7: Life assurance, and life-related protection, pension and investment products

Note: This sectoral guidance is incomplete on its own. It must be read in conjunction with the main guidance set out in Part I of the Guidance.

7.1 This sectoral guidance helps firms to interpret how the risk-based approach set out in Part I, Chapter 4 and the customer due diligence requirements set out in Part I, Chapter 5 might be applied to the specific circumstances of the protection, savings and pensions businesses of the insurance sector.

What are the money laundering risks in the protection, pension and investment business of the insurance sector?

7.2 The insurance sector provides a diverse range of products to customers via an equally diverse range of distribution channels. It has been noted that the majority of insurance products do not deliver sufficient functionality and flexibility to be the first choice of vehicle for the money launderer. However, it is also recognised that although the nature of these products helps reduce the money laundering risk, the funds used to purchase them could be the proceeds of crime. Where there are doubts as to the legitimacy of the transaction, verification of the customer's identity remains important as part of the investigation into the transaction and the customer.

The key drivers of risk

7.3 Part I, Chapter 4 states that any risk-based approach to AML needs to start with the identification and assessment of the risk that has to be managed and identifies key elements (or drivers) of risk as follows:

a) The profile of the customer, including his geographical location and source of funds;
b) The delivery mechanism, or distribution channel, used to sell the product; and
c) The nature of the product being sold.

7.4 In addition to the risks identified above, the increasing volume of activities outsourced by insurers brings an additional dimension to the risks that the insurer faces, and this risk must be actively managed - see Part I (2.7 ff). Insurers that outsource activities should assess any possible AML/CTF risk associated with the outsourced functions, record the assessment and monitor the risk on an ongoing basis.

7.5 FSA regulated firms cannot contract out of their regulatory responsibilities, and they remain responsible for systems and controls in respect of the activities outsourced, whether within the UK or to another jurisdiction. In all instances of outsourcing, it is the delegating firm that bears the ultimate responsibility for the duties undertaken in its name. This includes ensuring that the provider of the outsourced activities has satisfactory AML/CTF systems, controls and procedures.

7.6 Based on the views of insurance firms, the majority of this guidance focuses on risks from a product-led perspective; however, there are circumstances in which a customer's profile may add to the product risk. This is particularly the case with regard to Politically Exposed Persons – see Part I (5.5.18 ff). A firm must ensure that their own risk-based approach is appropriate to the particular circumstances they face.

Politically Exposed Persons (PEP)

7.7 Part I (5.5.18 ff) sets out general provisions for identifying, establishing business with, and monitoring PEPs. This sectoral guidance sets out the fundamental risks and business practices that insurers may wish to consider when developing a risk-based procedure. These risks and business practices may change, and it is therefore important that insurers monitor these developments and adjust their procedures accordingly.

7.8 When developing a procedure for identifying PEPs, insurers should target those areas of business that are at the greatest risk of having customers who meet the PEP criteria.

7.9 Based on the experience of a number of insurers, the insurance sector has a very low exposure to PEPs. The majority of products sold by insurers also do not lend themselves to storing or laundering the proceeds of crime, including corruption. It is likely therefore that the numbers of customers meeting the high-risk criteria are very low and those that are identified as PEPs are lower still.

7.10 Firms may consider using criteria such as accounts with non-UK residents[14] and investment value to determine their risk-based approach to PEP identification.

7.11 It is expected that this risk-based procedure will make the volume checking of new customers unnecessary. However, adequate measures to check PEP status for those customers meeting the high risk criteria should be undertaken during the course of establishing the business relationship. If a PEP is identified at this stage, senior management approval is required for establishing a business relationship. In the case of identifying an existing customer as a PEP, senior management approval for continuing the business relationship must be obtained as soon as practicable upon identifying a PEP.

7.12 The identification of a customer as a PEP is not in itself cause for suspicion, but requires an enhanced level of due diligence in line with the guidance set out in Part I. In some cases, however, this enhanced due diligence may trigger suspicions that the client is attempting to store or launder the proceeds of crime, including corruption. In such cases, a SAR and consent request must be submitted to SOCA, following the guidance set out in Part I, chapter 6.

Distribution Risk

7.13 The distribution channel for products may alter the risk profile. For insurers the main issues will be non face-to-face sales, such as online, postal ***or*** telephone sales. Part I, paragraphs 5.5.10ff outline the process for managing non face-to-face sales.

7.14 For business sold through agencies, such as IFAs, agency acceptance and ongoing management procedures may already meet the requirements set out in Part I, paragraphs 5.6.27 and 5.6.28. The MLRO should ensure that he is comfortable with the vetting processes undertaken by the firms distribution arm, for advisers, prior to the issue of and throughout the agency agreement. This should include the ability of the intermediary to provide copies of the underlying documents or data on request. The MLRO should be aware and satisfied with the level of monitoring of any material breeches/financial difficulties, which might call into question the agent’s status as fit and proper.

7.15 Once a business relationship is established with an intermediary, the Confirmation of Verification of Identity is the record for the purpose of meeting the record keeping requirements (this is irrespective of any outsourced administrative arrangement) and should be retained in accordance with the guidance provided in Part I, paragraphs 5.6.4ff. If, in the course of normal business, the

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[14] For the purposes of this guidance, a non UK resident is a person defined as such for UK tax purposes.

intermediary's standards are called into question, the insurer should review its status as a provider of CVIs. For higher risk business, such as non-UK, the MLRO will need to be satisfied that the level of customer due diligence carried out by the third party is commensurate with the risk and may wish to request copies of the underlying evidence obtained by the intermediary.

Product Risk

7.16 The remainder of this sectoral guidance concentrates on product risk. This is because, in the insurance sector, the nature of the product being sold is usually the primary driver of the risk assessment. This is because of the very different nature of each category of products (protection, pensions and investments) and the fact that each product's features are defined and restricted; some will only pay out on a verifiable event such as death or illness, whilst others are accessible only after many years of contributions. As well as limiting the flexibility of these products as potential money laundering vehicles, the restrictions also enable firms to more readily profile the products for 'standard' (and conversely, 'non standard' or 'suspicious') use by customers.

7.17 A smaller number of products sold by firms in the insurance sector, including single premium investment bonds and certain pensions, do feature increased flexibility. This should be acknowledged in the application of the risk-based approach.

7.18 The following are features which may tend to increase the risk profile of a product:

- accept payments or receipts from third parties;
- accept very high value or unlimited value payments or large volumes of lower value payments;
- accept cash payments;
- accept frequent payments (outside of a normal regular premium policy);
- provide significant flexibility as to how investments are managed to be liquidated quickly (via surrender or partial withdrawal) and without prohibitive financial loss;
- be traded on a secondary market;
- be used as collateral for a loan and/or written in a discretionary or other increased risk trust;
- accept overpayments.

7.19 The following are features that may tend to reduce the risk profile of a product:

- restricted capacity to accept third party receipts or make third party payments;
- have total investment curtailed at a low value due to either the law or a firm's policy;
- be relatively small value regular premium policies that can only be paid via direct debit;
- require the launderer to establish more than one relationship with a firm or another official body (e.g., certain types of pension products where the customer has to set up the product with the provider and to get HMRC approval and possibly appoint a Pensioner Trustee);
- have no investment value and only pay out against a certain event (death, illness etc) that can be checked by the product provider; and/or be linked to known legitimate employment.

7.20 The above are general lists of characteristics and are indicative only. Firms are strongly discouraged from using the lists in isolation for a mechanical 'tick box' style exercise. No characteristic acts of itself as a trigger. Not all products that may be used, say, as collateral for a loan, are automatically 'increased risk' by virtue of one characteristic alone. These general characteristics are given so that firms may weigh them up in overall balance for specific, branded products against their knowledge of the customer and their business.

7.21 In recent years there has been a growth in so called 'platform' or 'wrapper' product offerings from insurance firms, where a variety of products are offered to various target markets under an overarching 'wrapper' arrangement. These products may form, in effect, a portfolio arrangement for underlying clients or members, sold via arrangements conducted between the product provider and a third party - typically a regulated introducer (IFA) , Employer or similar. They may encompass a variety of risk factors that drive the level of customer due diligence (see paragraphs 7.2 to 7.28).

7.22 Firms may wish to consider whether they should apply a standard level of customer due diligence to the whole 'platform' or 'wrapper', or whether to graduate the level of customer due diligence dependent on the actual product occurrence and specific risk factors as/when they arise. The customer due diligence should be conducted as appropriate in accordance with paragraphs 7.1 to 7.58 and financial sanctions guidance in Part III, Section 4. Whichever approach is used, a firm should ensure that it documents its approach and is satisfied that the approach adequately addresses the money laundering and terrorist financing risks according to the combination of risk factors inherent in the 'platform' or 'wrapper' arrangement.

7.23 Where apparent inconsistencies exist, firms are expected to exercise judgement accordingly. For example certain pension products and platform based portfolio arrangements accept contributions from employers. Third party payments are normally indicative of increased risk according to the list in 7.18, however for such products, once appropriate due diligence has been enacted in respect of the employer; there is some risk reduction in respect of source of funds. Some of the other features of pension products (the restricted access to funds, the ability to take only a percentage of the fund as a lump sum on reaching retirement age, the involvement of HMRC), also reduce the product risk.

7.24 It is stressed that risk levels attributed to generic products in this document are intended to provide a starting point for a firm's risk assessment. Firms should consider whether their own, branded versions of those generic products possess features (such as a facility for top up payments or prohibition from receiving /making third party payments) which raise or lower the risk level. Equally, taking account of other risk drivers which might be identified (for example, the geographical location of a customer) may lead a firm to 'upgrade' or downgrade the overall risk level of a product from that indicated in this guidance. Part I, section 5.5 discusses risk drivers that are not specific to insurance products. Also, where a proposition for business involving a intermediate or reduced risk product is exceptional due to the size, source of funds or for another reason that suggests risk of fraud, money laundering or other usage of proceeds of crime additional due diligence will be appropriate perhaps via existing anti-fraud or other business risk management procedures. In December 2008, the FSA imposed a fine on AON, in a Principle 3 action focused on risk assessment, in particular in relation to controls relating to bribery and corruption (see www.fsa.gov.uk/pubs/final/aon.pdf).

Three overall risk levels

7.25 Firms in the insurance sector have carried out risk profiling of their products, applying the risk assessment criteria detailed above. This guidance draws on that work and establishes three overall levels of risk for insurance products in an AML context. The risk level determines what work a firm needs to carry out to meet industry standards. The three levels are:

a) reduced risk;
b) intermediate risk; or
c) increased risk.

7.26 When attributing an appropriate risk level, it is important to keep insurance risk in its wider context. As already noted, the majority of insurance products do not deliver sufficient functionality and flexibility to be the first choice of vehicle for the money launderer.

7.27 The products identified as 'increased risk' are therefore categorised as such only in the context of the insurance sector and are not intended to equate to references to 'high risk' in the wider context of the financial services industry as a whole.

7.28 The risk level attributed should always be based on the underlying product, irrespective of how it is described in the product provider's literature (i.e., substance prevails over form). Firms should expect to be in a position to justify the basis on which the risk assessment criteria have been applied.

7.29 Risk management is a continuous process (as noted in Part I, paragraph 4.30). The risk assessment process is not a one-time exercise, and it must be revisited and reviewed on a regular basis.

7.30 Finally, there is a need to monitor the environment in which the firm operates. It should be recognised that success in preventing money laundering in one area will tend to drive criminals to migrate to another area, business, or product stream. Firms should be aware of current risk assessments of money laundering/terrorist financing risk in the insurance sector and take them into consideration, along with trends they experience themselves. If displacement is happening, or if customer behaviour is changing, the firm should be considering what it should be doing differently to take account of these changes. A firm's anti-fraud measures will also help it understand its customers and mitigate the money laundering risks.

I - Reduced risk level

7.31 Some groups of products, due to their inherent features, are extremely unlikely to be used for money laundering purposes. Some of these are recognised by the Money Laundering Regulations as attracting Simplified Due Diligence [See Regulation 9(8)]. Others, such as Compulsory Purchase Annuities are considered part of the pensions product. The table below shows these products in their respective categories of protection and pensions. The table also shows a number of the typical features (or restrictions) of each product, which serve to limit their potential as money laundering vehicles and so qualify them for this risk level.

7.32 Risk levels attributed to generic products in this section are intended for guidance only. Firms should consider whether their own branded versions of these generic products have features that either reduce or increase this indicative risk level.

Protection	**Rationale**	
1 Term life assurance	*Typical features:* o *Only pays out on death of assured* o *No surrender value* o *Small, regular premiums: additional payments by customer not possible* o *Large premiums will normally require medical evidence* o *No investment element* o *Once term of policy is finished no payout and policy ceases*	*Timing of verification for pure protection products (Part I: 5.2.3,) ML Regs 9 (4). Part II 7.31*
2 Income protection products related to long-term illness	o *Only pays out on medical evidence and proof required as to loss of income* o *No surrender value* o *Small, regular premiums: additional payments by customer not possible*	*Timing of verification for pure protection products (Part I: 5.2.3,) ML Regs 9 (4), Part II 7.31*

3 Critical illness products relating to diagnosis of a specific critical illness	o *Only pays out on medical evidence* o *No surrender value* o *Small, regular premiums: additional payments by customer not possible*	*Timing of verification for pure protection products (Part I: 5.2.3), ML Regs 9 (4), Part II 7.31*
4. Group Life Protection	o Only pays on medical evidence o No surrender value o Premiums paid by employer – no member funding o Relatively small regular premiums	*Timing of verification for pure protection products (Part I: 5.2.3) ML Regs 9 (4). Part II 7.31*
Pensions		
5 Pension, superannuation or similar schemes which provide retirement benefits to employees **(see footnote 8)**, where contributions are made by an employer or by way of deduction from an employee's wages and the scheme rules do not permit the assignment of a member's interest under the scheme **(see footnote 9)**	o *Long term savings vehicle - No surrender value* o *Product may not be used as collateral*	*Qualifies for Simplified Due Diligence (Part I 5.4.5), ML Regs 13 (7)(c)*
6 Pensions annuities, whether purchased with the company running the long-term savings vehicle or through an open market option.	o *Product already subject to due diligence and ongoing monitoring from the pension provider*	*Qualifies for Simplified Due Diligence. ML Regs 13(7)(b)*
7 Rebate Only Personal Pension ("RPP")	o *Only funded by National Insurance Contribution rebates payable as a result of an individual being contracted out of SERPS or S2P*	*Qualifies for Simplified Due Diligence*
8 Immediate Vesting Personal Pension ("IVPP"). Purchased with the transfer from another pension for the purpose of exercising an open market annuity option.	o *Product already subject to due diligence and ongoing monitoring from the pension provider*	*Qualifies for Simplified Due Diligence. ML Regs 13(7)(b)*

[8] This would cover Contracted in and out Group Money Purchase Schemes, Final Salary Schemes,

s32 Buy Out Plans from the latter types of schemes (if no further contributions are allowed) and Rebate-only schemes.

[9] This qualification for Simplified Due Diligence is based on the Money Laundering Regulations 2007 13(7)(b), and is therefore not contingent on the monetary limits set out in 13(7)(a).

Customer due diligence

7.33 The recommended industry standard for protection products in this category is for due diligence on the customer and the beneficiary to be carried out at the point of claim. For most circumstances, the counter fraud checks at point of claim will satisfy these requirements.

7.34 For pensions annuities, it is sufficient for the insurer to satisfy itself that the pension scheme funding the annuity is HMRC-registered.

7.35 The recommended industry standard for reduced risk pension products is as follows:

Apply Simplified due diligence. Therefore *apart from monitoring,* customer due diligence does not apply to either the customer or the scheme.

However, where a firm considers that there are features of the nature of the employer or the scheme that present an increased risk of money laundering, the following enhanced due diligence measures may be appropriate:

a. Obtaining details of the trustees and the entity (usually the employer), copy of the relevant trust deeds, and verifying the scheme's HMRC/PSO number (this can be done, for example, by sight of the scheme's HMRC approval letter).

Note - HMRC does not now issue approval letters. However, if the firm has any concerns, on application and with the relevant authority, HMRC will provide documentary confirmation regarding the existence of the scheme.

b. Verifying the identity of the employer, or other corporate entity paying into the fund, in accordance with Part I, Chapter 5. Check that the firm is trading and appropriate to provide employees with a pension through a Companies House search or a visit to premises.

7.36 Firms are not required to assume that a payment from an unidentified source (e.g., by wire transfer from a UK bank or building society or a Bankers Draft or a UK Building Society counter cheque that does not identify the account from which it is made) is being made by a third party unless they are aware of some fact that suggests that this is, or may be the case.

7.37 Where an insurer decides to apply simplified due diligence to a particular product or type of business, there is no requirement to identify or verify the identity of beneficial owners and/or controllers. Ongoing monitoring, however, is still required.

7.38 In addition, the destination of funds at the time of redemption can be used as evidence of identity in cases where there has not previously been a requirement to verify, for example where the firm had been able to rely on an exemption. In these cases, depending on the firm's assessment of the risk presented by the situation, including the circumstances in which the customer acquired the investment, it may be possible to satisfy the standard identification requirement by means of a payment to an account with a UK or EU regulated credit institution in the sole or joint name of the customer. The old style IFA Certificates (confirmations of identity) had a tick box "Existing Customer Pre April 1994" – this exemption is not transferable to Insurers. The firm may, however, have completed a current customer review exercise to pick the verification of these customers up.

Monitoring

7.39 Companies must take a risk-based approach to monitoring reduced risk products. A company's normal anti-fraud controls should provide a suitably robust system of monitoring. The high annual limits for pensions in the post A-day tax regime provide greater scope for these products to receive large lump sum payments; a risk that may be mitigated by monitoring.

Frequently asked questions in relation to reduced risk

7.40

(i). What if we identify that a third party is / has been paying into a reduced risk protection product?

Firms should, in the course of their normal commercial business, be considering whether any suspicious or unusual circumstances apply, and should act accordingly, and this might involve verifying the identity of the third party. However, in the absence of such concerns, unless the third party is the beneficiary (who may be verified by counter-fraud checks at point of claim), there is no requirement to verify the identity of the third party premium payer for reduced risk protection products at any stage.

(ii) What if there is a change of beneficiary or if payout is made to a third party on one of these reduced risk products?

Unless the amount of money to be paid out is small and financial crime is not suspected, the identity of the third party must be verified before payout can take place. A letter of instruction from the original beneficiary will not normally suffice.

(iii) What if payments into exempt occupational pension schemes begin to be received from the employee rather than from the employer?

Firms should have adequate procedures and controls to identify where payments are not received directly from the employer but instead are received directly from the employee or another third party, whether by personal cheque or direct debit. Where such payments are received, and where the sums are considered material, standard identification and verification requirements set out in Part I, section 5.4 should be applied to the payer as soon as is reasonably practicable.

(iv) How does using the "source of funds" as evidence affect these reduced risk level products?

a) For reduced risk level products, firms may accept personal cheques and other payment instruments drawn on a customer's account as satisfying the requirement to verify the customer's identity.

b) Where the funds are being paid into a reduced risk level product by direct debit from an account in the customer's name, there is no additional requirement on firms to correlate the name on the direct debit instruction with the account details at the outset of the relationship. It is usual practice for firms to undertake further due diligence on the customer's identity before any payment is made, as part of their fraud prevention procedures. If a firm's procedures do not provide for further customer due diligence to be undertaken before any payment is made, it should confirm at the outset of the relationship that the payments made by direct debit are made from an account in the name of the client, in accordance with Part I, paragraph 5.3.92.

(v) What about verification on reduced risk level pension transfers?

There is no requirement to verify identity if **both** of the following conditions are satisfied:

1. the transfer is **from** an Occupational Pension Scheme which is not a Executive Pension Plan (“EPP”) or a Small Self Administered Scheme (“SSAS”); **and**
2. the transfer is **to** an Occupational Pension Scheme (which is not an EPP or a SSAS) **or** is **to** a S32 buy out plan with no additional funding.

(vi) *What if a pension-sharing order or pension-earmarking order (for example in the case of a divorce) is received for a reduced risk pension?*

Firms may accept court documents as verification of identity of the existing customer, if this has not already been completed.

Subject(s) of such an order that are explicitly nominated to receive funds should be regarded as the beneficial owner(s), and their identity may also be verified by reference to the court document(s).

(vii) *What if a payment on death is to be made direct to a beneficiary?*

Payments to beneficiaries on the instructions of the executor or administrator may be made once the beneficiaries have been sanction screened. If there are no sanctioned parties involved, there is no need to verify the identity of beneficiary, if the payment is made to an account in their name. However, if a beneficiary wishes to transact any business their own name, their identity will need to be verified, in line with the guidance in Part I, section 5.3, and paragraph 5.3.2.

II - Intermediate risk level

7.41 The intermediate risk level has been attributed to a group of products whose inherent features pose some risk of use for the purposes of money laundering or terrorist financing but they are significantly less than the risks posed by the “increased risk” grouping of insurance products. Some risk is acknowledged in the case, for example, of products with a facility for ‘top up’ payments, and therefore the standard level of due diligence is appropriate. The table below shows these products in their respective categories of protection, savings and pensions, together with some of their typical features or restrictions.

7.42 Risk levels attributed to generic products in this section are intended for guidance only. Firms should consider whether their own branded versions of these generic products have features that either reduce or increase this indicative risk level.

Protection

1 Whole of Life	*Typical features:* o *may accrue some surrender value* o *benefits usually payable on death or diagnosis of terminal illness* o *or, in some cases, critical illness of the policyholder* o *partial surrenders are normally allowed within specified limits* o *qualifying whole of life plans will comply with the rules applicable to qualifying life policies*
Savings and Investments	
2 Life assurance savings plan	*Typical features:* o *Long term savings plan often for retirement* o *Requires at least 5 years to gain positive return on investment* o *Often unable to be surrendered in first or second year, with penalties in years three to five* o *Additional 'top up' payments may be permitted* o *Sum assured/premium relationship broadly complying with HMRC Qualifying Rules*
3 Endowments	o *Long term savings plan for a set term, were often linked to mortgages* o *Sum assured/premium relationship broadly complying with HMRC Qualifying Rules* o *Usually long term, 10-25 years*
4 Trustee Investment Plan ("TIP")	o *The plans are governed by trustees* o *The plans must be associated with a pension scheme* o *All cash flows into and out of the Plan must be via the trustees*
Pensions	
5 Group Personal Pension ("GPP")	*Typical features:* o *Long term policy, usually up to 40 years* o *No surrender value*
6 Group Stakeholder Plan	o *Long term policy, usually up to 40 years* o *No surrender value* o *HMRC registered scheme* o *Annual and lifetime limits apply*
7 Income Drawdown Flexible Pension Plan Phased Retirement Plan	o *Typical features:* o *Policies only open to individuals between the ages 55 – 75, and people who have already accrued by a pension fund* o *The level of income which may be 'drawn down' is subject to limits set by the Government*
8 Free Standing Additional Voluntary Contribution Plan ("FSAVC")	o *Contributions cap set by pensions legislation and monitored by scheme administrator* o *Transfers are only possible to another regulated entity*

9 Stakeholder Plan	o *Long term policy, usually up to 40 years* o *No surrender value* o *HMRC registered scheme* o *Annual and lifetime limits apply*
10 Personal Pension Plan (not SIPP or SSAS)	o *Long term policy, usually up to 40 years* o *No surrender value.* o *HMRC registered scheme. Transfers are possible, but only to another registered scheme.* o *Annual and lifetime limits apply.*
11 Self Invested Personal Pension ("SIPP")	o *Provides a choice of allowable investments, including commercial property, i.e., can be used to buy business premises.* o *Long term policy, usually up to 40 years* o *No surrender value.* o *HMRC registered scheme. Transfers are possible, but only to another registered scheme.* o *Annual and lifetime limits apply.*
12 Executive Pension Plans ("EPPs") (excludes CIMPs & COMPs – see Minimal Risk section)	*Typical features:* o *Contributions from company to tax exempt fund, normally* o *Established by company directors for their benefit* o *Single premium payments permitted* o *Long term policy, usually up to 40 years* o *No surrender value.* o *HMRC registered scheme. Transfers are possible, but only to another registered scheme.* o *Annual and lifetime limits apply.*
13 Small Self Administered Schemes ("SSASs")	o *Small limited companies where directors are the main shareholders* o *Flexibility of investment options* o *Able to be used to raise loan capital* o *Long term policy, usually up to 40 years* o *No surrender value.* o *HMRC registered scheme. Transfers are possible, but only to another registered scheme.* o *Annual and lifetime limits apply.me* o *Pension provider is usually the trustee*
14 Immediate Vesting Personal Pension ("IVPP"). Purchased for purposes other than pursuing an open market annuity option.	o *Policies only open to individuals between the ages of 50 and 75.* o *Purchase not based on a transfer from another pension scheme.* o *Annuity usually purchased with one one-off payment to provide income for life.*
15 Purchased Life Annuity ("PLA") Hancock Annuity	o *No return of cash lump sum at end of the term selected or when customer dies* o *Once annuity purchased, purchaser cannot alter the arrangements or cash it in.*

7.43 As can be seen, the majority of intermediate risk level products are found in the pensions category, which reflects the restricted access to funds in a pension arrangement; pensions cannot be encashed and payments out are limited to tax free cash lump sums (for example, up to 25% of the fund for stakeholder and personal pensions) and regular income. In addition, some schemes will have an independent pensioner trustee who polices the running of the scheme on behalf of HMRC.

Customer due diligence

7.44 The recommended industry standard for intermediate risk products is as follows: Verify the identity of the customer and/or the relevant parties, as per the guidance set out in Part I, Chapter 5, at the outset of the business relationship.

7.45 Firms are not required to assume that a payment from an unidentified source (e.g., by wire transfer from a UK bank or building society or a Bankers Draft or a UK Building Society counter cheque that does not identify the account from which it is made) is being made by a third party unless they are aware of some fact that suggests that this is, or may be the case.

7.46 In accordance with Part I, companies must identify the beneficial owner, following the guidance in Part I, paragraphs 5.3.11 and 5.3.12.

7.47 In addition, the destination of funds at the time of redemption can be used as evidence of identity in cases where there has not previously been a requirement to verify, for example where the firm had been able to rely on an exemption. In these cases, depending on the firm's assessment of the risk presented by the situation, including the circumstances in which the customer acquired the investment, it may be possible to satisfy the standard identification requirement by means of a payment to an account with a UK or EU regulated credit institution in the sole or joint name of the customer. The old style IFA Certificates (confirmations of identity) had a tick box "Existing Customer Pre April 1994" – this exemption is not transferable to Insurers. The firm may however have completed a current customer review exercise to pick the verification of these customers up.

Monitoring

7.48 Insurance companies should have a programme of monitoring which reflects the intermediate risk status of the products mentioned above. A firm should ensure its employees are adequately trained to identify and report unusual business activity to the firm's nominated officer. Within the post A-day pensions regime, highly atypical pensions contributions should attract higher levels of scrutiny from pensions providers.

7.49 Firms should undertake ongoing monitoring for patterns of unusual or suspicious activity to ensure that higher-risk activity can be scrutinised. For example, top-up payments when these are much larger than current holdings, or for EPPs & SSASs, are areas that should receive scrutiny, as well as loans taken out using product as collateral.

Frequently asked questions in relation to intermediate risk

7.50

(i) What constitutes the outset of the business relationship?

In most cases a business relationship begins with the acceptance of a fully completed application or proposal form.

However, the business relationship is only formally established after the end of the cooling off period. This is important for the timing of customer due diligence.

(ii) What about cancellation during the "cooling-off period" leading to a refund of premium paid? In some cases, the customer has not yet been verified by that time.

Firms should seek to mitigate risk by refunding the premium to the customer by way of direct credit to the bank account from which the funds were paid or by an account payee crossed cheque in the customer's name. Firms should also consider whether the cancellation, taken into consideration with all other factors, raises suspicions about the transaction and if they do, consent must be sought from SOCA before paying out the sum. Where there is no such suspicion, firms should also verify the customer's identity before making a refund where the premium is 'large' (the sectoral guidance purposely does not set a lower limit, as materiality thresholds of individual firms will differ with the different features of the product) and/or circumstances appear unusual. (Note: this requirement also applies to increased risk business).

(iii) What information do we need to obtain in respect of intermediate risk pensions to satisfy customer due diligence requirements?

Verification should be undertaken in line with the guidance in Part I paragraphs 5.3.216 to 5.3.225.

CDD can be fully satisfied with the pension scheme tax reference number, which shows the scheme is registered with HMRC. (This information should be held by product provider.)

Note - HMRC do not issue approval letters. However, if the firm has any concerns, on application and with the relevant authority, HMRC will provide documentary confirmation regarding the existence of the scheme.

If pension scheme members make direct contributions to the scheme (not via salary deduction), their identities should be verified accordingly.

If benefit payments are made to the trustees or a member of the pension scheme, additional verification will not be required if the payment is made to an account in their name at an UK or EU regulated financial institution.

If a member requests that their Tax Free Cash amount is paid to a third party, additional checks will be required, including verification of the third party.

Contributions from any third party not connected to the pension scheme will require the third party's identity to be verified in accordance with Part I, chapter 5.

(iv) *What if the product provider is the trustee of the pension scheme?*

The individual members' identities need to be verified e.g., for individual personal pensions.

(v) Who are the relevant parties whose identity should be verified for TIPs?

Trustees.

For UK regulated financial services company trustees, only confirmation of regulatory number is required, or if funds are from a HMRC regulated scheme, the pension scheme tax reference number is sufficient.

Note - HMRC do not issue approval letters. However, if the firm has any concerns, on application and with the relevant authority, HMRC will provide documentary confirmation regarding the existence of the scheme.

(vi) What about verification on intermediate risk level pension transfers?

A risk-based approach can be taken, as a firm's identification and verification obligations for the contract owner(s) may be met if the transfer is from a FSA-regulated financial services firm.

In addition to obtaining the pension scheme tax reference number (which shows the scheme is registered with HMRC), the source of funds should be identified by obtaining:

1 the previous pension provider's name; and
2 the previous scheme or plan name, its reference or PSO/PSTR number where relevant and the type of plan

Taking a risk-based approach, consideration should be given to the jurisdiction from which a Qualifying Recognised Overseas Pensions Scheme originates, to determine whether any further verification of the relevant parties is required.

(vii) What about traded endowments?

The trading of an endowment policy increases exposure to money laundering. A policy can be bought and sold several times before a firm necessarily becomes aware of the reassignment, usually on payout. The insurer should verify the identity of the owner at payout usually in line with the standards set out in Part I, Chapter 5. Where the transfer/s have taken place though a 'market maker' in traded endowments, and that firm is regulated by the FSA, reliance may be sought from the market maker in accordance with Part I, section 5.5.

(viii) What about life assurance policies written in trust for intermediate risk products?

Life assurance policies are commonly written as simple life trusts, usually for inheritance tax planning reasons and not for the purpose of concealing the ultimate economic beneficiary of the policy. Therefore it is not appropriate to apply the identity requirements recommended in Part I (and in Part II, FAQs for Increased risk level e.g., Bonds) for trust vehicles that are used for other purposes and firms need only identify the Settlor in line with the standards in this section. However, firms should ensure that they have in place adequate procedures to identify where a trust poses a higher money laundering or terrorist financing risk and refer to the FAQs in increased risk section below.

(ix) What if a pension-sharing order or pension-earmarking order (for example, in the case of a divorce) is received for an intermediate risk pension?

Firms may accept court documents as verification of identity of the existing customer, if this has not already been completed.

Subject(s) of such an order that are explicitly nominated to receive funds should be regarded as the beneficial owner(s), and their identity may also be verified by reference to the court document(s).

(x) What if a payment on death is to be made direct to a beneficiary?

Payments to beneficiaries on the instructions of the executor or administrator may be made once the beneficiaries have been sanction screened. If there are no sanctioned parties involved, there is no need to verify the identity of beneficiary, if the payment is made to an account in their name.. However, if a beneficiary wishes to transact any business their own name, their identity will need to be verified, in line with the guidance in Part I, section 5.3 and paragraph 5.3.2.

III Increased risk level

7.51 The increased risk level has been attributed to a product whose inherent features open the possibility to their being used for money laundering purposes. The product may have a facility for third party and/or 'top up' payments, or is perhaps negotiable, and therefore an enhanced level of due diligence by asking for more information is appropriate. It is to this risk level that the majority of a firm's AML resource will normally be directed. The table below shows the product together with the features.

7.52 Risk levels attributed to the generic product in this section are intended for guidance only. Firms should consider whether their own branded versions of this generic product have features that either reduce or increase this indicative risk level. As stated before, the increased designation is used here to reflect the different average levels of investments in pensions, savings and other investment products experienced by firms and intermediaries across the sector.

Protection	
None	
Savings and investments	*Typical features:*
1 Single premium investment bonds, including: • With profits • Guaranteed • Income • Investment • Offshore international bonds	o *Open ended investment* o *Usually a 5 year recommended minimum investment term but can be surrendered earlier* o *Additional 'top up' payments permitted by policy holder and by third parties* o *May be segmented and individual segments may be assignable*
Pensions	
None	

7.53 As can be seen from the table above, the increased risk level product is in the investments category, which reflects the higher value premiums that can be paid into them, the relative ease of access to accumulated funds and the lack of involvement of external agencies such as the HMRC.

Customer due diligence

7.54 The recommended industry standard for increased risk products is as follows:

1. Verify the identity of the customer, and/or the relevant parties, as per the standard procedures set out in Part I, Chapter 5, at the outset of the business relationship

AND

2. Acquire prescribed information at the outset of the business relationship to satisfy the additional information requirements of Part I, Chapter 5:

a. source of funds for the transaction (e.g., a UK bank account in own name);
b. employment and salary details; and
c. source of wealth (e.g., inheritance, divorce settlement, property sale)

7.55 Firms are not required to assume that a payment from an unidentified source (e.g., by wire transfer from a UK bank or building society or a UK Building Society counter cheque that does not identify the account from which it is made) is being made by a third party unless they are aware of some fact that suggests that this is, or may be the case.

7.56 An insurer must, where appropriate, verify the identity of the beneficial owner for increased risk products in line with the provisions in Part I, paragraphs 5.3.11 and 5.3.12.

Monitoring

7.57 Firms should undertake ongoing monitoring for patterns of unusual or suspicious activity to ensure that higher risk activity can be scrutinised. A firm should ensure its employees are adequately trained to identify and report unusual business activity to the firm's nominated officer.

Frequently asked questions in relation to increased risk:

7.58

(i) Who are the relevant parties for these products in terms of verification of identity?

The relevant parties are summarised in the table below:

Savings/investments	*Relevant parties to be identified*
1 Bonds	o *Policy holder or applicant* o *All payers if different to policy holder* o *All payees if different to policy holder* o *Beneficial Owners (verification on higher risk cases – see FAQ v below)*
Pensions	
None	

(ii) What constitutes appropriate ongoing monitoring and controls?

a) Firms should, as part of normal commercial procedure, be considering for each product what 'trigger points' occur between customer entry and customer exit which might serve to increase that product's exposure to abuse. Examples of trigger points could be early surrender of a product ('early' in the context of a firm's normal business pattern for that product) or a change in payer and/or beneficiary. Appropriate transaction monitoring can then be set up.

b) This guidance purposely avoids setting monetary thresholds for monitoring (e.g., all surrenders over a certain € amount) because materiality will differ significantly between firms. Firms should identify key indicators pertinent to their own business patterns, taking into account, for example, average premium income size per customer and average duration of the contract in force. With that qualification, suggested standard practice for each increased risk product is summarised in the table below.

Savings/investments	*Suggested practice for monitoring and control*
1 Bonds	o *Cancellation (i.e., applications not proceeded with after funds received)* o *Early surrenders (i.e., within a certain time period, which is to be specified by individual firms) over a certain € threshold* o *Multiple partial surrenders, totalling up to (say) 75% of original investment, within the specified time period* o *Top up payments over a certain € threshold (dependent on individual firms' assessment of materiality) and frequency* o *Third party payments of any value* o *Non UK residents*
Pensions	
None	

(iii) Additional customer information is not always readily available when business has come through an intermediary. How should we go about obtaining it?

It is recognised that business transacted in a non face-to-face capacity, or through Financial Advisors, presents particular difficulties for insurance firms seeking to satisfy their additional information obligations under Part I, Chapter 5. Firms should, continue to obtain the limited information required via their own direct sales force (DSF) (where applicable) or, where business has come through an intermediary, should include a request for the information as part of their customer application or proposal form. Financial advisers and DSF should gather same level of data. It is suggested that the additional information required will be collected as part of an application form, and not part of the introduction certificate.

(iv). Do we need to obtain supporting documentation for the additional information requested from a customer?

Verification is limited to identity only. In most circumstances, additional customer information may be taken at face value. However, if the additional information provided appears incongruous or contradictory, this should serve to raise suspicions about the transaction and firms are then expected to make further enquiries which may in some circumstances involve seeking documentary support to the additional information.

(v) Who do we verify if a Bond is written in trust (Beneficial Owners)

Beneficial Owners need to be "identified". Their identity needs to be "verified" in line with the guidance in Part I, paragraphs 5.3.11 and 5.3.12.

Beneficial Owners include the trustees and also beneficiaries who are entitled to 25% or more of the trust property, this may be named individuals or a class of beneficiary.

At the outset of the business relationship firms should always seek to verify the identity of trustees (at the very least those that it receives instructions from). Payment should never be made to an unverified trustee.

Beneficiaries should always be "identified", for example this can be done by requesting a copy of the trust deed*

For lower risk cases, for example a UK customer that wishes to invest in a bond and for the firm to write this investment in trust, the identity of the customer (the settlor) and the trustees should be 'verified', and the beneficiaries or class of beneficiaries 'identified'.

In higher risk cases the named beneficiaries aged 18 or over, entitled to 25% or more of the trust property should also have their identities verified, at outset.

In all cases, regardless risk, if payment is made direct to a beneficiary at the request of a trustee, the identity of the beneficiary should be verified prior to payment being made, if not already done so.

** We recommend firms liaise with their legal consultants, over whether or not to request a copy of the trust deed.*

(vi) How does using the "source of funds" as evidence affect increased risk level products?

The source of funds should not be used as evidence of identity in respect of increased risk level products. However, where a firm's own, branded version of these generic products have features which reduce the indicative risk, it may conclude that its own product falls within the "intermediate" category of risk and follow the guidance given in respect of intermediate risk products.

(vii) What about Power of Attorney arrangements for these products?

Where any party requiring verification is represented by an individual or firm appointed under a Power of Attorney, the identity of the Attorney should also be verified using the principles established in Part I, paragraphs 5.3.89-5.3.91.

(viii) What about cancellation during the "cooling-off period" leading to a refund of premium paid? In some cases, the customer has not yet been verified by that time.

Firms should seek to mitigate risk by refunding the premium to the customer by way of direct credit to the bank account from which the funds were paid or by an account payee crossed cheque in the customer's name. Firms should also consider whether the cancellation, taken into consideration with all other factors, raises suspicions about the transaction and if they do, consent should be sought from SOCA before paying out the sum. Where there is no such suspicion, firms should also verify the customer's identity before making a refund where the premium is 'large' (the sectoral guidance purposely does not set a lower limit, as materiality thresholds of individual firms will differ with the different features of the product) and/or circumstances appear unusual.

Where funds have derived from a building society cheque or bankers' draft, the money cannot be returned to source. Firms may therefore wish to seek that the account to which the customer requests their funds are returned, is an established account in the firm's customers name, with a regulated financial institution. For example a bank statement could be requested as evidence.

(ix) What if a payment on death is to be made direct to a beneficiary?

Should executors or administrators instruct payments to be made directly to the beneficiaries, the identity of the beneficiaries should be verified, if not already done so, in line with the guidance in Part I, paragraphs 5.3.11 and 5.3.12, prior to the payment being made. Sanction checks should also be undertaken. Refer to Part III.