern on company letter head ➤ List of Directors ➤ Certified true copy of Balance sheet last two financial years ➤ Latest income tax return filed

	<ul style="list-style-type: none"> ➤ Latest Net worth Certificate ➤ Photograph ,PAN Card, Address & ID proof of a whole Time Director/ Promoters/ individual who have 5% or more than 5% shares of company ➤ Board Resolution for the appointment of Authorized person who will operate the account. ➤ Proof of address and identity of authorized person
Partnership Firms	<ul style="list-style-type: none"> ➤ Photograph of all Partners ➤ Pan card copy of partnership firm ➤ Registration Certificate ➤ Address proof of Firm ➤ Certified true copy of Partnership Deed ➤ Pan Card, Address & ID proof of all partners ➤ Authorization letter for the person authorized to open and operate the account ➤ Annual Return/statement of the partnership firm
HUF	<ul style="list-style-type: none"> ➤ Photograph of the Karta ➤ Pan Card copy of HUF and Karta ➤ Address Proof of HUF ➤ Declaration from the Karta

CLASSIFICATION OF CLIENTS

Clients are classified into different risk categories (Low, Medium or High Risk) based on various parameters like client's location (registered office address, correspondence addresses and other address if any applicable, nature of business activity, trading turnover, manner of making payment for transactions undertaken, relationship, etc.)

Broadly speaking the following are the guidelines for classification of categories

Low risk client - includes clients who:

- Provide references
- No delegation of authority for operation of account
- Always provide securities and funds in time
- Places order within reasonable period of time
- Turnover in line with financials
- Deal only on Delivery Basis
- Low turnover with low financial income
- Government Employees Low
- Housewives
- Retired Employees
- Agriculture Sector

Medium risk client: Any client who cannot be comfortably placed in neither in Low risk nor in High Risk category

- Medium Turnover with corresponding financial income
- Top 20 (HNI Clients)

High risk client - includes all clients mentioned under Special category of clients and any client against whom any order is passed by regulatory authorities or any investigation is launched which is pending Any client against whom any regulatory order is passed for accessing market then such client will automatically be black listed and no further trading should be done for those accounts.

- 2 or more instances of bouncing of cheques
- High Brokerage with low financial income
- High Turnover with low financial income
- Doing large volumes in illiquid scrips
- Advocate Clients
- Builder Clients
- Politician Clients
- Any large activity in Dormant Account

Clients of special category (CSC) include the following

- Non resident clients
- Trust, Charities, NGOs and organizations receiving donations
- Companies having close family shareholdings or beneficial ownership
- Politically exposed persons (PEP) of foreign origin
- Current / Former Head of State, Current or Former Senior High profile politicians and connected persons (immediate family, Close advisors and companies in which such individuals have interest or significant influence)
- Clients in high risk countries (where existence / effectiveness of money laundering controls is suspect, where there is unusual banking secrecy, Countries active in narcotics production, Countries where corruption (as per Transparency International Corruption Perception Index) is highly prevalent,
- Countries against which government sanctions are applied, Countries reputed to be any of the following – Havens / sponsors of international terrorism, offshore financial centers, tax havens, countries where fraud is highly prevalent.
- Non face to face clients (with less personal interaction).
- Clients with dubious reputation as per public information available etc

Further client once categorized as low risk client can be later categorized as high risk or vice versa depending on the nature of transactions and client behavior and client owner periodical report of his/her client. Based on the client category the trading limits are defined in the front end system.

RISK PROFILING OF THE CLIENT

We should accept client on the basis of risk they are likely to pose. The aim is to identify the clients who are likely to pose higher than average risk of money laundering. For this purpose we need to classify clients as Low Risk, Medium Risk and High Risk Clients. By classifying the clients we will be in a better position to apply appropriate customer due diligence process. That is, for high risk client we have to apply higher degree of due diligence and regular update of KYC profile. The factors of risk perception depend on client trading turnover, nature of transaction, manner of payment, client location and nature of business.

In order to achieve this objective, all clients should be classified in the following category.

- Category A- Low Risk
- Category B- Medium Risk
- Category C- High Risk

The clients of special category to classified even higher, such clients require high level of monitoring.

SUSPICIOUS TRANSACTIONS IDENTIFICATION & REPORTING

It is difficult to define exactly what constitutes suspicious transactions and as such given below is a list of circumstances where transactions may be considered to be suspicious in nature. This list is only inclusive and not exhaustive. Whether a particular transaction is actually suspicious or not will depend on the background, details of the transactions and other facts and circumstances.

- Identity of Client: Clients whose identity verification seems difficult or clients appear not to cooperate
 - False identification documents
 - Identification documents which could not be verified within reasonable time
 - Non face to face Client
 - Doubt over the real beneficiary of the account
 - Accounts opened with names very close to other established business entities.
- Multiple accounts
 - Large number of accounts having common parameters such as common partners / directors / promoters / address / email address / telephone numbers / introducers or authorized signatories
 - Unexplained transfers between multiple accounts
- Sudden activity in dormant accounts
- Unusual activity compared to past transactions
- Source of funds are doubtful or inconsistency in payment pattern
- Multiple transactions of value just below the threshold limit specified in PMLA so as to avoid possible reporting;
- Client having suspicious background or links with known criminals
- Large deals at prices away from the market.
- Accounts used as 'pass through'. Where no transfer of ownership of securities or trading is occurring in the account and the account is being used only for funds transfers/layering purposes.
- Trading activity in accounts of high risk clients based on their profile, business pattern and industry segment.
- As a standard policy we do not deal in cash for any transactions – whether for purchase or for selling.
- We have been taking close surveillance, where transaction amounting to Rs.10 lacs or more.
- We accept cheques only from the designated bank accounts.
- We accept and deliver shares only to the designated DP accounts.

REPORTING OF SUSPICIOUS TRANSACTIONS

Company is required to maintain and preserve the following information in respect of transactions PMLA Rules:

- The nature of the transactions
- The amount of the transaction.
- The date on which the transaction was conducted
- The parties to the transaction.
- Origin of funds
- Destination of funds and securities.
- The reason of suspicion

RETENTION OF RECORDS

As per PMLA Rules records have to maintained and preserved for the period of 10 years from the date of transaction between the client and intermediary.

We have observed the following document retention:

- We are bound to maintain all necessary records, As per the guidelines of SEBI Act, Company has to keep the records such as Register of transactions (Sauda book), Clients' ledger, General ledger, Journals, vouchers, ledgers, registers, etc., pertaining to Transactions for a period of 5 years.
- We have also bound to kept records, if any on customer identification (e.g. copies or records of official identification documents like passports, identity cards, driving licenses or similar documents), account files and business correspondence for the same period.

In situations where the records relate to on-going investigations or transactions, which have been the subject of a suspicious transaction reporting, they must be retained until it is confirmed that the case has been closed.

EMPLOYEE TRAINING

We ensure continuous training of concerned employees (Compliance, Accounts, etc) in order to keep the systems updated as well as conform to the guidelines of the authorities as well as follow the company's policies to adhere to these guidelines.

- In addition random check done by top management.
- The AML programme is reviewed after every six months to ensure that it is compliant with the requirements of the PMLA and the implementing regulations under it.