Administrative Measure Publication Notice

This Notice is being published by the Financial Intelligence Analysis Unit (FIAU) in terms of Article 13C of the Prevention of Money Laundering Act (PMLA) and in accordance with the policies and procedures on the publication of AML/CFT administrative measures established by the Board of Governors of the FIAU.

This Notice provides select information from the FIAU's decision imposing the respective administrative measures and is not a reproduction of the actual decision.

DATE OF IMPOSITION OF THE ADMINISTRATIVE MEASURE:

31 May 2023

SUBJECT PERSON:

Papaya Ltd

RELEVANT ACTIVITY CARRIED OUT:

Financial Institution

SUPERVISORY ACTION:

Compliance review carried out in 2020

DETAILS OF THE ADMINISTRATIVE MEASURE IMPOSED:

Administrative Penalty of €279,756, a Reprimand and a Follow-up Directive in terms of Regulation 21 of the Prevention of Money Laundering and Funding of Terrorism Regulations (PMLFTR).

LEGAL PROVISIONS BREACHED:

- Regulation 5(5)(a)(ii) of the PMLFTR and Sections 3.5.1 and 3.5.3 of the IPs Part I.
- Section 4.3.1.1 (iii) of the IPs Part I.
- Regulation 7(1)(c) of the PMLFTR and Section 4.4.2 of the IPs Part I.
- Regulation 7(2)(a) of the PMLFTR and Section 4.5.1(a) of the IPs Part I.

REASONS LEADING TO THE IMPOSITION OF THE ADMINISTRATIVE MEASURE:

Customer Risk Assessment – Regulation 5(5)(a)(ii) and Sections 3.5.1 and 3.5.3 of the IPs Part I

The customer risk assessment (CRA) risk score attributed to five of the customer files reviewed was not in line with the risks posed by the business relationships at the time of the examination. While the assigned score may have been representative of the risk profile at the time of onboarding, the changes surrounding the customer's activity together with the transactions taking place necessitated a review of the CRA and consequently, a higher risk rating than that attributed at the time of onboarding. Some example highlighting the Committee's decision are relayed hereunder:

File A: The customer was involved in the oil and gas industry, and although this information was included in the CRA, such activity did not carry a risk score. The overall risk score assigned to the customer was medium-risk. Committee members took into consideration the volume and value of the transactions that were taking place, noting how in less than two years, a total of Euro 516,481.19 were withdrawn in cash from three of the customer's accounts. The customer was a private company registered in Hong Kong, with the principal place of business being in Italy. The BO of the customer was an Italian individual. The customer was receiving funds from a company registered in the UK, and the cash withdrawals were taking place in France and in Italy. Committee Members highlighted that the medium-risk rating assigned by the Company was not justified in view of all the high-risk factors present in the relationship with this customer, especially when considering that the funds were being channelled between multiple jurisdictions and the volume of the amount withdrawn in cash, completely obscuring the audit trail of the payments.

File B: The customer's business activities were mainly related to financial leasing and providing factoring services. At the time of the examination, this specific customer had performed almost a quarter of all the transactions that took place within the Company and was assigned with a medium risk rating. In view of the value and volume of the transactions taking place, (for example, in one account there were over 1300 debit transactions and over 250 credit transactions between June 2018 and July 2020, both amounting to over Euro 57 million), together with the business activities of the customer (including financial leasing, the purchase of securities and factoring services) the Committee determined that the relationship merited a higher risk than the medium risk rating assigned. The Committee noted that the BO of this customer had personal connections with the Company's BO, and that such fact should have been taken into consideration to ensure that this relationship will not benefit from a less stringent approach in terms of AML/CFT requirements. Members of the Committee highlighted that the CRA should have been updated throughout the course of the business relationship in order to reflect the risks emanating from the business activities taking place.

Certification of documentation – Section 4.3.1.1(iii) of the IPs Part I

In two of the files reviewed, the documents collected to verify the identity of the BO were not certified. Moreover, in another file, the certification carried out was not dated, and thus it could not be established whether this was carried out prior to onboarding. The Company conceded to the reported findings and in fact had identified one of the shortcomings itself during an audit performed. Committee members thus concluded that the Company has breached its obligations.

Purpose and Intended Nature - Regulation 7(1)(c) of the PMLFTR and Section 4.4.2 of the IPs Part I

Information on the nature and details concerning the customer's business activity

Two of the files reviewed held generic information on the customers' purpose and intended nature of the business relationship. In fact, the only information found on file in relation to these customers was that they were 'manual workers' or 'self-employed'. The Company did not provide specific representations with regard to these two files. Instead, it informed the Committee that its systems will be updated and that a more robust application process for legal and natural persons will be applied, which process will also include obtaining information on the purpose and intended nature of the business relationship. Without such information, the Committee determined that the Company would not be able to build an understanding of the customer's business and risk profile.

Anticipated level and nature that is to be undertaken not collected

One of the files reviewed did not contain any information in relation to the anticipated level and nature of the business relationship. The Committee noted that although this customer was considered to be a high net-worth individual, no information or clarifications to understand the expected level of activity for this customer were obtained. Neither did the Company collect information on the estimated volume and value of the transactions to be carried out. The Company did not submit any specific representations with regards to this file. Committee members, thus, determined that in view of the lack of information held on file during the time when the compliance examination was being carried out as well as the fact that the Company failed to rebut the finding in its representations, the Company was in breach of its obligations.

Activities from which the customers derive their wealth

The compliance review revealed that the source of wealth of two customers was not identified by the Company. While the Committee took note that for one file, the Company collected several bank statements, these were not in a language that could be understood. Moreover, even if the description of the transactions included in the statements were to be in a language which could be understood, they were all debit transactions, and hence they could not be indicative of the customer's source of wealth. No representations were submitted for these two files, and hence the Company was found in breach.

The expected source(s) and origin of funds to be used during the business relationship

Six of the files reviewed held insufficient information to establish the expected source and origin of funds to be used in the business relationship. In fact, the information collected was at times limited to statements such as 'personal purposes' and 'services', which information is more aimed at understanding the purpose of the relationship rather than the expected source and origin of the funds. Members of the Committee took into consideration that the Company did not provide specific representations with regards to these files but referred to the representations submitted for the finding relating to the CRA, whereby it indicated that it will be adopting a more robust application process for legal and natural persons, which process includes obtaining information on the purpose and intended nature of the business relationship. Committee Members deliberated that the Company had failed to collect sufficient information on the expected source and the origin of the funds to be used throughout the business relationship, and in the absence of such essential information, it could not build a comprehensive business and risk profile. Thus, Committee Members found the Company in breach of its purpose and intended nature obligation for the abovementioned six files.

Ongoing monitoring – Scrutiny of Transactions - Regulation 7(2)(a) of the PMLFTR and Section 4.5.1(a) of the IPs Part I

Documentation collected to support transactions taking place was inadequate, and at times created more doubts rather than clarifications in regard to the transactions taking place. Examples of the findings reported and the Committee's conclusions are being relayed hereunder:

Example A: This customer received over Euro 6 million from another customer (customer K) of the Company in a period of around 2 years. Although the Company provided loan agreements to support these transactions, it could not be determined that these loans were provided for legitimate purposes. It was also noted how one of the loan agreements, which was for Euro 700,000, was updated to Euro 7 million. It transpired, that in less than a month the customer had lent Euro 8 million to customer K. The loan

agreements in place shed little light as to the purpose of such loans, stating only that these were needed for the realization of the borrower's economic activities. The Committee thus determined that the Company failed to scrutinize the documentation it had collected as part of its ongoing monitoring obligations and that it failed to scrutinize the transactions taking place, breaching its obligations at law.

Example B: Four incoming transactions amounting to over Euro 2 million and 25 outgoing transactions amounting to over Euro 4 million were carried out between October 2018 and July 2020. The customer had entered into three loan agreements with customer K (also mentioned in the case example above). Members of the Committee were seriously concerned at the fact that all three loan agreements in place had conflicting information with regards to who was acting as the lender and who was acting as the borrower. While the introductory section of all three agreements indicated that the customer was acting as the lender, and that customer K was acting as the borrower, in the section where the parties had to sign off the agreements, these roles were reversed, and the customer was now listed as being the borrower. Committee Members further noted that the value of the loan agreements in place and the value of the funds that were transferred between the customer and customer K did not match. In fact, as per the loan agreements on file, a total of Euro 2,956,000 had to be lent by the customer to customer K, however, as the statements reviewed, Euro 4,067,000 were transferred. Although the Company in its representations indicated that the discrepancy in value related to the interest rates and that it was up to the borrower to decide when to repay the loan, Committee members held otherwise. In fact, the Committee noted that the Euro 4,067,000 were transferred by the lender (i.e the customer), thus the difference could in no way be linked to interest rates which the borrower had to pay. The Committee also remarked on the urgency with which one of the loan agreements had to be repaid: a loan agreement of Euro 1,756,000, between the customer as the lender and customer K as the borrower, which was entered into on the July 2019 had to be repaid by August 2019, and thus only a month after the funds were borrowed. This should prompted the Company to obtain further information on the transactions being effected by its customers and ensure that it was not being used to facilitate ML/TF.

ADMINISTRATIVE MEASURES TAKEN BY THE FIAU'S COMPLIANCE MONITORING COMMITTEE (CMC):

When deciding on the appropriate administrative measures to impose, in addition to the specific breaches outlined above, the Committee took into consideration the importance of the obligations being breached, the level of seriousness, and at times systemic nature, of the findings identified, as well as the extent of ML/FT risk such failures could lead to. The Committee also considered the Company's size and the impact that the subject person's failures may have had on both its operations and on the local jurisdiction. The level of cooperation portrayed by the Company throughout the supervisory process was also factored in, including the Company's commitment to remediate its failures. The Committee also noted the Company's minimal regard towards its AML/CFT obligations.

In view of the above considerations, the Committee decided to impose an administrative penalty of two hundred seventy-nine thousand, seven hundred and fifty six Euro **(€279,756)** with regards to the breaches identified in relation to:

- Regulation 5(5)(a)(ii) of the PMLFTR and Sections 3.5.1 and 3.5.3 of the IPs Part I.
- Regulation 7(1)(c) of the PMLFTR and Section 4.4.2 of the IPs Part I.
- Regulation 7(2)(a) of the PMLFTR and Section 4.5.1(a) of the IPs Part I

In addition to the above, the Committee also issued a reprimand in relation to the below breach:

- Section 4.3.1.1 (iii) of the IPs Part I.

In terms of its powers under Regulation 21(4)(c) of the PMLFTR, the FIAU also served the subject person with a Follow-up Directive, to be able to assess the remedial actions being implemented by the subject person in view of the breaches identified. The aim of the Follow-up Directive is for the FIAU to ensure that the Company enhances its AML/CFT safeguards and that it becomes fully compliant with the obligations imposed in terms of the PMLFTR and the FIAU's IPs, as well as perform any required follow-up measures in relation to the Company's adherence to its AML/CFT legal obligations.

In virtue of this Directive, the Company is expected to make available an Action Plan indicating the remedial actions that it has carried out and implemented since the compliance examination, together with remedial actions which are expected to be carried out to ensure compliance following the identified breaches, this including but not limited to:

- Copy of the Company's CRA methodology together with a blank copy of the latest CRA.
- The Company's plan to ensure that active customers and newly onboarded customers are adequately assessed.
- The Company's plan to ensure that it collects, holds and monitors the purpose and intended nature of its business relationships and that it builds a comprehensive business and risk profile on each customer. In view of this, the Company is also required to provide copies of the latest versions of the onboarding forms being utilised.
- The Company's transaction monitoring procedures.
- Updates on the transaction monitoring systems and reports being generated by such systems, and if no updates have been carried out, the Company's plans to implement new systems or measures to monitor discrepancies between the transactions carried out and the business profile of the customers.
- Updates on the transaction monitoring alerts specifically in relation to money laundering and terrorism financing.

The Directive served on the Company shall ascertain that sufficient progress is achieved on all the procedures and measures referred to above, that customer profiles are updated and kept up to date, that customer activity is adequately understood and that the Company enhances its AML/CFT safeguards.

Finally, the Company has also been duly informed that if it fails to provide the above-mentioned action plan and supporting documentation within the specified deadline, the Company's default will be communicated to the Committee for its eventual actions, including the possibility of the imposition of an administrative penalty in terms of the FIAU's powers under Regulation 21 of the PMLFTR.

The administrative penalty hereby imposed is not yet final and may be appealed before the Court of Appeal (Inferior Jurisdiction) within the period as prescribed by the applicable law. It shall become final upon the lapse of the appeal period or upon final determination by the Court.

Key Takeaways

- A CRA needs to be kept updated throughout a customer's business relationship. The fact that a customer posed a particular risk at the start of a relationship does not mean that the risk will remain unchanged all throughout the rest of the relationship. Risk is not static and subject persons are expected to consider any changes in the activity of the customer including in the transactional behavior and pattern of the customer. Retaining or assigning the wrong risk rating to a customer may hinder the ongoing monitoring process and may also result in having suspicious activity and transactions go undetected.

- Understanding the purpose and intended nature of a business relationship is an essential AML/CFT obligation which enables a subject person to perform effective transaction scrutiny. Without an adequate business and risk profile, subject persons are unable to identify deviations from normal behavior or patterns and may result in subject persons failing to file a SAR or STR where required to do so.

- Ongoing monitoring should incorporate the review of the supporting documentation collected, such as loan agreements and invoices, in order to ensure that these are in line with the business activities and the risk profile of the customer. Simply collecting documentation and retaining it on file, without adequately reviewing the same and whether it is in line with the customer's profile, is futile.

- Although widely used and legal by their nature, loan agreements may be utilised as a means for the facilitation of ML. Common AML red flags associated with loan agreements include: (i) frequent loans between the same parties; (ii) loans do not contain the standard terms found in loan agreements (such as without a date for repayment, without any terms of interest or no information on the purpose of the loan); (iii) the loans contain unjustified or overly large amounts (iv) rapid repayment of the loan without a clear justification; (v) the source of funds used for the loan repayment is unclear or originates from a high-risk jurisdiction.

1 June 2023

APPEAL - On the 7th of September 2023, the FIAU was served with a copy of the appeal application filed by the Company before the Court of Appeal (Inferior Jurisdiction), from the decision of the FIAU.

The Company is, *inter alia*, contesting the FIAU's decision, in relation to the Company's Customer Risk Assessment, failure to obtain adequate and sufficient information on the anticipated purpose and intended nature of the business relationships and inadequate transaction scrutiny.

Finally, the Company states that the penalty imposed upon it by the FIAU is disproportionate and excessive.

The Company thus asked the Court to revoke the decision of the FIAU in its regard, or alternatively, to modify and reform said decision by reducing the penalty imposed upon it.

Pending the outcome of the appeal, the decision of the FIAU is not to be considered final and the resulting administrative penalty cannot be considered as due, given that the Court may confirm, vary or reject in whole or in part, the decision of the FIAU. As a result, the FIAU may not take any action to enforce the administrative penalty pending judgement by the Court.

This publication notice shall be updated once the appeal is decided by the Court so as to reflect the outcome of the same.