

GUIDANCE IN RESPECT OF MONEY SERVICE BUSINESSES

1A: Money service businesses (as customers of banks)

Overview of the sector

- 1A.1 The MSB industry is extremely diverse, ranging from large international companies with numerous outlets worldwide to small, independent convenience stores in communities with population concentrations that do not necessarily have access to traditional banking services or in areas where English is rarely spoken.
- 1A.2 The range of products and services offered, and the customer bases served by MSBs, are equally diverse. Indeed, while they all fall under the definition of a money services business, the types of businesses are quite distinct. Some MSBs offer a variety of services, whilst others only offer money services as an ancillary component to their primary business, such as a convenience store that cashes cheques or a hotel that provides currency exchange.
- 1A.3 MSB services can include one or more of the following activities:
- Currency dealing/exchanging;
 - Cheque cashing;
 - Money remitting; and
 - Issuing, selling and redeeming stored value and monetary instruments, such as money orders and traveller's cheques.
- Reg 26(1), 28(1) 1A.4 Under the ML Regulations, MSBs are required to register with HMRC in order to be able to carry out their activities, unless they are subject to FCA supervision. Registration is subject to the MSB meeting the 'fit and proper' test set out in the ML Regulations.
- Reg 3(3)(a)
Sch 1
Sch 2(1)(e) 1A.5 Where MSBs carry out money transmission services, they are included within the definition of financial institutions, and are therefore subject to the full provisions of the ML Regulations. The exemption from the ML Regulations for activities that are engaged in only on an occasional or very limited basis does not apply to money transmission services.
- SI 209/2009
Reg 6 1A.6 Under the Payment Services Regulations 2009, MSBs carrying out money remittance services must be included on a register maintained by the FCA. MSBs on the register can be:
- Authorised Payment Institutions (which are required to meet certain minimum standards in respect of capital, management and systems and controls, and whose client funds must be kept in a separate client account with an authorised bank); or
 - Small Payment Institutions (which are exempt from minimum capital requirements, but whose management must meet certain requirements on propriety and experience, and whose business level must be less than a prescribed monthly

- maximum); or
- Agents of an API or an SPI.

- 1A.7 Many different business models can be used to make money remittance payments, each carrying different AML/CTF risks. Several of these are described on the UKMTA website at www.ukmta.org.
- Reg 23(1)(d)(ii)
Reg 25(1)(b), 25(3),
26(1)(b) 1A.8 MSBs may be subject to supervision by the FCA for AML/CTF, if they are part of a banking or financial services group. Other MSBs are supervised by HMRC, which must maintain a register of those MSBs it supervises, and this register may in future be made available for public inspection. MSBs must not operate unless they are supervised by the FCA or registered with HMRC. Confirmation that a particular MSB is on the HMRC register may be found at <https://customs.hmrc.gov.uk/msbregister/checkTerms.do> (but this website does not allow access to the whole register itself).

What are the money laundering and terrorist financing risks in MSBs?

- 1A.9 Several features of the MSB sector make it an attractive vehicle through which criminal and terrorist funds can enter the financial system, such as the simplicity and certainty of MSB transactions, worldwide reach (in case of money remitters), the cash character of transactions, low thresholds, the often less stringent customer identification rules that are applied to low value transactions compared with opening bank accounts and reduced possibilities for verification of the customer's identification than in credit or other financial institutions. The nature of the underlying customer's relationship with the MSB and a low frequency of contact with them can also be a significant vulnerability.
- 1A.10 Generally, MSBs can be used for money laundering and terrorist financing in two ways: either by wittingly or unwittingly performing relevant transactions for their customers without knowledge of the illegal origin or destination of the funds concerned, or by a direct involvement of the staff/management of the provider through complicity or through the ownership of such businesses by a criminal organisation.
- 1A.11 MSBs can be used at all stages of the money laundering process. Currency exchanges specifically are an important link in the money laundering chain. Once the money has been exchanged, it is difficult to trace its origin. Also, considering that many are small businesses, currency exchanges can be more easily prone to takeover by criminals and used to launder money.
- 1A.12 Obtaining ownership of an MSB either directly or via sub-agent relationships provides criminals a perfect tool to manipulate the money transfer system and to launder money. Detecting such cases depends, to a certain extent, on the firm applying CDD measures and monitoring/reporting obligations effectively.
- 1A.13 The following indicators could be relevant in this context:

- Reluctance by the MSB to provide information about the identity of their customers when requested by the bank;
- Use of false identification and fictitious names for customers;
- Turnover of the MSB exceeding, to a large extent, the cash flows of other comparable businesses in the sector;
- Suspicious connections of the MSB owner;
- Suspicious transactions performed on the bank accounts of the MSB or its owner;
- Suspicion that a business (such as a travel agent or corner shop) is actually providing MSB services to the customers of its primary business, or leveraging another business name/type to cover up unregistered activity;
- Overly complicated agent/principal networks (e.g. multiple principals for one agent, agents with their own agents etc.) with inadequate oversight by principal.

1A.14 A survey carried out by FATF suggests the most important factors that may indicate possible misuse of MSBs include:

- Use of underground remittance systems;
- Mismatch between the economic activity, country of origin, or person and the money remittances received;
- Periodic transfers made by several people to the same beneficiary or related persons;
- Transfers over a short period of time of low amounts that together represent a large sum of money;
- Transfers from one or more senders in different countries to a local beneficiary;
- Sudden inflow of funds in cash followed by sudden outflow through financial instruments such as drafts and cheques;
- Structuring of transactions and/or changing of MSB for subsequent orders to keep a low profile; and
- False information during the customer identification procedure/lack of co-operation.

1A.15 Many reported cases of abuse involve small value wire transfers (although some involve high-value amounts), but the total value of funds involved in these cases can be quite significant, raising the possible involvement of organised criminal activity.

Risk assessment

1A16 The risk inherent in the MSB sector is not the nature of the sector itself, but the potential for the abuse of the sector by criminals. It is therefore important that firms understand these potential risks, and manage them effectively. This risk will be greater in some MSBs than in others, and firms should be able to carry out a risk assessment that allows such a judgement to be made.

1A.17 As a part of a risk-based approach, firms should hold sufficient information about the circumstances and business of their customers and, where applicable, their customers' beneficial owners, for two principal reasons:

- to inform their risk assessment processes, and thus manage their money laundering/terrorist financing risks effectively; and
- to provide a basis for monitoring customer activity and transactions, thus increasing the likelihood that they will detect the use of their products and services for money laundering and terrorist financing.

1A.18 A firm should establish whether the MSB is itself regulated for money laundering/terrorist financing prevention and, if so, whether the MSB is required to verify the identity of its customers and apply other AML/CTF controls – in the case of a non-UK MSB, whether these obligations and controls are to UK standards, or to standards equivalent to those laid down in the money laundering directive. How UK based customers deal with non-UK MSBs can be relevant – especially if there is a non face to face element in the relationship.

1A.19 A firm should determine whether the MSB business is a principal in its own right, or whether it is itself an agent of another MSB. MSBs which operate as principal, or through a limited number of offices/agents present a different risk profile from MSBs which operate through a network of agents – it is important to understand the way the latter type of MSB monitors and confirms compliance by its agents with the AML/CTF controls it lays down.

1A.20 MSBs which carry out periodic internal or external audits or reviews of their AML/CTF controls, including those at its branches and agents, demonstrate a more pro-active management of their ML/TF profile. The outcome of such audits or reviews will be of interest to firms.

1A.21 The information about an MSB that firms should consider obtaining as part of their risk assessment includes

- Types of products and services offered

In order to assess risks, firms should know the categories of money services engaged in by the particular MSB customer.

- Maturity of the business, and its owners' experience

It is relevant to consider whether or not the MSB is a new or established operation, the level of experience the management and those running the business have in this type of activity, and whether or not providing money services are the customer's primary, or an ancillary, business.

- Location(s) and market(s) served

Money laundering risks within an MSB can vary widely depending on the locations, customer bases, and markets served. Relevant considerations include whether markets served are domestic or international, or whether services are targeted to local residents or to broad markets. For example, a convenience store that only cashes payroll or government cheques generally presents a lower money laundering risk than a cheque casher that cashes

any type of third-party cheque or cashes cheques for commercial enterprises (which generally involve larger amounts).

➤ Anticipated account activity

Firms should ascertain the expected services that the MSB will use, such as currency deposits or withdrawals, cheque deposits, or funds transfers. For example, an MSB may only operate out of one location and use only one branch of the firm, or may have several agents making deposits at multiple branches throughout the firm's network. Firms should also have a sense of expected transaction amounts.

➤ Purpose of the account

Firms should understand the purpose of the account for the MSB. For example, a money transmitter might require the bank account to remit funds to its principal clearing account or may use the account to remit funds cross-border to foreign-based agents or beneficiaries. Accounts for use in the MSBs remittance business should be separate from accounts used for the administration of the MSB itself.

1A.22 As with any category of customer, there will be some MSBs that present lower risks of money laundering compared with those that pose a significant risk. Firms should therefore neither define nor treat all MSBs as intrinsically posing the same level of risk. Put simply, a convenience store that also cashes payroll cheques for customers purchasing groceries cannot be equated with a money transmitter specialising in cross-border wire transfers to jurisdictions posing heightened risk for money laundering or the financing of terrorism, and therefore the AML obligations on firms will differ significantly.

1A.23 Annex 1A-I lists factors that might indicate a lower, or higher, risk of ML/TF in MSBs.

Customer due diligence

About the customer

Regulation 5(c) 1A.24 The firm should ensure that it fully understands the MSB's legal form, structure and ownership, and must obtain sufficient additional information on the nature of the MSB's business, and the reasons for seeking the product or service.

1A.25 It is important to know and understand any associations the MSB may have with other jurisdictions (headquarters, operating facilities, branches, subsidiaries, etc.) and the individuals who may influence its operations (political connections, etc.). A visit to the place of business may be helpful to confirm the existence and activities of the entity.

Ownership and control

Regulation 5(b) 1A.26 In deciding who the beneficial owner is in relation to a customer who is not a private individual, the firm's objective must be to know who

has ownership or control over the funds which form or otherwise relate to the relationship, and/or form the controlling mind and/or management of any legal entity involved in the funds.

Regulation 6(1)
Regulation 5(b)

1A.27 As part of the standard evidence, the firm will know the names of all individual beneficial owners owning or controlling more than 25% of the MSB's shares or voting rights, (even where these interests are held indirectly) or who otherwise exercise control over the management of the company. The firm must take risk based and adequate measures to verify the identity of those individuals (see Part I, paragraphs 5.3.11 and 5.3.12). Verifying the identity of the beneficial owner(s) will take account of the number of individuals, the nature and distribution of their interests in the entity and the nature and extent of any business, contractual or family relationship between them.

1A.28 Following the firm's assessment of the money laundering or terrorist financing risk presented by the MSB, it may decide to verify the identity of one or more directors, as appropriate, in accordance with the guidance for private individuals (Part I, paragraphs 5.3.68 to 5.3.114). In that event, verification is likely to be appropriate for those who have authority to operate an account or to give the firm instructions concerning the use or transfer of funds or assets, but might be waived for other directors. Firms may, of course, already be required to identify a particular director as a beneficial owner if the director owns or controls more than 25% of the company's shares or voting rights (see Part I, paragraph 5.3.135).

1A.29 Part I, paragraphs 5.3.138 – 5.3.141 refer to the standard evidence for corporate customers, and Part I, paragraphs 5.3.142 – 5.3.148 provide further supplementary guidance on steps that may be applied as part of a risk-based approach.

Nature and purpose of the relationship

Regulation 5(c)

1A.30 A firm must understand the purpose and intended nature of the business relationship to assess whether the proposed business relationship is in line with the firm's expectation and to provide the firm with a meaningful basis for on-going monitoring. In some instances this will be self-evident, but in many cases the firm may have to obtain information in this regard.

1A.31 Depending on the firm's risk assessment of the situation, information that might be relevant may include some or all of the following:

- record of changes of address;
- the expected source and origin of the funds to be used in the relationship;
- the origin of the initial and on-going source(s) of wealth and funds of the MSB;
- copies of recent and current financial statements;
- the various relationships between signatories and with underlying beneficial owners;
- the anticipated level and nature of the activity that is to be undertaken through the relationship, on each account to be opened;

- the MSB's settlement arrangements, including the relationship with parties in the second and third miles.

1A.32 In the light of the risk it perceives in the proposed customer, a firm may include consideration of matters such as:

- its public disciplinary record, to the extent that this is available;
- the nature of the customer, the product/service sought and the sums involved;
- any adverse experience of the other firm's general efficiency in business dealings;
- any other knowledge, whether obtained at the outset of the relationship or subsequently, that the firm has regarding the standing of the firm to be relied upon.

MSB's AML/CTF policies

1A.33 HMRC has issued guidance to MSBs on their AML/CTF obligations. As with any other customer subject to AML obligations, the extent to which a firm should enquire about the existence and operation of the anti-money laundering programme of a particular MSB will be dictated by the firm's assessment of the risks of the particular relationship. Given the diversity of the MSB industry and the risks they face, there may be significant differences among AML programmes of MSBs. The resources and experience available within the MSB's compliance function and, in a principal/agent situation, how the principal ensures and monitors compliance with the AML/CFT standards in their agents, are also relevant.

1A.34 In the light of the information that the firm has on the MSB's AML/CTF policies and procedures, it should consider what further steps it should take to be comfortable that these policies are reasonable and effective, possibly including seeing the results of an audit or review of the MSB's AML/CTF policies and procedures.

Enhanced due diligence (EDD)

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| Regulation 14(1)(b) | 1A.35 | A firm's due diligence should be commensurate with the level of risk of the MSB customer identified through its risk assessment. If a firm's risk assessment indicates potential for a heightened risk of money laundering or terrorist financing, it will be required to conduct further due diligence in a manner commensurate with the heightened risk. |
| | 1A.36 | Whenever faced with less transparency or less independent means of verification of the client entity, firms should consider the money laundering or terrorist financing risk presented by the entity, and therefore the extent to which, in addition to the standard evidence, they should verify the identities of other shareholders and/or controllers. |
| | 1A.37 | While the extent to which firms should perform further due diligence beyond the minimum will be dictated by the level of risk posed by the particular customer, it is not the case that all MSBs will always require additional due diligence. In some cases, no further customer due diligence will be required - in other situations, however, the further due diligence required may be extensive. In all cases, the level of due |

diligence applied will be dictated by the risks associated with the particular customer.

- 1A.38 Depending on the level of perceived risk, and the size and sophistication of the particular MSB, firms may pursue a range of actions as part of an appropriate due diligence review or risk management assessment of an MSB seeking to establish an account relationship. Similarly, if the firm becomes aware of changes in the profile of the MSB to which services are being provided, additional steps may be appropriate. Firms will not uniformly require any or all of the actions identified for all MSB customers.
- 1A.39 Where the customer is an overseas, unregulated MSB (see 1A.42 if a UK MSB), additional due diligence should be undertaken to ascertain and assess the effectiveness of the MSB's internal policy on money laundering/terrorist financing prevention and its CDD and activity monitoring controls and procedures. In larger cases, where undertaking due diligence on a branch, subsidiary or affiliate, consideration may be given to the parent having robust group-wide controls, and whether the parent is regulated for money laundering/terrorist financing to UK or equivalent standards. If not, the extent to which the parent's controls meet UK or equivalent standards, and whether these are communicated and enforced 'effectively' throughout its network of international offices, should be ascertained.
- 1A.40 Where there are indications that the risk associated with an existing business relationship might have increased, the firm should, depending on the nature of the product or service provided, request additional information, for example as to the MSB's activities, customer base or ownership, in order to decide whether to continue with the relationship. A firm should have a clear policy regarding the escalation of decisions to senior management concerning the acceptance or continuation of higher-risk business relationships.

On-going monitoring

Reg 8

- 1A.41 Firms are required to conduct on-going monitoring of business relationships, and to identify and report known or suspected suspicious activity or transactions. Risk-based monitoring of accounts maintained for all customers, including MSBs, is a key element of an effective system to identify and, where appropriate, report suspicious activity. The level and frequency of such monitoring will depend, among other things, on the firm's risk assessment and the activity across the account. The firm may require that a regular (or periodic) audit or review of the MSB's AML/CTF controls is carried out.
- 1A.42 Based on the firm's assessment of the risks of its particular MSB customer, monitoring should include periodic confirmation that initial projections of account activity have remained reasonably consistent over time. The mere existence of unusual transactions does not necessarily mean that a problem exists, but may be an indication that additional review is necessary. Furthermore, risk-based monitoring generally does not include "real-time" monitoring of all transactions flowing through the account of an MSB, such as a review of the payee or drawer of every deposited cheque.

- 1A.43 Examples of unusual activity across MSB accounts, that may or may not be potentially suspicious generally involving significant unexplained variations in transaction size, nature, or frequency through the account, could include:
- A cheque casher depositing cheques from financial institutions in jurisdictions posing heightened risk for money laundering or the financing of terrorism or from countries identified as having weak anti-money laundering controls when the MSB does not overtly market to individuals related to the particular jurisdiction;
 - A cheque casher seeking to deposit currency. Given that a cheque casher would typically deposit cheques and withdraw currency to meet its business needs, any deposits of currency may be an indicator of suspicious activity;
 - A money transmitter transferring funds to a different jurisdiction from expected based on the due diligence information that the firm had assessed for the particular money services business. For example, if the money transmitter represented to the firm or in its business plan that it specializes in remittances to Latin America and starts transmitting funds on a regular basis to another part of the world, the unexplained change in business practices may be indicative of suspicious activity; or
 - A money transmitter or seller/issuer of money ordering deposits currency significantly in excess of expected amounts, based on the due diligence information that the firm had assessed for the particular MSB, without any justifiable explanation, such as an expansion of business activity, new locations, etc.
- 1A.44 Given the importance of the requirement for MSBs to register, a firm should file a suspicious activity report if it becomes aware that an MSB is operating without registration with HMRC, or authorisation by the FCA.
- 1A.45 There is no requirement in the ML Regulations that a firm must close an account that is the subject of a suspicious activity report. Firms are therefore not expected automatically to terminate existing accounts of MSBs based solely on the discovery that the customer is an MSB that has failed to comply with registration requirements (although continuing non-compliance by the MSB may be an indicator of heightened risk). In these circumstances, further enquiries ought to be made.

RISK INDICATORS

To assist firms in determining the level of risk posed by an MSB as a customer, the following are examples that may be indicative of lower and higher risk, respectively. In determining the level of risk, a firm should not take any single indicator as determinative of the existence of lower or higher risk. Moreover, the application of these factors is fact-specific, and a conclusion regarding an account should be based on a consideration of available information.

An effective risk assessment should be a composite of multiple factors, and depending upon the circumstances, certain factors may be weighed more heavily than others.

Examples of potentially lower risk indicator:

The MSB –

- primarily markets to customers that conduct routine transactions with moderate frequency in low amounts;
- offers only a single line of money services business product (for example, only cheque cashing or only currency exchanges);
- is a cheque casher that does not accept cheques drawn on foreign banks;
- is a cheque casher that only cashes payroll or government cheques;
- is an established business with a known operating history;
- only provides services such as cheque cashing to local residents;
- is a money transmitter that only remits funds to domestic entities; or
- only facilitates domestic bill payments.

Examples of potentially higher risk indicator:

The MSB –

- allows customers to conduct higher-amount transactions with moderate to high frequency;
- offers multiple types of money services products;
- is a cheque casher that cashes cheques for commercial businesses;
- is a money transmitter that offers only, or specialises in, cross-border transactions, particularly to jurisdictions posing heightened risk for money laundering or the financing of terrorism or to countries identified as having weak anti-money laundering controls;
- is a currency dealer or exchanger for currencies of jurisdictions posing heightened risk for money laundering or the financing of terrorism or countries identified as having weak anti-money laundering controls;
- is a new business without an established operating history;
- is a relatively small concern, with few staff but is a principal with a large agent network - this mitigates against effective supervision and control of agents ;
- the MSB has agents who have agents of their own, or the principal is itself an agent of another business; or
- carries out third party trade based settlements as part of the clearance process.