FIAU

Guidance Note:

On obtaining Source of Wealth Information related to Parties other than the Customer

Issued: July 2022

INTRODUCTION

One of the Customer Due Diligence measures that subject persons must apply in terms of Regulation 7(1)(c) of the Prevention of Money Laundering and Funding of Terrorism Regulations (PMLFTR) is that of "assessing and, as appropriate, obtaining information on the purpose and intended nature of the business relationship, and establishing the business and risk profile of the customer". To ensure compliance with this obligation, subject persons must obtain information and, where necessary, documentation about the nature and extent of the customer's business, financial or commercial activities. The extent of this requirement depends on the circumstances and level of money laundering and funding of terrorism (ML/FT) risks identified for each individual case. The importance of obtaining this information can be easily grasped when one considers Section 4.4 of the Implementing Procedures – Part I.

Adhering to this obligation may be quite straightforward when the customer is an individual. However, **ensuring compliance with this requirement may not be as easy when the customer is a body corporate or a legal arrangement**. In this context, questions may arise whether it is necessary to go beyond the customer and ask questions on the source of wealth and the activities of parties which may be related to the customer, as is the case with regards to the customer's beneficial owners. **The collection of information and documentation when it is clearly unnecessary runs counter not only to the risk-based approach but may also raise concerns from a data protection point of view.**

It is also possible that during the relationship it becomes necessary to request specific information on one or more individual transactions, which result in significant resources being made available to the customer for the purpose of pursuing its activities. This would be key to ensure compliance with Regulation 7(1)(d) of the PMLFTR and assess whether any of the transactions in question are merely unusual or are otherwise suspicious, resulting in the need to submit a Suspicious Transaction Report (STR).

This would usually require the subject person to understand who is making the resources available, how the financing is to done and above all why it is required. However, there are also situations where it may become necessary to obtain information or documentation as to how the funds being provided to the customer have been generated, to establish the source of wealth of the individual or entity providing the additional resources. The purpose of this Guidance Note is to provide guidance on this specific aspect, by setting out the most common scenarios where a subject person would be expected to ask questions and obtain information, supplemented by documentation, on the activities or source of wealth other than the customer's own.

It is important to note that the **guidance provided should be applied to the extent that it is relevant within the context of the service/s provided by each subject person**. These dictate **whether there is a business relationship in place between the subject person and the customer, and the level of visibility the subject person has of what is taking place with respect to the customer in terms of financing and transactions**. In addition, this Guidance Note is not exhaustive, and one cannot exclude that there may be other scenarios where, on a risk sensitive basis, the subject person would have to look at the source of wealth of an individual, entity or legal arrangement even though not the same as the subject person's customer.

This document is intended to be read within the context of the Implementing Procedures – Part I and any sector specific Implementing Procedures issued by the FIAU. It is a document of general application and does not replace any sector specific obligations and directions.

1. BODY CORPORATES UNDERTAKING COMMERCIAL ACTIVITIES

Body corporates like companies and commercial partnerships are usually established to carry out commercial activities, during which the body corporates will inevitably require the services of one or more subject persons. When establishing a business relationship, subject persons must establish what is the source of wealth of the body corporate. This may also hold true where an occasional transaction is assessed to present a high risk of ML/FT[1]. In situations where the body corporate has developed its commercial activities and has an up and running money generating business, it is very likely that its source of wealth will be those same commercial activities. Obtaining information on the nature and extent of these commercial activities, supported by audited financial statements, would therefore be sufficient to satisfy the obligation to establish a customer's source of wealth[2] as long as the financial statements attest to a sound financial situation resulting from the company's turnover generated from the carrying out of its own activities.

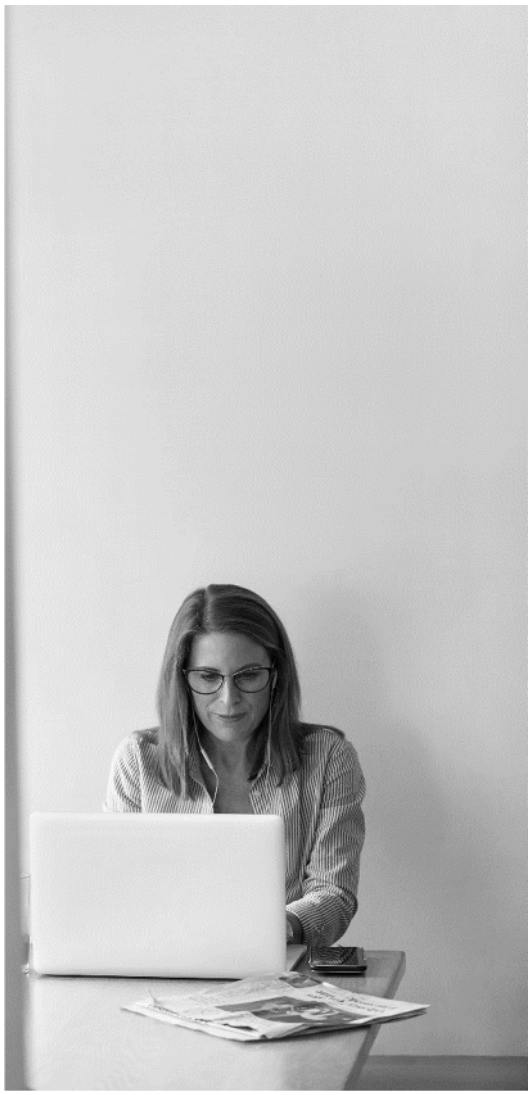
1.1. THE BENEFICIAL OWNER

However, there may be situations where additional questions would need to be asked, even at on-boarding stage, to establish how the body corporate intends to finance its commercial activities or how it has obtained its current resources. A body corporate may have just been established, in which case two scenarios present themselves, i.e., either the body corporate has been established with no or just the bare minimum capital required in terms of law, or its shareholders or partners have contributed significant resources. In the first case it is necessary **to establish how the body corporate is to finance its activities**. Possible means of additional financing may include **additional capital contributions, new investors coming in, shareholders' loans or even a possible offer to the public**. On the other hand, in situations where the body corporate is already, to an extent, financially self-sustaining at such an early stage, one would have to consider **how whoever contributed funds or assets acquired them**.

[1] In line with the risk-based approach and the obligations relating to the application of Enhanced Due Diligence measures, where a subject person considers an occasional transaction to present a high risk of ML/FT there is the need to adopt and apply mitigating measures that are sufficiently robust to address the identified risks. In these situations it is very likely that the risks will somehow be associated with the funds or funding method being used, with the only effective mitigating measure being to undertake checks with respect to the customer's source of wealth and source of funds. Unless otherwise stated, it is not usual for these checks to be carried out in the case of occasional transactions, other than to the extent that it may be necessary for risk assessment purposes and this would justify their nature as mitigating measures in the case of occasional transactions. However, it is also true that other scenarios may arise where the risks associated with the occasional transaction arise from factors other than the funds or funding method being used, which would require the application of alternative mitigating measures.

[2] In the absence of audited financial statements or where the subject person had in precedence audited the customer's financial statements itself, subject persons could for example obtain alternative evidence of the financial well-being of the company such as contractual agreements complemented by bank statements.

Often times this raises the question as to the beneficial owner's own source of wealth, since the said individual would have provided the initial capital or transferred assets to the newly created body corporate, or who eventually will in some way finance the activities of the body corporate. In these situations, **the subject person is expected to obtain information on the source of wealth of this individual and how fresh capital will be made available**. This needs to be done **in line with the risk-based approach which requires to request supporting documentation accordingly**. Obtaining documentation would address any increase in ML/FT risk due to the significant amounts involved.



It is important for subject persons to bear in mind that when one refers to source of wealth, **the reference is not merely to whether one has the necessary resources available, but to how the wealth was generated or acquired**. Thus, copies of bank statements would not *per se* be sufficient as documentary evidence of one's source of wealth. They show that the individual has a given sum of money, but not how they were generated. The information and documentation that needs to be obtained is, whether for example, this was due to a property sale, a significant inheritance, income generated through other business undertakings, savings generated through a high paying position, coupled possibly, with share options and/or a significant golden handshake, the sale of a business a patent and other commercial activities. It is these activities that would have generated the funds held and which would therefore be considered as one's source of wealth.

In situations where the beneficial owner does not contribute other than what is considered a reasonable initial amount affordable by most people; there would usually be no expectation that the subject person collects information on the beneficial owner's source of wealth. One exception to this rule is with respect to situations where the beneficial owner happens to be a Politically Exposed Person (PEP). In this case, it would be key to establish the source of wealth of the individual, in line with what is required in terms of Regulation 11(6) of the PMLFTR, independently of the actual amount of funding provided. Any additional source of wealth information allows the subject person to understand better whether there is anything amiss with the body corporate. This could indicate possible instances of funds originating from illicit gains flowing through the body corporate.

At times, querying how a body corporate intends to finance its activities can also be of assistance to understand who the actual beneficial owner of the body corporate is. The beneficial owner of a company is likely to be identified as such on the basis of the shares or voting rights held. However, there may be instances where funds are made available by a third party, who is willing to finance the activities of the body corporate without being given a stake in it, but who pending repayment of his investment, is allowed to veto certain key decisions and therefore for all intents and purposes is exercising control over the body corporate through means other than holding shares or voting rights[3].

[3] For additional information on the concept of 'control through other means' in the determination of beneficial ownership, please refer to Section 4.2.2.1 (ii) of the Implementing Procedures – Part I.

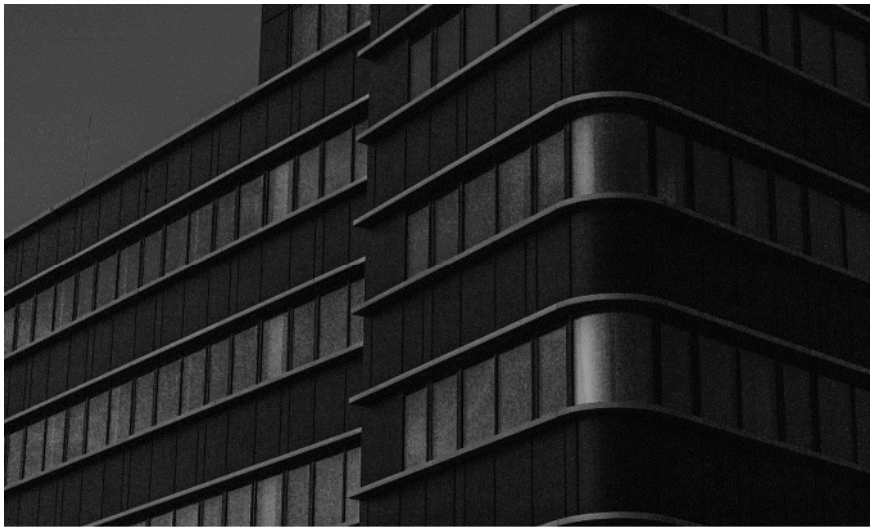
1.2. SENIOR MANAGING OFFICIALS AS BENEFICIAL OWNERS

In line with the definition of beneficial owner provided under Regulation 2(1) of the PMLFTR, it is possible that a customer's senior managing officials need to be considered as the customer's beneficial owners. In this scenario, it is highly unlikely that there will be the need to obtain any information and/or documentation, on the source of wealth of these individuals. Not only are they considered as beneficial owners due to the position they hold rather than any effective ownership or control over the body corporate but more important still they would not be injecting any funds or providing any assets to the said body corporate.

Any individual holding one of the positions referred to in Section 4.2.2.1 (iii) of the Implementing Procedures – Part I is not expected to contribute financially out of their own funds to the running of the body corporate's activities. This holds true independently of the level of risk assigned to the business relationship established with the body corporate or the occasional transaction carried out on its behalf. **Should the subject person become aware of any financing provided by any such individual, the subject person should question whether there is more than meets the eye. They must consider whether this may be indicative of the individual in question exercising control through other means over the customer. At such a point there may be the need to go beyond just understanding how and why the financing is being provided, but also delve on a risk sensitive basis, into the individual's source of wealth.**

A degree of confusion is possible due to the obligation arising from Regulation 11(6)(b) of the PMLFTR, which requires a subject person to take adequate measures to establish the source of wealth and funds of the beneficial owner who has been determined to be a PEP. Should the subject person therefore take action to establish the source of funds of a senior managing official who is a PEP and who needs to be considered as the body corporate's beneficial owner? Indeed, where the body corporate is part of the public administration or is otherwise a State-owned enterprise, it is very likely that the senior managing official is not only considered as the beneficial owner, as required in terms of Section 4.2.2.1

(iii) of the Implementing Procedures – Part I, but will also be a PEP. The same reasoning referred to in the previous paragraph should be considered here and the subject person does not need to query the source of wealth of the individual concerned, unless there are circumstances dictating otherwise. When it comes to body corporates that are part of the public administration or are State-owned enterprises, it is very likely that it is the individual's appointment to management that results in the said individual being considered as a PEP.



One must bear in mind that the requirements set out in Regulation 11(6) of the PMLFTR are intended to counter the risk that the PEP, when acting in a private capacity rather than in an official position, makes use of body corporates or other vehicles to facilitate instances of corruption, bribery or misappropriation or to launder the proceeds of these crimes.

1.3. SOURCE OF WEALTH OF SHAREHOLDERS

Subject persons should also be careful not to focus unnecessarily on the beneficial owner as a possible alternative source of financing, as this can mislead the subject person. Situations may arise where the customer is to receive a significant injection of capital through the introduction of new investors, but this does not result in any changes in beneficial ownership. However, there may still be a subscriber that contributes substantially to this capital injection, in which case the subject person is considered to have an obligation to understand from where the money is originating and how it has been derived. This requires the subscriber to disclose information and documentation on his source of wealth.

Example:

Company 'A' is registered on 1 April 2021 with an issued share capital of €2,000,000 divided into 2,000,000 shares of €1 each. Shareholder 'X' holds 50% of the shares issued and is determined to be the beneficial owner of Company 'A'. The rest of the share capital is divided into smaller holdings, none of which meet the requirements to have their holder considered as a beneficial owner.

On 1 December 2021, Company 'A' increases its issued share capital from €2,000,000 to €3,000,000. Shareholder 'X' participates in the said capital increase and increases its holding from 1,000,000 shares to 1,005,000 and is therefore still a beneficial owner as he holds 33.5%. However, the main subscriber this time is Shareholder 'Y', who acquires 700,000 of the newly issued shares and therefore ends up acquiring 70% of the fresh issue of shares, but only holds 23.33% of the overall issued share capital. The remaining 295,000 shares are taken up by smaller new investors, none of which however hold a particularly significant percentage.

In this case, it would still be expected that questions be asked as to the source of wealth of Shareholder 'Y', even though this shareholder does not meet the requirements to be considered as a beneficial owner of Company 'A'. In this case, Shareholder 'Y' is the main person contributing significant funds to the company, which would still be part of Company 'A's source of wealth, and therefore it is necessary to understand where the funds came from and how they were derived.

In addition, where funds or assets are to be channelled or are being channelled through a structure or a holding body corporate, it is possible that the customer will attest to financing being made available by these companies. **This could be true, though one would need to verify this statement based on something more than the customer's own declarations. The subject person needs to obtain audited financial statements to determine whether the immediate or other body corporate within the corporate structure have the necessary financial means to provide the customer with financial assistance[4].** Do the financial statements attest to a financial position that allows the holding body corporate to provide this assistance? What is the level of turnover, profits and retained earnings? Are there repeated shareholders' loans to keep the company afloat? Do the financial statements somehow cast doubts about the viability of the said body corporate? Depending on the answers to these questions, the subject person may need to delve further into how the customer is going to finance its activities.

[4] Please refer to Footnote 2 with respect to situations where audited financial statements may not be available or may not be relied upon.

2. TRUSTS AND FOUNDATIONS

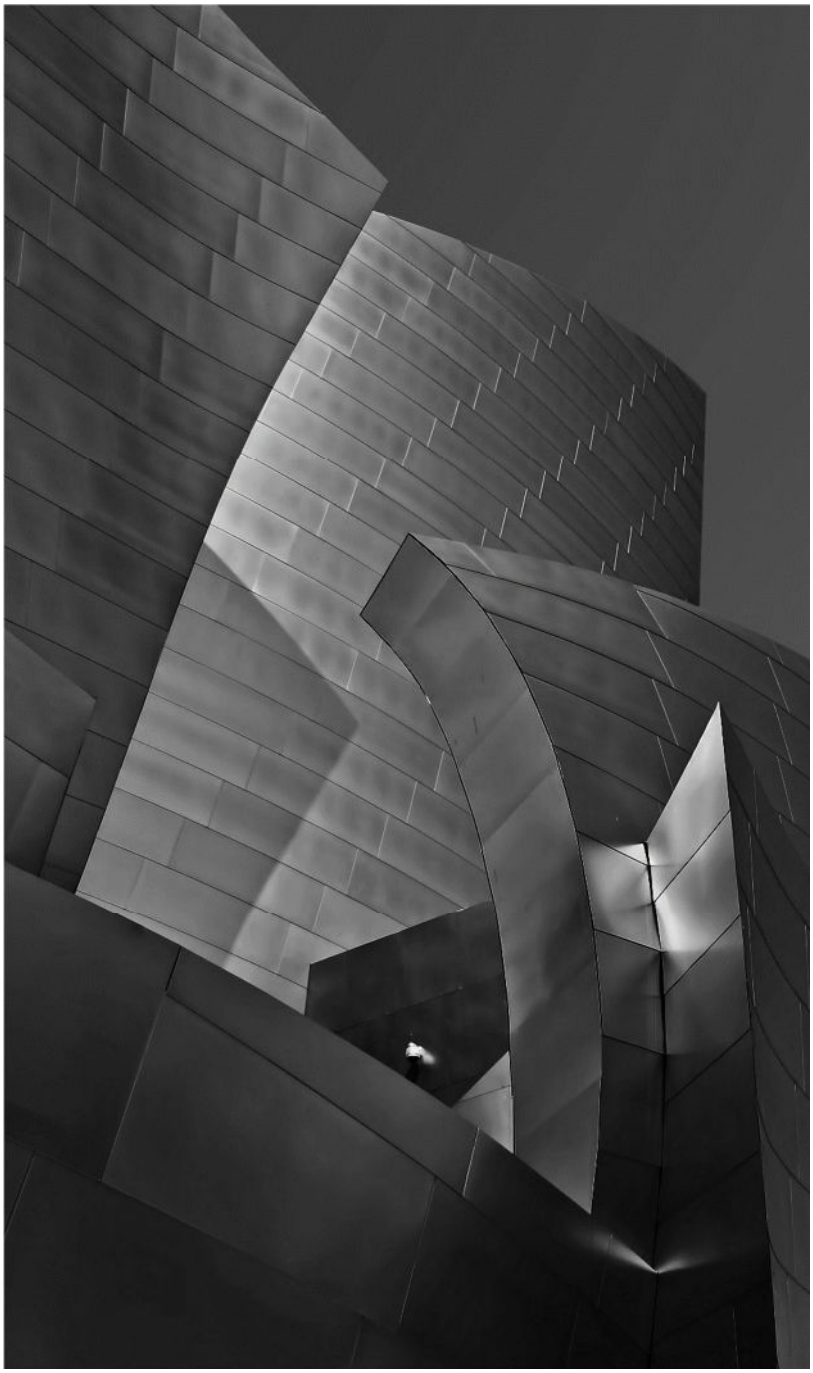
Trusts and foundations can be used for quite similar purposes as both can be used for estate management and charitable purposes. In both instances, the same principles set out for body corporates apply, in so far as there may be the need to determine the source of wealth of parties, other than the customer itself. **This is more relevant where a foundation or trust has just been established or it is not financially autonomous and is therefore still dependent on the original or subsequent endowments or settlement of assets on trust.**

In any such instance, the **subject person must establish what is the source of wealth of the founder or settlor and determine whether the assets were legitimately acquired**. This applies both to the original and to any additional future endowments or settlements. In this context it is important to note that even though the administrators, the trustees and any beneficiaries need to be considered as beneficial owners, it is not necessary determine their source of wealth, as they would not be contributing

financially to the foundation or trust in their given capacity. This is more so with respect to charity trusts and purpose foundations, including any which may be registered as voluntary organisations. Equally, in the case of trusts established for estate management purposes and private foundations, there is no need to obtain information on the source of wealth of the beneficiaries, as they are to receive funds from the foundation or trust, rather than channelling any to them.

When a trust is set up for estate management purposes or a private foundation is established and a minimal amount of funds by way of trust settlement or endowment are utilised; as with companies, pertinent questions should be asked. In this scenario, the **subject person should ask whether additional funds or assets are to be channelled into the foundation or trust**. The answer is likely to be in the affirmative and therefore the subject person is required to obtain at least information on who is to provide any additional funds or assets. It is necessary to verify that anyone doing so has the justified means to provide them, and when eventually these assets or funds are settled on trust, the necessary supporting documentation is requested.

3. ASSOCIATIONS



Associations are one of the most common forms of entities established to pursue social, cultural, and philanthropic purposes. Their source of wealth therefore, usually arises from membership fees and fund-raising activities. Occasionally there may be donations or government grants. **In these situations it is expected that a subject person requests additional information regarding the amounts involved. This may include obtaining information on the source of wealth of the individual or entity making the donation.** However, this would be expected only if the amounts involved are deemed significant.

In this context, **obtaining information and documentation on the source of wealth of the individuals identified as beneficial owners in terms of law**, especially where these happen to be the administrators and will not channel any funding towards the association, will not add any value to one's understanding of ML/FT risk and the mitigation thereof.

4. INDIVIDUALS

The situations where a subject person may be required to establish the source of wealth of a third party is not limited to situations where the customer is a corporate entity. Similar situations can arise where the customer is an individual and a third party pays off the customer's dues. Possible scenarios include where a third party:

(i) pays off the balance due on loan facilities or credit cards;
(ii) pays the amount due for the acquisition of immovable or movable property;
(iii) provides funds for savings, investment or living expenses purposes, etc.

In these circumstances, the subject person **must consider this factor within its customer risk assessment, to determine the level of ML/FT risk presented by the relationship or occasional transaction**. It is also necessary to establish (a) whether there is a **reasonable explanation for the**

third party to be providing the funds; and (b) based on the possible risks presented, **obtain information and documentation to clarify and verify the source of wealth of the third party**. The weaker the connection between the customer and the third party, **the more one needs to query the third party's source of wealth, especially if the amounts are quite substantial**.

It may very well be acceptable for a parent to set aside some funds for a child and have them placed in the child's name, but one must verify the parental source of wealth to ensure that the funds used are legitimate. This also applies when a partner pays off the outstanding balances on any credit cards or loan facilities. **When no tie can be established which would reasonably explain why the third party is willing to make funds available for the benefit of the customer, the ML/FT risk has to be considered as particularly high and therefore the level of information and documentation required needs to be increased and its verification more thorough.**

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