

# INTRODUCTION TO CONCURRENT AUDIT

&

## KYC/ AML COMPLIANCES

SEMINAR ON  
CONCURRENT  
AUDIT  
WIRC,  
03<sup>RD</sup>

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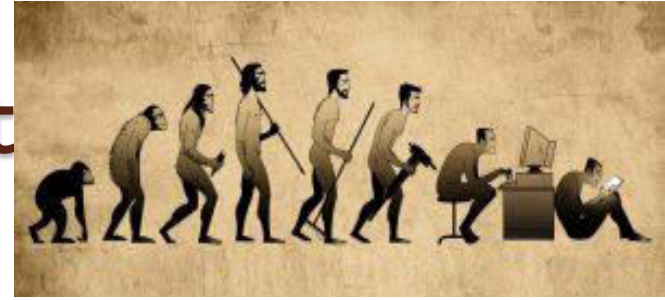
INTRODUCTION TO CONCURRENT  
AUDIT & KYC/AML COMPLIANCES

# What is Concurrent Audit of Bank



- Concurrent audit is a systematic and timely examination of financial transactions on a regular basis to ensure accuracy, authenticity, compliance with procedures and guidelines.
- It is an constant evaluation of the banking transactions to determine whether the internal control mechanisms are effectively working and simultaneously identify areas of improvement to enhance efficiency.
- Concurrent audit system is regarded as part of a bank's early warning system to ensure timely detection of irregularities and lapses, which also helps in preventing fraudulent transactions at branches.

# Evolution of Concurrent Audit in India



- concurrent audit was in existence in large and exceptionally large bank branches, it was formally introduced by the Reserve Bank of India *vide* its circular of October 1993. This measure of the Reserve Bank of India (RBI) arose out of the recommendations of the *Ghosh Committee on frauds and Malpractices in Banks*.
- In its said circular, the banking regulator explained concurrent audit as being “an examination which is contemporaneous with the occurrence of transactions or is carried out as near thereto as possible. It attempts to shorten the interval between a transaction and its examination by an independent person.”

# Objective of Concurrent Audit in Bank

- The primary objective of the introduction of a formal system of concurrent audits in banks was to serve as an administrative support to branches.
- The RBI circular also clarified that concurrent audit is essentially a management process.



**ANALYSE**

# Objective of Concurrent Audit in Bank

- To ensure compliance of laid down systems and procedures.
- To examine books of accounts, records and registers to ensure that they are maintained in accordance with the prescribed systems.
- To ensure adequate measures are being taken in advance to prevent future frauds, etc., to avoid difficulties, which may arise.
- To detect and arrest any leakage of income, if any. Evaluating the quality of customer services provided and giving useful suggestions.
- To assess overall performance of the branch while assessing productivity and profitability and to offer useful comments on the basis of audit conducted. Restriction of matter discussed on the spot with the help of concerned official.
- To report any inefficiency in any operational level.

# Objective of Concurrent Audit in Bank

- To scrutinize the completeness of documents submitted for availing advances and other facilities and physical checking of stocks and other assets at relevant places.
- **To follow up with authorities to ensure timely rectification of irregularities reported which were not rectified on the spot.**
- Verify prompt timely and regular submission of the periodical and statutory returns.

# Types of banking institutions prevailing in India:

- Presently, the following types of banking institutions prevail in India:
  - Commercial Banks
  - Regional Rural Banks
  - Co-Operative Banks
  - Development Banks more commonly known as 'term-lending institutions'
  - Payment banks
  - Small finance banks



# Commencement of Concurrent Audit

- checklist or flow till commencement is given below:
  - On receipt of appointment letter:
    - Write for No Objection to the immediate previous auditor
    - Send Acceptance letter along with statement of Fidelity, Confidentiality etc.
    - Contact the respective Branch Manager – for programme, arrangement and status report
  - To carry with branch during their visit to the branch:
    - Authorization Letter
    - Necessary guidelines
    - Various Formats
    - Letter head of the branch
  - Audit Programme
    - Allocation of work
    - Commencement of the work as per schedule given in subsequent paragraphs



# **Banking Products and services**

- Acceptance of Deposits
- Granting of Advances
- Remittances
- Collections
- Receipt of Foreign Contribution on behalf of the Registered Persons/Organization
- Cash Management Product
- Issuance of Letters of Credit and Guarantees
- Merchant Banking Business
- Credit Cards

# Banking Products and services

- Technology-based Services
- Dividend/ Interest/ Refund Warrants
- Safe-keeping Services
- Lockers
- Handling Government Business
- Depository Participant (DP) Services
- Automated Teller Machine (ATMs)
- Exchange of Notes
- Debit Cards
- **Auto Sweep Facility in Saving Account**

# Banking Products and services

- Reverse Mortgage
- Prepaid Payment Instruments in India
- **Para-banking Activities**

*Equipment Leasing, Hire Purchase and Factoring Services*

*Mutual fund business*

*Money Market Mutual Funds (MMMFs):*

*Entry of banks into Insurance Business*

*Primary Dealership Business*

*Pension Funds Management*

*Portfolio Management Services*

# Deposits

- The Bank accounts are broadly classified into the following categories:
  - Savings Deposit;
  - Current Deposit;
  - Fixed Deposit;
  - Recurring Deposit;
  - Saving cum fixed deposit/Swift A/C;
  - Non-resident Account; etc

# Advances

- **Various Forms of Credits**
  - The advances made by banks are, normally, in the following forms:
- Cash Credit
- Overdraft
- Loans
- Loans can be either secured or unsecured.

# INTERNAL CONTROL IN BANKS

- The system of internal control extends beyond those matters which directly relate to the functions of the Banking systems. The functions are classified as under:
  - Credit Function:
    - Exercise of Loaning Powers.
    - Pre sanction Appraisal.
    - Documentation
    - Creation of Charges
    - Creation of Mortgage
    - Post Sanction monitoring and follow up.
    - Non fund based limits scrutiny and proper treatment of its reversal.
    - FOREX functions- whether as per FEMA guidelines and banks internal procedure.

# INTERNAL CONTROL IN BANKS

- Non Credit Function:
  - Balancing
  - Cash Management.
  - Currency Chest
  - Remittance in transit
  - ATM
  - Bankers account and clearing.
  - Suspense and sundries.
  - Daily monitoring system.
  - Account opening and KYC.
  - Conduct and Maintenance of accounts.
  - Security forms inventory.
  - Bills for Collection/Demand draft.
  - Government Business.
  - Safe deposit vault.

# INTERNAL CONTROL IN BANKS

- Customer service
- Computer functions:
  - Environmental Controls.
  - Physical and Logical Controls
  - Maintenance and Business controls.
  - Network Control.
  - Operational Control.



# INTERNAL CONTROL IN BANKS

- Compliance Functions
  - Inspection report.
  - Return submission.
  - Communication & response.
  - Regulatory compliance.
- Branch Management.
- Security

# Internal control procedures

- Internal control procedures of a bank, generally, fall under the following categories:
- Delegation of powers
- Authorization of transactions
- Segregation and rotation of duties
- Maintenance of adequate records and documents
- Accountability for and safeguarding of assets
- System configuration and account mapping
- Independent checks
- Identification of Customer

# VIGILANCE FUNCTION IN BANKS

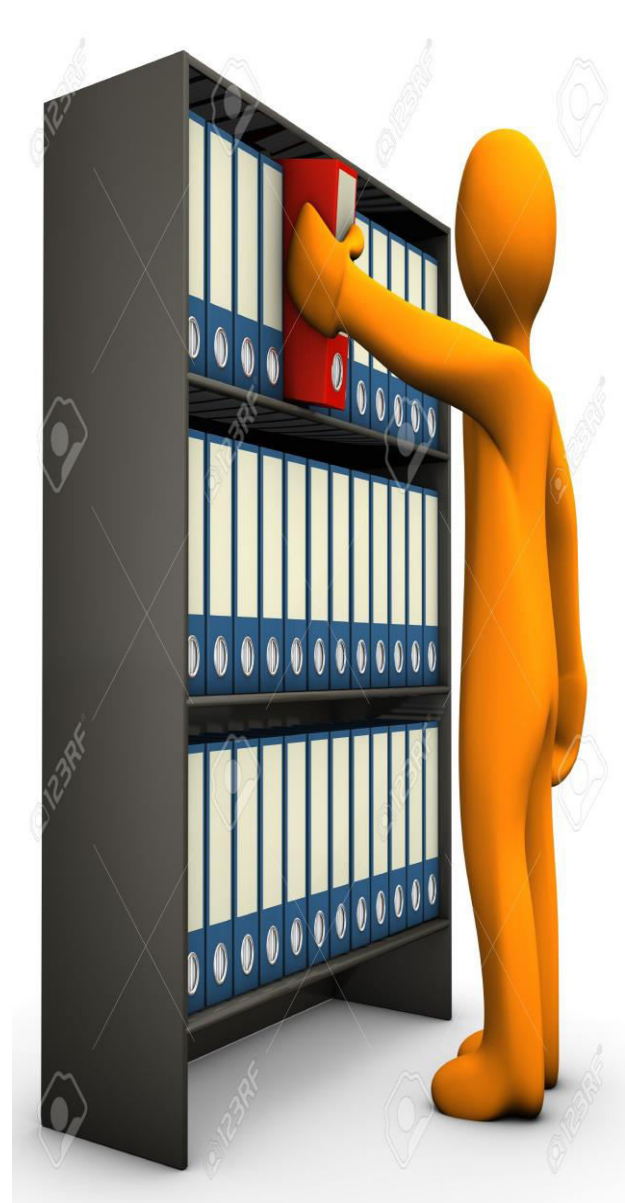
- **Inspection**
  - Branch Inspection
  - Head Office Inspection
  - RBI Inspection
- **Internal Audit Function in Banks**
  - Revenue Audit
  - Stock and Receivable Audit
  - Credit Audit
  - Risk Based Internal Audit
- **Information Systems (IS) Audit**
- **Forensic Audit**

# COVERAGE

- RBI vide circular (RBI/2015-16/133DBS.CO.ARS.No. BC. 2/08.91.021/2015-16) has stated that Concurrent audit at branches should cover at least 50% of the advances and 50% of deposits of a bank. The following branches, business activities/verticals of a bank may be subject to concurrent audit:
- Branches rated as high risk or above in the last Risk Based Internal Audit (RBIA) or serious deficiencies found in Internal Audit.
- All specialized branches like Large Corporate, Mid Corporate, exceptionally large/very large branches (ELBs/VLBs), SME.
- All Centralised Processing Units like Loan Processing Units (LPUs), service branches, centralized account opening divisions, etc.
- Any specialized activities such as wealth management, portfolio management services, Card Products Division, etc.
- Data Centres.
- Treasury/branches handling foreign exchange business, investment banking, etc. and bigger overseas branches.
- Critical Head Office Departments.
- Any other branches or departments where, in the opinion of the bank, concurrent audit is desirable.

# Working File

- The concurrent auditor should keep all the working papers on record which are used in finalizing the reports. The following papers can be kept in permanent audit file:
  - Letter of engagement, undertaking/comment by the firm to the bank.
  - Audit checklist.
  - Information regarding branch business, data, nodal officer, status of branch, whether computerized/parallel category of branch, etc.
  - Performance of monthly, quarterly, annual report revenue report.
  - Correspondence with the bank for any matter.



# Working File

- the current audit file may include all other papers relevant to the concurrent audit, for example:
  - Branch Audit Programme.
  - Branch's statement as on the data of the report on which basis it is prepared.
  - Periodic correspondence with the concerned departmental officer.
  - Irregularities intimated to the Controlling Officer.
  - Discussion of the audit report.
  - Particulars of big borrowers, depositors, etc.
  - Circulars received from head office of the audited bank.

# Commencement of Concurrent Audit

- The concurrent auditor would, therefore need to the following documents in particular before the commencement of the audit.
  - The appointment letter together with the management circular/ instruction on the subject.
  - Acceptance Letter
  - Communication to previous auditor

# Other Important Areas to be Covered

- Coverage of all the Vital Areas
- Regularity of Verification
- Emphasis of Concurrent Audit
- Maintenance of Records
- Reporting Method.
- Rectification of Irregularities



# Audit Programme



- A concurrent audit programme listing the procedures essential for meeting the objective of the concurrent audit plan.
- The concurrent audit programme identifies, in appropriate details, the objectives of the concurrent audit in respect of each area, the procedures to be performed to achieve those objectives, the staff responsible for carrying out the particular activity, the time allocated to each activity as also the sufficiently detailed instruction to the staff as to how to carry out those procedures.

# Audit Programme

- The concurrent audit programme may also have provision for information, such as, the procedures actually performed, reasons for not performing the originally identified procedures, actual time consumed in carrying out the relevant procedure, reasons for deviations from budgeted time, etc.
- A well-prepared, comprehensive audit programme helps proper execution of the work as well as of the proper supervision, direction and control of the performance of the engagement team

# Audit Planning and Documentation

- The concurrent auditor should document matters which are important in providing evidence that the concurrent audit was carried out in accordance with the basic principles of an audit and as per terms of reference.
- The concurrent auditor should record the audit plan as per the checklist and the format of audit report given by the respective bank's circulars, terms of engagement, scope of work, etc., and the engagement letter should also be taken into consideration in this regard

# MINIMUM AUDIT PROGRAMME FOR CONCURRENT AUDIT

- Minimum Audit Programme for Concurrent Audit has been prescribed in RBI Circular “Concurrent Audit System in Commercial Banks – Revision of RBI’s Guidelines” dated July 16, 2015, which is as follows

# AUDIT PROGRAMME-CASH TRANSACTIONS

- Physical verification on surprise basis of cash at branch and ATM along with safekeeping and custody.
- Ensure that there is no accumulation of large stocks of heavy cash and cut/mutilated/soiled notes, which otherwise need to be reported.
- If cash holdings are beyond the prescribed cash retention limit, the same also need to be reported
- The concurrent auditor would also need to verify whether cash is promptly remitted to the currency chest or to RBI and need be reported if the same is not being so deposited
- Short or excess cash , that needs to be reported
- Daily cash transactions, particularly any abnormal receipts and payments.

# AUDIT PROGRAMME-CASH TRANSACTIONS

- Surprise verification of cash by an officer other than the joint custodian.
- Proper accounting of and availability of insurance cover for inward and outward cash remittances.
- Accounting of currency chest transactions and delays/omission in reporting to RBI.
- Reporting of Counterfeit Currency.
- All cash transactions of Rs. 10 lakh and above reported in CTR.
- That all cash transaction of Rs. 50,000 and above invariably indicate Pan No./Form 60.
- RBI has issued Master Circular on the Scheme of Penalties for bank branches including currency chests based on performance in order to ensure that all bank branches provide better customer service to members of public with regard to exchange of notes and coins, in keeping with the objectives of Clean Note Policy.

# **CLEARING TRANSACTIONS**

- Reconciliation with bank's account at Clearing House and review of old outstanding entries for reconciliation.
- Drawings allowed against uncleared instruments - sanction by the controlling authority.
- Clearing difference adjustment, a/c is being balanced from time to time and no amount is outstanding for long period. The possibility of long outstanding amount may be proved to be fraudulent

# ***CLEARING TRANSACTIONS***

- Accounting of inward and outward clearing is being done on daily basis.
- In case of branch is handling clearing, the clearing account is reconciled to nil balance every day.
- Entries of Cheques returned by other banks is properly recorded in respective customer's account.
- Outstanding entries needs to be verify and the necessary action should be taken accordingly.



# **REMITTANCES/BILLS FOR COLLECTION – INWARD AND OUTWARD**

- Verification of funds by way of TC/NEFT/RTGS or any other mode in cash.
- Accounting of inward and outward remittance transactions is to be verified.
- Examination of service charges such as exchange, commission, expenses, interest, overdue interest etc are recovered.

# DEMAND DRAFTS

- Demand Draft's of Rs. 50,000/- and above are not to issued through accounts and not against cash.
- Verify the inward bills on hand which should tally with records.
- In case of returned bills, the same are to be debited to "Past Due and Dishonored Bills".
- Overdue bills should be properly followed up/ non-payment notices are served.

# DEPOSITS

- KYC/AML guidelines in opening of fresh accounts should be followed and monitoring of transactions in such accounts shall be carried on regularly basis.
- In case of no PAN available, Form No. 60 shall be held on record.
- Verify quick mortality accounts.
- Receipt/payment of term deposit beyond Rs. 20,000/- is made only through current/savings bank account. or by A/c payee cheque.

# DEPOSITS

- Inoperative/ dormant accounts shall be classified properly and operations in such dormant accounts are authenticated by the competent authority.
- Renewal procedure of term deposits should be verified and in case of auto renewal, the same has to be done on due date or else the same shall be closed.

# DEPOSITS

- Deduction of tax at source from interest income on term deposits shall be done as per laid down procedure.
- Settlement of claims of deceased customers and payment of TDRs against lost receipts and obtention of indemnities, etc. has to be as per prescribed guidelines.

# DEBIT BALANCE IN SAVING AND CURRENT ACCOUNT

- Outstanding debit balances in savings and current account has to be verified and accordingly the same are to be reported.
- Interest on such debit balances is promptly recovered.

# ISSUE OF CHEQUE BOOKS/CARDS ETC

- Verification of procedures for issuing of cheque books/cards and the same is accordingly followed.
- In case of Cheque books delivered to third person and necessary precautions as mentioned below are taken. Authority letter bearing an attestation of signature of the person who is authorized to collect the cheque book, by the customer should be obtained.
- Customer signature of said letter should be verified by the bank official.
- Account holder is informed accordingly through SMS on mobile wherever possible.

# ISSUE OF CHEQUE BOOKS/CARDS ETC

- Physical verification of ATM cards, debit cards, credit cards, passwords and PINs, control over issue & delivery, safe keeping and custody at all the locations.
- Physical verification of other deliverable items, control over issue, safe keeping and custody



# NOMINATIONS

- The nomination forms for deposits, lockers and safe custody shall be obtained as per prescribed norms.
- Details of nomination is entered properly in the system with authorization.
- Acknowledgement of having received and registered the nomination is issued to the customer.
- Nomination Register is properly maintained and posted upto date.

# LETTER OF CREDIT(LC)/BANK GUARANTEE (BG).

- LC/BG should be issued/amended as per the approved format/model guarantee prescribed and standard limitation clause incorporated.
- Verify whether counter indemnity obtained as prescribed.
- In case of any deviation from the terms of sanction in regard to margin, security, purpose, period, beneficiary, collection of charges, commission/fee, shall be reported accordingly.

# LETTER OF CREDIT(LC)/BANK GUARANTEE (BG).

- Whether payment is made to the debit of party's account on due date without creating overdraft/debiting suspense, in case of deferred payment guarantee

# HOUSEKEEPING

- Exceptional transaction reports are generated and verified by branch staff as prescribed.
- Review of all balance sheet heads and outstanding entries in accounts, e.g., suspense, sundry and inter-bank accounts. Review of follow up of entries pending for reversal.
- Scrutiny of daily vouchers with more emphasis on high value transaction including high value expenses and debit entries in Suspense account.
- 
- Debits in accounts where signatures are pending for scanning.
- 
- Whether records related to KYC/vouchers and other critical areas are sent to specific places like archival centre, record room as per stipulated periodicity.

# KNOW YOUR CUSTOMER



ANTI-MONEY LAUNDERING

**Deter. Detect.  
Prevent.**



INTRODUCTION TO CONCURRENT  
AUDIT & KYC/AML COMPLIANCES

# Know Your Customer (KYC)

- One of the most prominent area in a concurrent audit is verification of compliance of KYC & AML norms.
- KYC refers to the policies and procedures established by the Banks, Intermediaries and Financial Institutions (BIF) to ensure that banking system is not used by malafide people and criminal elements for money laundering activities

# KYC MEANS -

**Know your customer** (alternatively **know your client** or 'KYC') is the process of a business verifying the identity of its clients and assessing potential risks of illegal intentions for the business relationship.

The process of knowing your customer, is conducted either before or during the time that they start doing business with them.

# WHY KYC IS NECESSARY?

- KYC is mainly used to ensure that only qualified people have access to use a certain service. This is done so that minors, undocumented immigrants, or people with criminal histories are prevented from using the service.
- It also creates a database of information which law enforcement can use in their investigations in the case of some future criminal activity



# CUSTOMER

“Customer” may be defined as:

- A person or entity that maintains an account and/or has a business relationship with the bank;
- One on whose behalf the account is maintained (i.e. the beneficial owner);
- Beneficiary of transactions conducted by professional intermediaries, such as Stock Brokers, Chartered Accountants, Solicitors etc. as permitted under the law, and
- Any person or entity connected with a financial transaction which can pose significant reputation or other risks to the bank, say, a wire transfer or issue of a high value demand draft as a single transaction.

# FACTS ABOUT KYC

- The cost of AML compliance across U.S. financial services firms equaled \$25.3 billion per year based on survey responses from more than 150 decision-makers at banks, investment, asset management and insurance firms, according to LexisNexis Risk Solutions in its inaugural 2018 True Cost of AML Compliance report for the United States.

# FACTS ABOUT KYC

- The study found the True Cost of AML Compliance for European financial services companies equals US\$83.5 billion<sup>2</sup> (€70.1 billion).
- Source-Survey Edition of LexisNexis® Risk Solutions: THE TRUE COST OF ANTI-MONEYLAUNDERING COMPLIANCE-September 2017

# **PMLA AND KNOW YOUR CUSTOMER (KYC) POLICY**

- In terms of the provisions of Prevention of Money-Laundering Act, 2002 and the Prevention of Money-Laundering (Maintenance of Records) Rules, 2005, Regulated Entities (REs) are required to follow certain customer identification procedures while undertaking a transaction either by establishing an account based relationship or otherwise and monitor their transactions.

# KEY ELEMENTS OF ELEMENTS



# KEY ELEMENTS OF ELEMENTS

- **Customer Acceptance** – Customer Acceptance Policy should implement following regulations:
  - No account is opened in anonymous or fictitious/benami name.
  - No account is opened where the RE is unable to apply appropriate CDD measures, either due to non-cooperation of the customer or non-reliability of the documents/information furnished by the customer.
  - No transaction or account based relationship is undertaken without following the CDD procedure.
  - The mandatory information to be sought for KYC purpose while opening an account and during the periodic updation, is specified.
  - ‘Optional’/additional information, is obtained with the explicit consent of the customer after the account is opened.

# Customer Acceptance

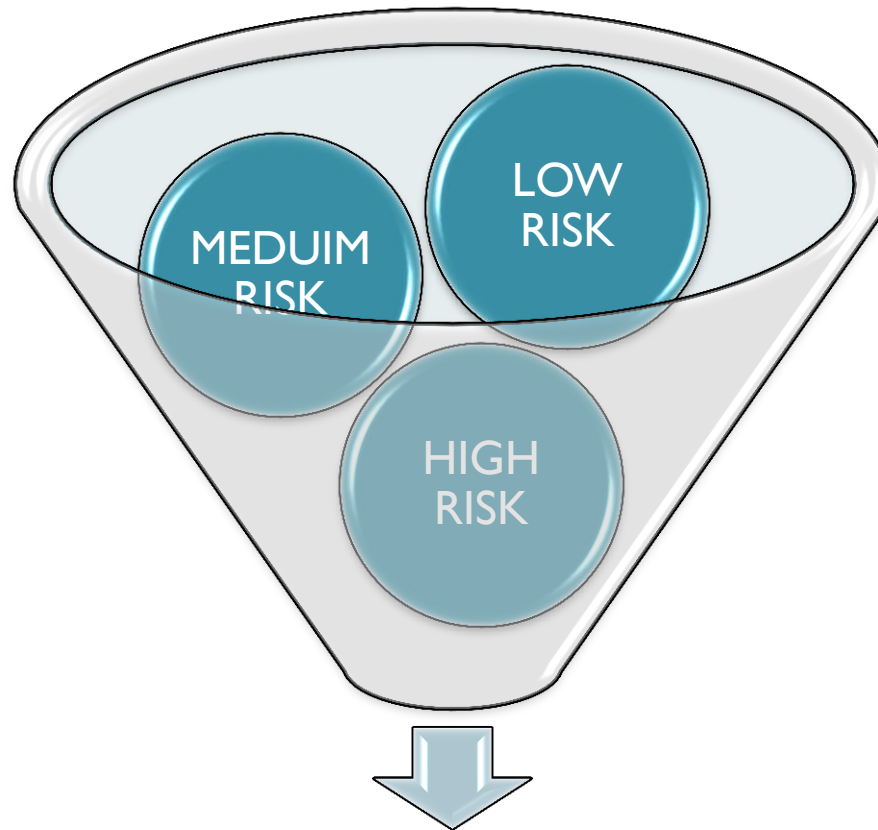
- An existing KYC compliant customer of a RE desires to open another account with the same RE, there shall be no need for a fresh CDD exercise.
- CDD Procedure is followed for all the joint account holders, while opening a joint account.
- Circumstances in which, a customer is permitted to act on behalf of another person/entity, is clearly spelt out.
- Suitable system is put in place to ensure that the identity of the customer does not match with any person or entity, whose name appears in the sanctions lists circulated by Reserve Bank of India.

# RISK MANAGEMENT

- Customers shall be categorized as low, medium and high risk category, based on the assessment and risk perception.
- Risk categorisation shall be undertaken based on parameters such as customer's identity, social / financial status, nature of business activity, and information about the clients' business and their location etc. No financial sector business is immune from the activities of criminal elements.
- The level of Money Laundering Risk that Bank is exposed to by a customer relationship depends on:
  - o Type of the customer and nature of business
  - o Type of product/service availed by the customer or
  - o Country where the customer is domiciled.



- Based on the above criteria, the customers are classified into three Money laundering Risk levels as follows:



**RISK CATEGORISATION**

# LOW RISK CUSTOMER

- All the customers who are not High/ Medium Risk customers are low risk customers.
- These are the type of customers whose identity and source of wealth can be easily identified and the transactions in whose accounts by and large conform to the known profile which are as under:
  - Salaried employees whose salary structures are well defined
  - People belonging to low economic strata of the society whose accounts show small balances and low turnover.
  - Government Departments and Government owned companies, regulators and statutory bodies etc.,
  - Customers who are employment-based or with a regular source of income from a known source which supports the activity being undertaken (this applies equally to pensioners or benefit recipients, or to those whose income originates from their partners' employment).
  - Customers with long term and active business relationship with the Bank (who are not coming under High / Medium Risk)
  - NPOs / NGOs promoted by United Nations or its agencies

# MEDIUM RISK CUSTOMER

- The indicative List of Medium risk customers is furnished hereunder:
- Non-Bank Financial Institution
- Stock brokerage
- petrol Import / Export
- Petrol/Diesel Station
- Car Dealership & Used car sales
- Electronics (wholesale)
- Travel agency
- Telemarketers & Providers of telecommunications service, internet cafe, IDD call service, phone cards, phone center
- Dot-com company or internet business

# MEDIUM RISK CUSTOMER

- Cash-Incentive Business such as Restaurants, retail shops, parking garages, fast food stores, movie theaters etc.
- Practitioners, (small, little known)
- Venture capital companies.

# HIGH RISK CUSTOMER

- Individuals or entities listed in the schedule to the order under section 51A of the Unlawful Activities (Prevention) Act, 1967 relating to the purposes of prevention of, and for coping with terrorist activities.
- Individuals and entities in watch lists issued by Interpol and other similar international organizations
- Customers with dubious reputation as per public information available or commercially available watch lists
- Individuals and entities specifically identified by regulators, FIU and other competent authorities as high-risk.
- Customers conducting their business relationship or transactions in unusual circumstances, such as significant and unexplained geographic distance between the institution and the location of the customer, frequent and unexplained movement of accounts to different institutions, frequent and unexplained movement of funds between institutions in various geographic locations etc

# HIGH RISK CUSTOMER

- Politically exposed persons (PEPs) of foreign origin, customers who are close relatives of PEPs and accounts of which a PEP is the ultimate beneficial owner;
- Non-resident customers and foreign nationals 10. Embassies / Consulates.
- Off-shore (foreign) corporation / business
- Non face-to-face customers
- High net worth individuals

# HIGH RISK CUSTOMER

- Firms with 'sleeping partners'
- Companies having close family shareholding or beneficial ownership
- Shell companies which have no physical presence in the country in which it is incorporated.
- The existence simply of a local agent or low level staff does not constitute physical presence.
- Investment Management/ Money Management Company / Personal Investment Company.
- Accounts for "gatekeepers" such as accountants, lawyers, or other professionals for their clients where the identity of the underlying client is not disclosed to the financial institution.
- Client Accounts managed by professional service providers such as law firms, accountants, agents, brokers, fund managers, trustees, custodians, etc

# HIGH RISK CUSTOMER

- Trusts, Charities, NGOs/NPOs (especially those operating on a cross-border basis) unregulated clubs and organizations receiving donations (excluding NPOs / NGOs promoted by United Nations or its agencies)
- Money Service Business: including seller of: Money Orders / Travelers' .
- Dealers in high value or precious goods (e.g. jewel, gem and precious metals dealers, art and antique dealers and auction houses, estate agents and real estate brokers). 26. Customers engaged in a business which is associated with higher levels of corruption (e.g. arms manufacturers, dealers and intermediaries).
- Customers engaged in industries that might relate to nuclear proliferation activities or explosives.



# RISK RATING REVIEW-

- All branches shall ensure maintaining and updating of customer risk profile on a continuous basis. A review of risk categorization of customers should be carried out at a periodicity of not less than once in six months.

# Parameters for Review

## Business Intelligence

- Customer Constitution
- Business Segment/Occupation
- Country of residence/nationality
- Product subscription
- Account status

## Transaction Type

- Cash
- Clearing
- Transfers/Remittances

## Transaction Trend

## AML Alerts/ Signals

# **BANKS SHOULD AVOID OPENING FOLLOWING ACCOUNTS**

Benami or anonymous accounts

Accounts of known criminals or banned entities

Shell banks

Pooled accounts on behalf of clients by Lawyers & Accountants who are bound by customer confidentiality

# Types of Customers

## Non Face to Face Customers

- Apply Enhanced procedures to mitigate the higher risk
- First payment to be effected through the customers account with another bank
- Presents a greater money laundering or terrorist financing risk- inherently difficult to ascertain the identify of the person

## Accounts of Politically Exposed Persons (PEPs)

- Gather sufficient information available in public domain.
- Seek information about sources of funds.
- Decision to open the A/c to be taken at senior level & mentioned in the form
- A/c subject to enhanced monitoring
- Same process to be applied to family members of PEPs

# CUSTOMER IDENTIFICATION

- While undertaking customer identification, bank shall ensure that:
  - (a) Decision-making functions of determining compliance with KYC norms shall not be outsourced.
  - (b) Introduction shall not be sought while opening accounts.
  - (c) The customers shall not be required to furnish an additional OVD, if the OVD submitted by the customer for KYC contains both proof of identity and proof of address.

# CUSTOMER IDENTIFICATION

- The second requirement of knowing the customer is to ensure that sufficient information is obtained on the nature of the business that the customer expects to undertake or any expected, or predictable pattern of transaction.

# PERIODICAL UPDATION OF KYC

- Branches would need to continue to carry out on-going due diligence with respect to the business relationship with every client and closely examine the transactions in order to ensure that they are consistent with their knowledge of the client, his business and risk profile and, wherever necessary, the source of funds
- KYC updation exercise will be required to be :
  - 2 /3 years for high risk accounts
  - 5 to 8 years for medium risk
  - 8 to 0 years for low risk
- The periodicity of updation of documents is to be done along with client's due diligence on annual basis

# PERIODICAL UPDATION OF KYC

- Physical presence of the clients may, however, not be insisted upon at the time of such periodic updation.
- Fresh photographs will be required to be obtained from minor customer on becoming major.
- Banks may not insist on physical presence of the customer at the time of periodic updating.
- Banks may not seek fresh documents if an existing KYC compliant customer of a bank desires to open another account in the bank.
- Do not seek fresh proof of identity and address at the time of periodic updation from the customer who are categorized as 'low risk' in case of no change in status with respect to their identity and address



# CUSTOMER IDENTIFICATION

- Necessary checks shall be applied before opening a new account so as to ensure that the identity of the customer does not match with any person with known criminal background or with banned entities such as individual terrorists or terrorist organizations etc.
- Branches shall not open an account where they are unable to apply appropriate customer due diligence measures i.e., branch is unable to verify the identity and/or obtain documents required as per the risk categorization due to non-cooperation of the customer or non-reliability of the data furnished to the bank

# CUSTOMER IDENTIFICATION

- Information to be collected for Customer Identification: Information collected at the outset for customer identification purpose to include
  - i) the purpose and reason for opening the account or establishing the relationship
  - ii) the anticipated level and nature of the activity that is to be undertaken
  - iii) the expected origin of the funds to be used within the relationship
  - iv) Details of occupation / employment to be sought for bank accounts and sources of wealth or income will be required for some banking relationships

# CUSTOMER IDENTIFICATION

- Features to be verified and documents that may be obtained from customers. Branches / Offices are advised to note the following for compliance:
- RBI , has clarified that the discretion given to the Banks in the clause " Any document notified by Central Govt" stands withdrawn and it should be "officially valid document".
- Further, RBI has clarified the list of officially valid documents as:
  - 1. Passport,
  - 2. PAN card,
  - 3. Driving license,
  - 4. Voter's Identity Card,
  - 5. Job Card issued by NREGA and
  - 6. Letter issued by UIAI.

# CUSTOMER IDENTIFICATION

- Branches should invariably verify the Xerox copy of the document with the original and certify on the Xerox copy of the document that "Verified with original" under the signature of authorized official of the Branch.
- With regard to obtaining of two sets of KYC documents, i.e., one each for identity and address proof, the following are revised guidelines:

Single document for proof of identity and proof of address.

If the address on the document submitted for identity proof by the prospective customer is the same as that declared by him/ her in the account opening form, the document may be accepted as a valid proof of both identity and address (passport, PAN Card with covering letter, Driving Licence, Voter's ID Card etc.)

# CUSTOMER IDENTIFICATION

- Introduction not Mandatory for opening accounts:

Since introduction is not necessary for opening of accounts under PML Act and Rules or Reserve Bank's extant KYC instructions, branches may not insist on introduction for opening bank accounts of customers.

# CUSTOMER IDENTIFICATION

- Individual Non-Resident Accounts to be opened on the basis of the following documents:

Passport & Residence Visa Copies of these documents sighted in original by the bank official or duly attested by Banker/Notary Public/Indian Embassy/Employer to the satisfaction of the bank.

# CUSTOMER IDENTIFICATION

- Accounts of Foreign students studying in India: Branches shall open accounts of Foreign students studying in India under "NRO category" only as they are treated as "Non-Resident".
- The opening of the accounts by individual/s of Bangladesh Nationality shall be allowed by the branches , subject to satisfying itself that the individual/s hold a valid VISA and valid residential permit issued by Foreigner Registration Office(FRO)/Foreigner Regional Registration Office (FRRO) concerned.

# CUSTOMER IDENTIFICATION

- Minor accounts Often a family member or guardian would open an account for a minor. In cases where the adult opening the account does not already have an account with the Branch, the identification proof for that adult or any other person who will operate the account should be obtained.
- In case of self operated minor accounts in addition to the photograph and proof of age, the documents required to establish the identity and address as applicable in the case of individual be obtained.



# CUSTOMER IDENTIFICATION

- Societies/ Associations / Clubs

The following documents are to be obtained for opening accounts of Clubs, Societies and Associations wherever applicable:

- Resolution for opening of the account • A copy of Bye-laws
- Copy of certificate of registration in the case of registered clubs, societies and associations

# CUSTOMER IDENTIFICATION

- Salaried Employees:

In case of salaried employees, it is clarified that with a view to containing the risk of fraud, banks should rely on certificate / letter of identity/ address issued only from corporate and other entities of repute and should be aware of the competent authority designated by the concerned employer to issue such certificate / letter.

Further, in addition to the certificate / letter issued by the employer, banks should insist on at least one of the officially valid documents as provided in the Prevention of Money Laundering Rules (viz. passport, driving licence, PAN card, Voter's Identity card, etc.,) or utility bills for KYC purposes for opening bank accounts of salaried employees of corporate and other entities

# CUSTOMER IDENTIFICATION

- Joint Account:

In case of joint accounts, applicants who are not closely related to each other (as can be inferred from the Account opening form) would require to establish their identity and address independently.

## Married Woman Accounts:

As part of Customer Identification Procedure, while opening / transferring accounts of newly married women and allowing conversion of name & signature in the existing accounts of women upon marriage, Marriage Certificate, Notarised Affidavit or Clear photograph of the wedding and Address proof of the groom etc. along with additional information in prescribed formats are to be obtained.

# CUSTOMER IDENTIFICATION

- Walk-in-customers (non account based customers):

All transactions of walk-in customers pertaining to third party products are also subjected to KYC norms/AML measures as applicable to Banks products. NOTE: In terms of Clause (b) (ii) of Sub-rule (1) of Rule 9 of the PML Rules, 2005, Branches are required to verify the identity of the customers for all International Money Transfer operations.

With regard to reporting of transactions carried out by walk-in-customers, detailed instructions are furnished under "Reporting of Cash/Suspicious Transactions" .

# Hindu Undivided Family (HUF)

- HUF comes into being because of a particular concept under Hindu Law whereby all the members of the family reside together jointly, carry on a business activity jointly and hold the property jointly and therefore, it is termed as Hindu Undivided Family.
- The following documents are to be obtained for opening accounts of HUF:

Declaration from the Karta Proof of Identification of Karta

Prescribed Joint Hindu Family Letter signed by all the adult coparceners.

# CUSTOMER IDENTIFICATION

- Proprietary Concerns :

The following are the list of documents that shall be provided as activity proof by the proprietary concerns:

1. Registration certificate (in the case of a registered concern),
2. Certificate/license issued by the Municipal Authorities under Shop & Establishment Act, GST and Income Tax returns,
3. CST/VAT certificate

# CUSTOMER IDENTIFICATION

- Proprietary Concerns :
  - 4) Certificate/Registration document issued by Sales Tax/Service Tax/Professional Tax Authorities,
  - 5) License issued by the Registering Authority like Certificate of Practice issued by Institute of Chartered Accountants of India, Institute of Cost Accountants of India, Institute of Company Secretaries of India, Indian Medical Council, Food and Drug Control Authorities,
  - 6) Registration/licensing document issued in the name of the proprietary concern by the Central Government or State Government Authority/Department.
  - 7) Banks may also accept IEC (Importer Exporter Code) issued to the proprietary concern by the office of DGFT.
  - 8) The complete Income Tax Return (not just the acknowledgement) in the name of the sole proprietor where the firm's income is reflected, duly authenticated/ acknowledged by the Income Tax authorities and
  - 9) Utility bills such as electricity, water, and landline telephone bills in the name of the Proprietary Concern as required documents for opening of bank accounts of Proprietary Concerns

# CUSTOMER IDENTIFICATION

- COMPANY:
- For opening an account of a company, one certified copy of each of the following documents shall be obtained:
  - (a) Certificate of incorporation.
  - (b) Memorandum and Articles of Association
  - (c) A resolution from the Board of Directors and power of attorney granted to its managers, officers or employees to transact on its behalf.
  - (d) Officially valid documents in respect of managers, officers or employees holding an attorney to transact on its behalf.



# CUSTOMER IDENTIFICATION

- Partnership Firm

For opening an account of a partnership firm, one certified copy of each of the following documents shall be obtained:

(a) Registration certificate.

(b) Partnership deed.

(c) Officially valid documents in respect of the person holding an attorney to transact on its behalf.

# CUSTOMER IDENTIFICATION

- TRUST

For opening an account of a trust, one certified copy of each of the following documents shall be obtained:

(a) Registration certificate.

(b) Trust deed.

(c) Officially valid documents in respect of the person holding a power of attorney to transact on its behalf.

# CUSTOMER IDENTIFICATION

- AOP/BOI:

For opening an account of an unincorporated association or a body of individuals, one certified copy of each of the following documents shall be obtained:

- (a) Resolution of the managing body of such association or body of individuals;
- (b) Power of attorney granted to transact on its behalf;
- (c) Officially valid documents in respect of the person holding an attorney to transact on its behalf and
- (d) Such information as may be required by the Bank, to establish the legal existence of such an association or body of individuals

# CUSTOMER IDENTIFICATION

- The e-KYC service of Unique Identification Authority of India (UIDAI) shall be accepted as a valid process for KYC verification under the PML Rules, as
  - (a) the information containing demographic details and photographs made available from UIDAI as a result of e-KYC process is treated as an 'Officially Valid Document', and
  - (b) Transfer of KYC data, electronically to the bank from UIDAI, is accepted as valid process for KYC verification.

# MONITORING OF TRANSACTIONS

- Branches should pay special attention to all complex, unusually large transactions and all unusual patterns, which have no apparent economic or visible lawful purpose for the accounts where credit are made for unusual amounts.
- The background including all documents/office records/memorandums pertaining to such transactions and purpose thereof should, as far as possible, be examined.

# MONITORING OF TRANSACTIONS

- Transactions that involve large amounts of cash inconsistent with the normal and expected activity of the customer should particularly attract the attention of the Branch. Very high account turnover inconsistent with the size of the balance maintained may indicate that funds are being washed through the account.
- In case of an account already opened where a branch has not been able to apply appropriate KYC measures due to non-furnishing of information and/or non-cooperation by the customer, the branch should consider blocking of further transactions / closing the account or terminating the banking business relationship after issuing due notice to the customer explaining the reasons for taking such a decision.

# ISSUES IN KYC

- Rising KYC costs
- Regulation Changes and Compliance Issues
- Lack of skilled professionals
- Increased customer friction
- Improve frequency & quality of inspection
- Aggressive sales culture of banks

ANTI-MONEY LAUNDERING

**Deter. Detect.  
Prevent.**



INTRODUCTION TO CONCURRENT  
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# What is Money Laundering ?

- “Any act or attempted act to conceal or disguise the identity of illegally obtained proceeds so that they appear to have originated from legitimate sources”.
- In other words, it is the process used by criminals through which they make “dirty” money appear “clean”

# OBJECTIVE OF MONEY LAUNDERING.

- To prevent banks from being used, intentionally or unintentionally, by criminals for Money Laundering activities or terrorist activities.
- To enable banks to know/ understand their customer and their financial dealings better.
- To put in place a proper control mechanism for detecting and reporting suspicious transaction.
- It will also enhance fraud Prevention.
- To ensure compliance with guidelines issued by the regulators including FIU-IND & RBI

# MONEY LAUNDERING RISKS

Bank is exposed to the following risks:

- Reputational Risk; Risk of loss due to server impact on bank's reputation which is more valuable asset of the organization.
- Compliance Risk; Risk of loss due to failure to comply with key regulations governing the bank's operations

# KYC STANDARDS

- The key elements of policy are as under :
- CAP ( Customer Acceptance Policy )
- Risk management
- CIP ( Customer Identification Procedure )
- Monitoring of transactions

# Legislative & Regulatory Framework

- Prevention of Money Laundering Act, 2002 (PMLA, 2002)
- Recent Amendments in Prevention of Money Laundering Act (PMLA) & PML (Maintenance of Records) Rules
- Unlawful Activities (Prevention) Act, 1967
- Financial Action Task Force (FATF)
- Reserve Bank of India (RBI)
- Financial Intelligence Unit – India (FIU-IND)
- Indian Banks Association (IBA)

# Reporting Requirements

- Prevent banks/FIs from being used, intentionally or unintentionally, by criminal elements for money laundering or terrorist financing activities. In terms of the Rule 3 of the PML (Maintenance of Records) Rules, 2005

Banks are required to furnish following to the Director, FIU-IND

- Cash Transaction Report (CTR)
- Counterfeit Currency Report (CCR)
- Suspicious Transactions Report (STR)
- Not for Profit Organization Transaction Report (NTO)
- Cross Border Wire Transfer (CBWT/EFT)

Report	Periodicity	Description
CTR	15th day of succeeding month	<ul style="list-style-type: none"> <li>a) Cash transactions above Rs. 10 lakhs or its equivalent in foreign currency</li> <li>b) Cash transactions integrally connected to each other below Rs. 10 lakhs or its equivalent in foreign currency in a month</li> </ul>
CCR	15th day of succeeding month	<ul style="list-style-type: none"> <li>a) Cash transactions where forged or counterfeit currency notes or bank notes have been used as genuine</li> <li>b) Forgery of a valuable security or a document has taken place facilitating transactions.</li> </ul>
NTR	15th day of succeeding month	Receipts by NPOs of more than Rs. 10 lakhs or its equivalent in foreign currency
STR	Within 7 working days on the transaction being determined suspicious	<ul style="list-style-type: none"> <li>a) Based on 54 Red Flags issued by IBA</li> <li>b) Based on Law Enforcement Queries received by Bank</li> <li>c) Based on Media Reports &amp; Public Complaints</li> <li>d) Monitoring by employees</li> </ul>
CBWT	15th day of succeeding month	All cross border wire transfers of more than Rs. 5 lakhs or its equivalent in foreign currency where either the origin or destination of fund is in India

## SUSPICIOUS TRANSACTION

Transaction whether or not made in cash which, to person acting in good faith –





# GROUNDS FOR SUSPICION

- Activity in accounts
  - Unusual activity compared with past transactions
  - Sudden activity in dormant accounts
  - Activity inconsistent with what would be expected from declared business
  
- Identity of client
  - False documents
  - Identification documents which could not be verified within reasonable time
  - Accounts opened with names very close to other established business entities
  
- Background of client
  - Suspicious or links with known criminals
  
- Multiple accounts
  - Large number of accounts having a common account holder, introducer or authorized signatory with no rationale
  - Unexplained transfers between multiple accounts with no rationale
  
- **Nature & value of transactions**

# ALERTS FOR IDENTIFYING SUSPICIOUS TRANSACTION

- Alerts through AML Package
- Behavioral Alerts
- Notice/Letter from Law Enforcement Agency
- Adverse Media News
- 54 Red Flag Indicators by IBA
- CTRs & NTRs
- Monitoring Accounts of Multi Level Marketing Firms
- Beneficial Owner
- Trade Finance
- Overseas Forex Trading through Electronic /Internet Trading Portals
- Demat A/cs
- Locker Transactions

# CUSTOMER BEHAVIORAL INDICATORS

- Reluctancy to provide information
- Unusual curiosity
- Giving confusing details
- Refuse to give reason for a transaction
- Numerous deposits & withdrawals
- Avoiding contact with branch
- Unexpected repayment of loan
- Account with multiple institutions

# ISSUES IN MONITORING SYSTEM

- The software flags numerous transactional alerts.
- Monitoring non-automated parameter and training to be imparted to staff at the branch level
- Documentation of reasons for classifying a transaction as normal & not reporting is as STR
- Maintenance of audit trail to be in place for auditors to assess whether the process laid down on paper is being followed

# DEFICIENCIES IN IMPLEMENTING KYC – AML POLICIES

- Poor quality of data - false positives & less time to focus on the real risks
- Data scale is massive & diverse -Single view of client transaction missing
- Understaffed & Untrained Human Resources & lack of incentives to blow the whistle on black money
- Lack of support from strong processes & technology – use of data analytics
- Check Box approach
- Revenue generation pressure forcing dilution of norms.
- Profit maximization drives banks beyond core tasks, to hawk products such as equities, insurance & mutual funds.

# DEFICIENCIES IN IMPLEMENTING KYC – AML POLICIES

- No verification of customer's address or job. Risk assessment mostly re-actionary.
- Absence of robust & ongoing due diligence process – especially risk profiling
- Processes not implemented strongly during modifications
- Security around creation/ modification of client – account master not strong enough.
- Communication gaps between Marketing – Sales & Risk / Compliance – Centralized decentralized operations

# Measures to Deter Money Laundering

- Zero tolerance for KYC – AML breaches
- Tone at The Top – Walk the Talk -
- Consider ML risks in daily operations, develop new financial products, establish new business relationships & changes in customer profiling.
- Screening of employees before hiring & those accessing sensitive information
- Appropriate quality training to staff
- Quick & timely reporting of suspicious transactions
- Complaint resolution / Whistle Blower system

# TRANSACTION ABOVE RS.50000/-

- Banks are required to issue DD/MT/TT/ Travelers cheques for Rs.50000/- & above by following the proper due diligence and only by debit to customers' accounts or against payee's account cheques and not in cash.
- The same rule applied for sale of Third Party Products, Gold Coins, and sale of Foreign Exchange



# PAN (FORM 60/61) REQUIREMENT

IT Act rule 114B has made it mandatory PAN (Form 60/61 in the absence of PAN) for the certain banking transaction.

- 1. Opening of an account (other than basic saving);
- 2. An application for issuing Credit/Debit card;
- 3. Opening of Demat account;
- 4. Deposit/payment of cash exceeding Rs.50,000/day;
- 5. Amount exceeding Rs. 50,000/- or aggregating more than Rs. Five lac in a financial year;
- 6. Payment of cash by way of DD/PO aggregating more than Rs. 50,000/- in a financial year.

NB:- As per IT Act Rule 114D retain Form 60/61 for a period of six years from end of F/y of transaction.



**THANK YOU**  
**CA JIGNESH NAGDA**

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