

VB/AD – n°2016-50/Div

**European Securities and Markets Authority**

**European Banking Authority**

**European Insurance and Occupational Pensions Authority**

Paris, 21th january 2016

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| **AFG response to the ESMA, EBA & EIOPA consultation on “ simplified and enhanced customer due diligence and the factors credit and financial institutions should consider when assessing the money laundering and terrorist financing risk associated with individual business relationships and occasional transactions” – JC 2015 061** |

**General comments**

The Association Française de la Gestion financière (AFG) [[1]](#footnote-1) is grateful to have the opportunity to respond to the Joint Committee of the European Supervisory Authorities’ consultation on the assessment of the money laundering and terrorist financing risk. AFG fully supports the authorities’ objective to to seek feedback from the stakeholders on this matter, which is of utmost importance. French asset managers are aware that they must fully participate to the fight against money laundering and terrorist financing and AFG is playing a very active role in helping them to perform their duties.

As a preliminary comment, it is worth recalling the principle laid out by the Directive allowing, upon justification provided by an EU management company, a modulated vigilance relying on a risk control. Hence, it is essential to give management companies the possibility to implement a scheme efficient, adapted and proportionate to their activities and organisation, without requiring control modalities which would prove disproportionate.

Sources of information n° 14 and following

The topic of sources of information is particularly important. The “bundled indicator” method certainly is the most efficient.

Sources of information n° 18 and following

* **Does the customer or beneficial owner have links to sectors that are associated with higher corruption risk, such as construction, pharmaceuticals and healthcare, arms trade and defense, extractive industries and public procurement? (n°19- 1)**

The sectors listed here encompass too widely entire economic areas. Even though it is indeed relevant to properly take this criterion into account, the latter cannot on its own be sufficient to consider as risky all the companies in the sectors listed.

* **Does the customer have political connections, for example, are they a Politically Exposed Person (PEP), or is their beneficial owner a PEP? Does the customer or beneficial owner have any other relevant links to a PEP, for example, are any of the customer’s directors PEPs and if so, do these PEPs exercise significant control over the customer or beneficial owner? Where a customer or their beneficial owner is a PEP, firms must always apply enhanced due diligence measures in line with Article 20 of Directive (EU) 2015/849. (n°19- 5)**

A global search for PEPs in the boards of directors or supervisory boards (“directors”) of clients seems a particularly heavy requirement. However, the search for PEPs among “directors” of clients is justified in the absence of a beneficial owner.

* **Is the customer’s or their beneficial owner’s background consistent with what the firm knows about their former, current or planned business activity, their business’ turnover, the source of funds and the customer’s or beneficial owner’s source of wealth? (n°19- 10)**

The proposed provisions seem unrealistic to us: not only is the collection of such type of prospective data from clients likely to prove difficult but also, even though the management company might obtain the planned business activity and business’ turnover from its client, such information would only be of a hypothetical nature.

* **Are there any adverse media reports about the customer, for example are there any allegations of criminality or terrorism (proven or not) against the customer or their beneficial owners? If so, are these credible? Firms should determine the credibility of allegations on the basis of the quality and independence of the source data and the persistence of reporting of these allegations, among others (n°20-1)**

The wording used here seems too general with the risk to capture, with the word “any”, unreliable sources. An adequate level of journalistic ethics and the existence of a recognised editorial line are necessary so that media reports may efficiently be taken into consideration; also, the issue of the presumption of innocence should be raised, and, in any case, it is not possible in practice to decipher and exploit all the media in the whole world in all languages. We therefore suggest to replace “any” by “strong”.

* **Are there indications that the customer might seek to avoid the establishment of a business relationship? (n°21- 2)**

This wording is too obscure and should be clarified.

* **Is there a sound reason for changes in the customer’s ownership and control structure? (n°21- 6)**

The sentence as worded here does not reflect the daily reality of people in charge of AML-CFT issues and of front office staff in management companies. The expression “sound reason” should be further defined.

* **Where the customer is a non-resident, could their needs be better serviced elsewhere? Is there a sound economic or lawful rationale for the customer requesting the type of financial service sought? (n°21- 11)**

It is impossible for a management company to have a global vision which would cover all the equivalent services of its competitors worldwide. We suggest to amend the proposed wording which may lead to confusion.

* **Is the jurisdiction a known tax haven, secrecy haven or offshore jurisdiction? (n°23- 5)**

It would be desirable to clearly identify the relevant categories; lists should be provided in order to clear any ambiguity.

* **Risk factors that may be relevant when considering the risk associated with a product, service or transaction’s transparency include:** 
  + **To what extent do products or services facilitate or allow anonymity or opaqueness of customer, ownership or beneficiary structures, for example certain pooled accounts, bearer shares, fiduciary deposits, offshore and certain onshore trusts and dealings with shell companies?**
  + **To what extent is it possible for a third party that is not part of the business relationship to give instructions, e.g. certain correspondent banking relationships? (n°26)**

Taking into account the form of investment in collective investment schemes, which are mostly held in bearer form, they should not systematically be considered as products facilitating anonymity. It would therefore be useful to specify that this does not concern mutual funds.

* **Where a firm does not develop automated systems to allocate overall risk scores to categorise business relationships or occasional transactions in house but purchases them from an external provider, it should understand how the system works and how it combines risk factors to achieve an overall risk score. Firm must always be able to satisfy itself that the scores allocated reflect the firm’s understanding of ML/TF risk and it should be able to demonstrate this to the competent authority. (n°35)**

It is important that the adequacy of the scheme is assessed taking into account the organisational choices made by the management company, which are by nature varied.

* **why the customer looks for a specific product or service, in particular where it is unclear why the customer’s needs cannot be met better in another way, or in a different jurisdiction; (n°57 ii- b)**

It is not possible for a management company to have a global vision which would cover all the equivalent products of all its competitors worldwide; furthermore, it is not its aim to address its clients to competitors. In our opinion, this sentence should be removed.

**CHAPTER 8**

This chapter aimed more specifically at management companies seems to provide a clear approach of the profession of asset management. We suggest however to clarify a few points.

The customer’s behaviour

* **the circumstances in which the customer makes use of the “cooling off” period gives rise to suspicion; (n°194- 6)**

Points raised in no 193 (Product, service or transaction risk factors) & points 1 to 5 in no 194 (Customer or investor risk factors) are well-known; however, we wonder about the notion of “cooling period”.

* **using multiple accounts without previous notification, especially when these accounts are held in multiple or high risk jurisdictions. (n°194- 7)**

Using several accounts is not in essence indicative of a particularly high risk; “especially” should be removed.

The customer’s nature (page 74)

* **the customer is an unregulated fund who carries out little or no due diligence on its underlying investors;**

The wording used here is more relevant to the British than to the French framework. We call for the considered legal structure to be formally specified in relation to the French context (regulated management company managing a non regulated fund).

* **the customer is an unregulated third party investment vehicle, for example a hedge fund;**

The wording used here is more relevant to the British than to the French framework. The definition of what is understood under “hedge fund” is missing.

**The customer’s business, for example the customer’s funds are derived from business in sectors that are associated with higher financial crime risk. (Page 74)**

The issue arises of activity sectors defined very widely (please refer to 19-1), leading in particular to the question of companies operating in these sectors and listed on a regulated market of the EU.

* **The following factors may indicate lower risk (n°196)**
* **the customer is an institutional investor whose status has been verified by an EEA government agency, e.g. a government-approved pensions scheme;**
* **the customer is a government body from an EEA jurisdiction.**

To the extent that we move from a system including exemptions to a system whereby only lower risks remain, it seems essential that the latter are further developed. All regulated entities should be qualified as low risk.

With reference to our regulation the following may be pointed out:

* Banking institutions
* Insurance companies and brokers
* Pension institutions
* Mutual societies and companies engaged in insurance, re-insurance or capitalisation activity
* The French central bank
* The Institut d’émission d’outre-mer
* Investment firms (except for investment management companies)
* Credit institutions having their head office in a Member State of the EEA
* Legal persons whose indefinitely, jointly and severally liable members are credit institutions which have their head office in the EEA
* Legal persons having their head office in metropolitan France or in overseas departments of France or in Saint-Barthelemy or in Saint-Martin and whose main or single purpose is the clearing of financial instruments
* Market undertakings
* Central securities depositories and securities settlement system managers
* Financial investment advisers
* Intermediaries acting on behalf of third parties which own financial securities
* Investment management companies in relation to the investment services they perform or in relation to the distribution of units or shares of collective investment schemes whether they manage the latter or not
* Bureaux de change
* Natural or legal persons which, on a usual basis, perform operations relating to the real property of third parties
* Legal representatives and directors responsible of casinos and groups, clubs and companies which organise gambling activities, lotteries, bets, sports and racing betting activities
* Persons which, on a usual basis, trade or organise the sale of precious stones, precious goods, antiques and works of art
* Companies providing banking services with respect to payment which are exempt from authorisation by the Autorité de contrôle prudentiel
* Certified public accountants and employees who are authorised to perform the profession of certified public accountant
* Lawyers at the Council of State and at the Court of Cassation, lawyers, avoués at courts of appeal
* Notaries
* Court bailiffs
* Administrators of justice and judicial representatives
* Judicial auctioneers and public auction sales companies
* Persons performing the activity of company domiciliation
* Listed companies

Country or geographic risk factors

* **the investor or their custodian is based in a high risk jurisdiction, including off-shore jurisdictions**

**(n°196-1)**

The notion of “off-shore jurisdictions” is not clearly defined; several definitions co-exist at European level.

* **Investment managers typically need to develop a good understanding of their customer, their customer’s circumstances and anticipated levels of transactions to help them identify suitable investment portfolios. This information will be similar to that firms will obtain for AML-CFT purposes. (n°197)**

It would be useful to clarify the notion of “anticipated levels of transactions”.

* **identify and, where necessary, verify the identity of underlying investors where the customer is an unregulated third party investment vehicle; (n°198)**

In case of an “unregulated third party”, our diligence measures will only cover the management company in charge of managing the vehicle (we have no visibility on the clients of this third party and will as a consequence be totally unable to implement this requirement).

**CHAPTER 9**

As a preliminary comment, it seems important to us to highlight the need to properly allocate the diligence measures between depositaries and management companies.

* **Investment funds can be abused for ML/TF purposes. Retail funds are often conducted on a non-face to face basis; access to such funds is often easy and holdings of investment funds can easily be transferred between different parties (n°201)**

In no way does the easy access to retail funds make them riskier. Retail funds, which are in any case subject to diligence measures by distributors and are strictly regulated, are not a concern.

Vehicles are in no way risky in themselves, it is the clientele which entails the AML risk.

Which concrete reality does this sentence refer to? The notion of “holdings of investment funds” is not understandable: if it refers to fund units, there is no secondary market for the retail segment in France. Such a transfer is impossible. Therefore, we cannot see which reality the following comment refers to: “investment funds can easily be transferred between different parties”.

Furthermore, in no way does the easy access to retail funds make them by nature riskier. Retail funds, which are in any case subject to diligence measures by distributors and are strictly regulated, are not a concern.

**It should be emphasised that in no way are vehicles risky in themselves in principle, it is the clientele which entails the AML risk, if there is to be any.**

* **The following factors may indicate higher risk:**
* **the transaction involves third party subscribers or payees, in particular where this is unexpected;**
* **the transaction involves accounts or third parties in multiple jurisdictions, in particular where these jurisdictions are associated with a high ML/TF risk. (n°203)**

The wording of this paragraph could be further detailed.

* **The following factor may indicate lower risk: third party payments are not allowed (n°204)**

It should be reminded that this is a responsibility of the depositary (a prohibition is not appropriate).

* **the circumstances in which the customer makes use of the “cooling off” period gives rise to suspicion; (n°205-6)**

We wonder about the notion of “cooling off period” (please refer to no 194-6).

* **The following factors may indicate higher risk: the fund admits a wide, or unrestricted, range of investors (n°207)**

A more precise definition would allow excluding in particular collective investment schemes.

In any case, we cannot rely on the principle that a retail fund would be riskier because it is open to all. Retail funds, which are in any case subject to diligence measures by distributors and are strictly regulated, are not a concern.

It should be reminded that in no way are vehicles risky in themselves, it is the clientele whichentails the AML risk.

* **The following factors may indicate lower risk:**
* **the fund admits only a specific type of low-risk investors;**
* **the fund can be accessed only through regulated financial intermediaries in EEA countries, who are within scope of their national AML-CFT legislation (n°208)**

It should be recalled that in France a management company which uses a regulated distributor lies outside the scope of the regulation for this distribution; only the distributor should comply with the AML-CFT obligations.

Furthermore, it seems difficult for a management company to ensure that only low risk investors subscribe to a fund, except for dedicated funds, which implies that all other funds would be considered as “high risk”. Cases which are outside the scope should be specified, with a description of the different types of business relationships.

In any case, diligence measures performed by management companies may only target distributors.

* **The following factor may indicate higher risk: investors’ funds have been generated in high risk jurisdictions, in particular those associated with higher levels of predicate offences to money laundering. (n°209)**

The word “generated”, too wide, would by nature relate to the business of very large listed companies. Indeed, in practice, it is simply impossible for a management company to make the link between the funds entrusted and the country of origin of these funds as far as multinational companies are concerned. At best, we will be able to ask the question to this type of clients and have to rely on a declarative statement (but then, of which use is this type of answer) or else our interlocutor will have no idea about it (which is very likely).

* **requiring that the redemption payment is made through the initial account used for investment; (n°210-4)**

Additional precisions would allow to helpfully restrict the wording (person change, listed country…). In any case, this requirement cannot be complied with at all times, for objective and matter-of-fact reasons, without implying a sensitivity zone with regards to AML-CFT : for example, clients which use several banks.

* **establishing limits on number and/or amount of transactions (n°210-5)**

Limits in terms of number and amount seem very/too sensitive to implement: not the same limit depending on the size of the clients’ assets and the nature of the funds? Fair treatment and best interest of unit holders? How would these limits be defined, on which criteria? The implementation of this point is not always possible, it seems that at least “where relevant” and the fact that the distributor is in charge of performing the relevant due diligence should be added.

Rather than a definition in terms of number and amount, the best solution for management companies certainly is to consider the commitment in their AML-CFT scheme to put in place alerts based on these criteria (number and amount of the transactions) considering their own risk-based approach according to the specificity of their clients and products.

* **obtaining approval from senior management at the time of the transaction when a customer uses a product or service for the first time (n°210-7)**

This provision should be limited to the start of business relationships with risky clients.

* **using anti-impersonation fraud checks to mitigate the risk of impersonation fraud where the relationship is conducted on a non-face to face basis. Examples include sending a letter to the customer’s address or applying additional verification measures (such as checking against online databases) to verify the existence of the purported identity (n°210-9)**

It would be desirable to specify that the choice to elect one or two measures in order to do so belongs to the management company.

* **Where a firm uses a financial intermediary to distribute fund shares, for example a regulated platform, a bank or a financial adviser, that intermediary may be regarded as the firm’s customer provided that the intermediary acts on its own account as the direct counterparty of the firm. This could be the case, for example, where the intermediary receives from its customer a mandate to manage their assets or carry out one or more investment transactions. In those situations, the firm should treat the intermediary’s customers as the fund’s beneficial owners. (n°212)**

In our opinion, this wording seems by nature to create confusion: it is important to recall that article 3 point 2d of the 4th Directive excludes from the scope of the AML-CFT collective investment undertakings which do not market their units or shares.

“on its own account” refers to a distributor; however, final clients of our distributors are not our clients.

2 cases may arise:

* + Either this intermediary acts on its own behalf and in such a case it is an investor client. The management company is fully responsible for the relevant due diligences and for the fight against money laundering;
  + Or this intermediary acts as a distributor and in such a case it also is a client of the management company; the investment management company should perform the relevant due diligences solely on its distributor. However, **the client of the distributor is not a client of the management company and the responsibility of performing due diligence on final clients fully belongs to the distributor.**

In addition, the significant costs implied by the implementation of AML-CFT processes for asset management companies should be recalled. In fact, considering that distributors are themselves subject to AML-CFT obligations, it seems useful in general to avoid any overlaps and costs that may be associated with a duplication of the AML-CFT work.

* **the ML/TF risk associated with the business relationship is low, based on the firm’s assessment of the financial intermediary´s business, the types of clients the intermediary’s business serves and the jurisdictions the intermediary’s business is exposed to, among others (n°213-2)**

It would be desirable to specify that in this case the relevant distributors do not invest in the management companies’ funds.

* **the firm is satisfied that the intermediary applies robust and risk-sensitive CDD measures to their own clients and their clients’ beneficial owners. It may be appropriate for the firm to take risk-sensitive measures to assess the adequacy of its intermediary’s CDD policies and procedures, for example by referring to publicly available information about the intermediary’s compliance record, liaising directly with the intermediary or by sample-testing the intermediary’s ability to provide CDD information upon request. (n°213-3)**

Cases whereby “sample testing” is used should be limited to situations whereby the management company performs an enhanced due diligence.

* **Where those conditions are met, and subject to applicable national legislation permitting this, SDD may consist of the firm: identifying and verifying the identity of its intermediary, including the intermediary’s beneficial owners (n°214)**

What is meant by “intermediary’s beneficial owners” should be specified (please refer to number 212).

1. The Association Française de la Gestion financière (AFG) represents the France-based investment management industry, both for collective and discretionary individual portfolio managements. 600 management companies are based in France. AFG members manage 3,000 billion euros, making the Paris fund industry a leader in Europe for the financial management of collective investments (with 1,500 billion euros managed from France, i.e. 19% of all EU assets managed in the form of investment funds). In the field of collective investment, our industry includes – beside UCITS – the whole range of AIFs, such as: employee savings schemes, regulated hedge funds/funds of hedge funds, private equity funds, real estate funds and socially responsible investment funds. AFG is an active member of the European Fund and Asset Management Association (EFAMA) and of PensionsEurope. AFG is also an active member of the International Investment Funds Association (IIFA). [↑](#footnote-ref-1)