

“KYC, Anti Money Laundering, Suspense account, Sundry Assets & Income Leakages”



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KYC



- Know Your Citizen
- Know your Client
- Know Your Customer



- What is KYC ?
 - KYC (Know Your Customer) is a framework for banks which enables them to know / understand the customers and their financial dealings to be able to serve them better.

- Why KYC ?
 - Banking operations are susceptible to the risks of money laundering and terrorist financing.

- How to do KYC ?
 - to follow certain customer identification procedure for opening of accounts and monitoring transactions of a suspicious nature for the purpose of reporting it to appropriate authority

Objective of KYC



- To prevent banks from being used, intentionally or unintentionally, by criminal elements for money laundering activities .
- To know/understand their customers and their financial dealings better which in turn help them manage their risks prudently.

Money Laundering and Financial Terrorism

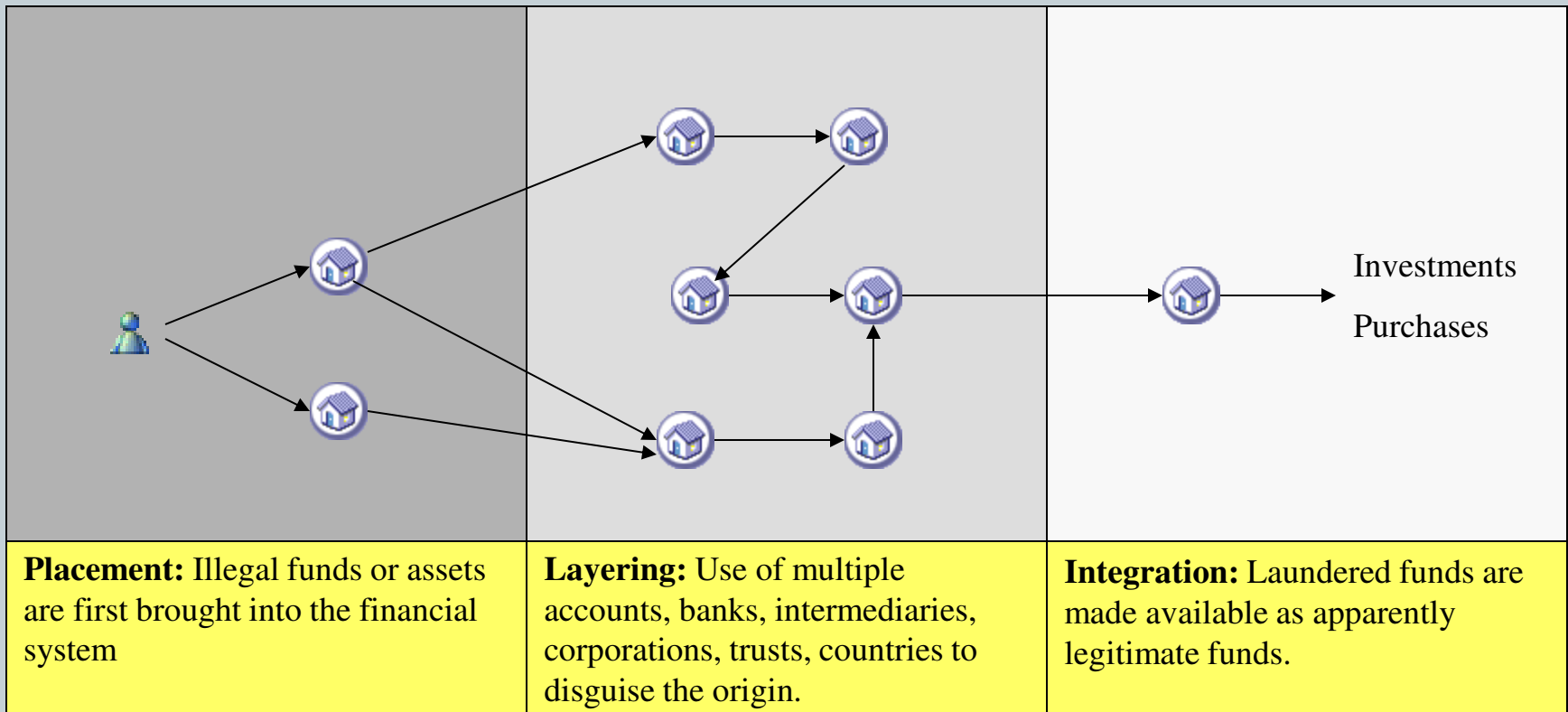


- Money laundering:
 - Money laundering refers to conversion of money illegally obtained to make it appear as if it originated from a legitimate source. Money laundering is being employed by launderers worldwide to conceal criminal activity associated with it such as drugs /arms trafficking, terrorism and extortion.
 - Money launderers send illicit funds through legal channels in order to conceal their criminal origin
- Financial Terrorism
 - Financial Terrorism means financial support to, in any form of terrorism or to those who encourage, plan or engage in terrorism.
 - Those who finance terrorism transfer funds that may be legal or illicit in original in such a way as to conceal their source and ultimate use, which is to support Financial Terrorism.

What is Money Laundering ?



Money Laundering is the process by which illegal funds and assets are converted into legitimate funds and assets.



Important: All money laundering transactions need not go through this three-stage process.

Legal Obligation under PMLA



PMLA and the Rules impose obligations on

- ✦ banking companies
- ✦ financial institutions
- ✦ intermediaries of the securities market

to

- ✦ maintain records
- ✦ furnish information
- ✦ verify identity of clients



- Reporting of Cash Transactions
- Reporting of Suspicious Transactions:
 - ✦ All suspicious transactions whether or not made in cash
 - ✦ STR should be filed with FIU within **seven** working days of establishment of suspicion at the level of Principal Officer.

Suspicious transaction



- Suspicious transaction means a transaction whether or not made in cash which, to a person acting in good faith –
 - gives rise to a reasonable ground of suspicion that it may involve the proceeds of crime; or
 - appears to be made in circumstances of unusual or unjustified complexity; or
 - appears to have no economic rationale or bonafide purpose;

Reasons for Suspicion” for banking companies

- **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 identification 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 background 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

Reasons for Suspicion” for banking companies (Contd.)



- **Nature of transactions**
 - Unusual or unjustified complexity
 - No economic rationale or bona fide purpose
 - Frequent purchases of drafts or other negotiable instruments with cash
 - Nature of transactions inconsistent with what would be expected from declared business

- **Value of transactions**
 - Value just under the reporting threshold amount in an apparent attempt to avoid reporting
 - Value inconsistent with the client’s apparent financial standing

Customer



- For the purpose of KYC policy a ‘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);
 - Beneficiaries 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 reputational or other risks to the bank, say a wire transfer or issue of high value demand draft as a single transaction.



- Know What?

- True identity and beneficial ownership of the accounts
- permanent address, registered & administrative address,
- sources of funds,
- nature of customers' business
- etc.

When is KYC Required to be done



- Opening a new account.
 - In respect of accounts where documents as per current KYC standards have not been submitted while opening the initial account.
 - Opening a Locker Facility where these documents are not available with the Bank for all the Locker facility holders.
 - When the Bank feels it necessary to obtain additional information from existing customers based on conduct of account or to update KYC norms at periodic intervals.
 - When there are changes to signatories, mandate holders, beneficial owners etc.
 - For non-account holders approaching the Bank for high value one-off transactions like Drafts, Remittances etc.
 - Availing any service of the bank such as credit card, etc.,

Key Elements of KYC policies



- 1) Customer Acceptance Policy;
- 2) Customer Identification Procedures;
- 3) Monitoring of Transactions; and
- 4) Risk management



Customer Acceptance -

- Ensure acceptance of only legitimate and bona fide customers
 - Issue of mechanism to verify ID
 - Issue of Multiple IDs
 - Issue of list of suspects/criminals/unwanted elements
 - Awareness and training of staff

Customer Identification-

- Ensure that the customers are properly identified to understand the risks they may pose.
 - Background check of new customer
 - Background check of existing clients
 - Issue of List of suspects/criminals/unwanted elements
 - Awareness and training of staff



Transactions Monitoring-

- Monitor customers accounts and transactions to prevent or detect illegal activities.
 - Issue of Mechanism to verify financial details
 - Transactions inconsistent with customers profile (business)
 - Unexplained transfers between multiple accounts with no rationale
 - Sudden activity in dormant accounts

Risk Management-

- Implement processes to effectively manage the risks posed by customers trying to misuse facilities.
 - Categorization of customers: high/medium/low risk : a dynamic concept
 - Constant interaction between front desk and the compliance team required
 - Awareness and training of staff

Customer Acceptance Policy



- Banks must ensure that explicit guidelines are in place on the following aspects of customer relationship in the bank.
 - No account is opened in anonymous
 - Parameters of risk perception are clearly defined.
 - Documentation requirements and other information to be collected.
 - Circumstances, in which a customer is permitted to act on behalf of another person/entity, should be clearly spelt out
 - Necessary checks before opening a new account .
 - Not to open an account or close an existing account where the bank is unable to apply appropriate customer due diligence

Customer Identification Procedure (CIP)



- The policy approved by the Board of banks should clearly spell out the Customer Identification Procedure to be carried out at different stages i.e.
 - While establishing a banking relationship;
 - While carrying out a financial transaction or
 - When the bank has a doubt about the authenticity/veracity or the adequacy of the previously obtained customer identification data.
- Identifying the customer and verifying his/ her identity by using reliable, independent source documents, data or information.

Individuals



- Proof of Identity – (any one of the documents)
 - Passport / PAN Card / Voter’s Identity Card / Driving License
 - Any Identity Card – to the satisfaction of the Bank
 - Letter from a recognized public authority or public servant verifying the identity and address of the customer to the satisfaction of the bank

- Proof of Address – (any one of the documents)
 - Telephone Bill / Electricity Bill / Ration Card / Bank pass book or statement
 - Letter from a recognized public authority or public servant verifying the identity and address of the customer to the satisfaction of the bank
 - Letter from the employer to the satisfaction of the bank

Companies



- Proof of Identity & Proof of Address –
 - PAN Card / PAN Allotment letter
 - Memorandum and Articles of Association/ Certificate of Incorporation
 - Resolution of the Board of Directors to open the bank account and authorising persons to operate the account
 - Proof of Identity and Proof of Address of the persons authorized to operate the account as per Board Resolution.
 - Power of Attorney granted to its managers/officers/employees to transact business on its behalf.
 - Any officially valid document establishing the proof of existence and proof of address of the entity to the satisfaction of the bank such as :
Telephone Bill / Electricity Bill / Bank pass book or statement

Partnership Firms



- Proof of Identity & Proof of Address –
 - PAN Card / PAN Allotment letter
 - Partnership Deed
 - Registration certificate, if registered with the Registrar of Firms.
 - Power of Attorney granted to its partners or its managers/officers/employees to transact business on its behalf.
 - Proof of Identity and Proof of Address of the persons so authorized to operate the account as per Power of Attorney.
 - Any officially valid document establishing the proof of existence and proof of address of the entity to the satisfaction of the bank such as :
Telephone Bill / Electricity Bill / Bank pass book or statement

Trusts / Societies



- Proof of Identity & Proof of Address –
 - PAN Card / PAN Allotment letter
 - Trust Deed
 - Registration certificate, if registered with the Charity Commissioner / Registrar of Co-operative Societies or such other appropriate Authority.
 - Resolution of the Managing Body of the institution
 - Power of Attorney granted to its trustees / office bearers or its managers/ officers/employees to transact business on its behalf.
 - Proof of Identity and Proof of Address of the persons so authorized to operate the account as per Power of Attorney.
 - Any officially valid document establishing the proof of existence and proof of address of the entity to the satisfaction of the bank such as :
Telephone Bill / Electricity Bill / Bank pass book or statement

Monitoring Transactions



- To effectively control and reduce their risk, following requirements:
 - have an understanding of the normal and reasonable activity of the customer –
 - to identify transactions that fall outside the regular pattern of activity.
- Extent of monitoring will depend on :
 - Risk sensitivity of the account.
The bank may prescribe threshold limits for a particular category of accounts and pay particular attention to the transactions which exceed these limits.

Other precautions



- Banks should ensure that any remittance of funds by way of demand draft, mail/telegraphic transfer or any other mode and issue of travellers' cheques for value of Rupees fifty thousand and above is effected by debit to the customer's account or against cheques and not against cash payment
- Banks should not make payment of cheques/drafts/pay orders/banker's cheques bearing that date or any subsequent date, if they are presented beyond the period of three months from the date of such instrument.
- Banks should ensure that the provisions of Foreign Contribution (Regulation) Act, 2010, wherever applicable, are strictly adhered to.

Risk Management



- For the above, the Board of Directors of the bank should:
 - Ensure that an effective KYC programme is put in place by establishing appropriate procedures and ensuring their effective implementation.
 - Responsibility should be explicitly allocated within the bank for ensuring that the bank's policies and procedures are implemented effectively.
 - Customer education,
 - Introduction of new technologies,
 - Applicability to branches outside India and
 - Appointment of principal officer.

Other Issues



- How can a proprietor of a firm open an account?
- How can a person having no valid documents open account?
 - No account shall be opened in anonymous or fictitious names or when the identity of the customer matches with any person with known criminal background or banned entities.
 - Similarly accounts should not be opened when the bank is unable to verify the identity and/or obtain documents required as per the bank's policy.

Small Accounts



- “Small account” means a savings account in a banking company where-
 - the aggregate of all credits in a financial year does not exceed rupees one lakh,
 - the aggregate of all withdrawals and transfers in a month does not exceed rupees ten thousand, and;
 - the balance at any point of time does not exceed rupees fifty thousand”.
- An individual who desires to open a small account in a banking company may be allowed to open such an account on production of a self-attested photograph and affixation of signature or thumb print, as the case may be, on the form for opening the account, subject to certain conditions

Conditions to open a small account



- the designated officer of the banking company certifies under his signature that the person opening the account has affixed his signature or thumb print, in his presence;
- a small account shall be opened only at Core Banking Solution linked banking company branches or in specified branch where it is possible to manually monitor the account;
- a small account shall remain operational initially for a period of twelve months, and thereafter for a further period of twelve months and with the entire relaxation provisions to be reviewed in respect of the said account after twenty four months.
- a small account shall be monitored and when there is suspicion of money laundering or financing of terrorism or other high risk scenarios, the identity of client shall be established through the production of officially valid documents and
- foreign remittance shall not be allowed to be credited into a small account unless the identity of the client is fully established through the production of officially valid documents.



- Is this information kept confidential?
 - Banks should keep in mind that the information collected from the customer for the purpose of opening of account is to be treated as confidential and details thereof are not to be divulged for cross selling or any other like purposes.
 - Banks should, therefore, ensure that information sought from the customer is relevant to the perceived risk, is not intrusive, and is in conformity with the guidelines issued in this regard. Any other information from the customer should be sought separately with his/her consent and after opening the account

KYC and Aadhar Card Linkage



- KYC norms as such does not include Aadhar card as one of the documents. However many banks are constantly sending messages to link Aadhar Card to your bank account/credit card/mobile number etc.,
- Aadhar is mass surveillance technology. Unlike, targeted surveillance which is a good thing, and essential for national security and public order — mass surveillance undermines security.
- Right to privacy
 - A NINE-judge Bench of the Supreme Court by its unanimous historic decision ruled that privacy is a fundamental right, and that the matter has deepened its understanding of fundamental rights as an inalienable inherent rights in every human being.

Mockery of Aadhar Card



भारत सरकार

GOVERNMENT OF INDIA



टॉमी सिंघ

Tommy Singh

पिता : शेरु सिंघ

Father : Sheru Singh

जन्म वर्ष / Year of Birth : 26-11-2009

पुरुष / Male

5485 5000 8000



आधार — आम आदमी का अधिकार

Mockery of Aadhar Card



- A government-authorized Aadhaar enrolment centre was blacklisted for publishing former India cricket team captain's personal details.
- More than a million Aadhaar numbers were leaked by Jharkhand, & Punjab governments and 210 websites of the central and state government departments displaying personal details and Aadhaar numbers of beneficiaries . In some cases, UIDAI moved swiftly to shut down the website but days after the leaks, and at least four other data breaches were reported.
- A Bengaluru-based software developer was arrested for allegedly accessing the Aadhaar database through a mobile application he had developed.
- 209470519541: This was the 12-digit unique identification number prescribed to Lord Hanuman some years back. The Aadhaar card bore a picture of the popular Hindu god, addressed him as the son of 'Pawan' and even displayed a mobile number and thumbprint.

Revenue Leakage



- **Income**

- Computerized and auto operated
- Computerized, but manually option
- Non-computerized

- **Expenses**

Incomes of Bank



- a) Interest Earned On Advances
- b) Penal Interest
 - On Overdue installments &
 - On Late Submission of stock statement
- c) Processing Fees
- d) Cash Credit Renewal Charges
- e) Inspection Charges
- f) Documentation Charges
- g) Minimum Balance Charges
- h) Ledger Folio Charges

Revenue Audit



- Study the relevant circulars pertaining to charges given by bank, Go through the Format of Audit Report & Annexure attached to the audit report. Design the Query Sheet in Format of annexure given to bank & get some print out copies of query sheet before going to audit.
- Prepare a separate file for audit & don't forget to carry Audit engagement letter given by head office along with file & query sheet formats, circulars, r scales, audit pens, pencils calculators.
- Prepare the Short Audit Programme for audit covering which areas to be covered & to be covered by whom.
- Auditors are advised to keep in mind the period of audit so as to avoid haphazard way of audit.



- Scrutinize the previous revenue audit reports, latest concurrent audit reports of branch to get the idea of nature of leakage that can be possible to identify. Get Some idea about Bank Officials & Nature of their duties, positions,
- Get Some Basic idea about branch's banking software (i.e. Putting A/c No, Period of Audit) so as to facilitate easy viewing of customer ledger.
- Ask the Bank manager to make available Advances Sanction Register for our Audit Period, Jottings of Some Important accounts, such as Top 10 cash credit, savings, current and deposit accounts, List of NPAs etc.,

What Auditor should do?



- Primary responsibility with the concurrent auditor of the branch
- As statutory auditor, verify the control for accounting of income
- Review the concurrent audit report and check whether all observation highlighted have been rectified
- Test check all stream of the income i.e. Income, Commission & Exchange
- Verify whether the interest rate is properly captured in CBS vis-à-vis sanction terms

What Auditor should do?



- Verify the calculation of interest income and verify the same with the interest debited to the borrower account
- Commission on BG/ LC, check whether the commission is charged at standard rate and in case of any concession, verify the approval from sanctioning authority
- Two types of entries for collection of commission – System/ Manual
- Request for the dump of manual entries and verify the correctness of commission as the same is prone to error



- Verify the recovery of penal interest due to non-submission/ delay in submission of stock statement
- In respect of Interest expenses, generally, the controls are centralized for interest rate on deposits
- Test check whether the correct interest rate is assigned to a FD based on type of FD, amount, tenor

Income Leakage



- Application of interest on all types of loans. The auditor should see the flagged accounts where interest is not charged.
- Correct rate of interest as per sanctioned terms. Especially, in case of advance against Fixed Deposit of third party, the interest should be changed additionally.
- Concessions given to the borrower in the rate of interest on loans should be seen. Whenever rates are revised, the impact thereof on the concessions needs to be seen more carefully.
- In case of NPA accounts, the interest is to be recognized as income only on realizable basis. It should be realized out of fresh and genuine credits and not from fresh sanction of loans.



- Penal interest should be verified. The penal interest is on account of delay in submission of stock statements, non-compliance of the terms of sanction, incomplete documentation, non-renewal of facilities after due date, etc.
- Temporary overdrafts (TOD) in saving bank accounts or current accounts. Similarly, excess drawings in cash credit accounts attract additional interest.
- Other charges on the following accounts should also be checked- - Cheque book charges - Minimum balance charges - Loan processing charges - Commitment charges on the advances not utilised - Cheque return charge .
- Commission and exchange should be checked- - DD/TT/MT - Balance certificate charges - Solvency certificate charges.
- Other income - Interest on investment, if any. - Locker rent- recovery of locker rent and position of outstanding locker rent

Income Leakage



- For all expenses, the auditor should see the sanction by appropriate authority, proper documentation and correctness in accounting.
- The other areas covered could be the following- Interest paid on different types of deposits - Interest paid on borrowings - Reversal of interests paid or interest on premature deposits - Establishment expenses - Rent for premises - Service tax payments and payment of other taxes - Professional fees, legal fees, etc. - General charges account.

Suspense Account



- Suspense account is often used to temporarily record certain items till the determination of the precise nature thereof or pending transfer thereof to the appropriate head of account;
- Some examples :
 - Debit balances arising from payment of interest warrants/ dividend warrants pending reconciliation of amounts deposited by the company concerned with the bank and the payment made by various branches on this account;
 - Amounts of losses on account of frauds awaiting adjustment.

Suspense accounts, sundry deposits, etc.



- Suspense accounts are adjustment accounts in which certain debit transactions are temporarily posted whose authorisation is pending for approval.
- Sundry Deposit accounts are adjustment accounts in which certain credit transactions are temporarily posted whose authorisation is pending for approval.
- As and when the transactions are duly authorised by the concerned officials they are posted to the respective accounts and the Suspense account/Sundry Deposit account is credited/debited respectively.

First step to check Suspense Account



- In Finacle - Balance in Suspense/ Sundry accounts can be verified from ACLI/ACSP. The breakup of old outstanding entries can be obtained from MSGOIRP menu.
- You should have a list of all assets, liabilities, provisions, suspense accounts, income-expense accounts etc. in your PR menu, with their current balances.
- Details of old outstanding entries may be obtained from the branch and the reasons for delay in adjusting the entries may be ascertained.

What Should Auditor do, then?



- Special attention to any unusual items in suspense account since these are prone to fraud risk.
- Refer the guidelines issued by Head office in this regard
- Obtain break up of Suspense account and sundry assets
- Review all outstanding entries more than 90 days
- Verify the reason for delay in adjusting the outstanding entries
- Adequate provision to be made for such items in case the same is not realizable



- Review the realisability of all outstanding suspense
- Advance given for any expense i.e. Travel Advance – check whether expenses incurred, provision to be made
- Advance given for fixed assets - check whether the assets received, if yes, the same needs to be capitalized
- Generally, entry-wise details of Suspense account, Sundry Assets is provided by the branch, review the same and check whether provision is required for item which is not realisable

In short



- Ask for and analyse their year-wise break-up.
- Check the nature of entries parked in such Accounts.
- Check any movement in such old balances and whether the same is genuine and has been properly authorised by the competent authority.
- Check for any revenue items lying in such accounts and whether proper treatment has been given for the same.

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