

## CHAIRMAN'S COLUMN



Dear colleagues,

The beginning of the current year in the EAG work is marked by the completion of the first and commencement of preparations for the second round of the EAG mutual evaluations. The EAG Secretariat has drafted its second round mutual evaluation procedures and has continued to work with its member-states within the framework of their removal from the EAG first round of mutual evaluations follow-up procedures.

Among the key events that took place in the recent past was the FATF assessors training workshop for the EAG, MONEYVAL and MENAFATF Secretariats, hosted by Russia in early March in Moscow. We are grateful to all countries, as well as to the FATF and FSRB Secretariats, that sent their representatives to participate in the event.

Mutual evaluations have been and remain a priority for the Eurasian Group. Therefore, the next step of the EAG in this area will be an assessors training workshop for the EAG member-states in October this year in India. We also plan to participate in the pre-mutual evaluation workshops organized by the FATF style regional bodies – the EAG partners.

On the eve of the 20<sup>th</sup> Anniversary Plenary of the Eurasian Group, to be held in Moscow, I would like to urge all member-states to intensify their work within the EAG. One of the issues to be considered at the forthcoming EAG Plenary meeting is a voluntary tax compliance programs and the impact of implementation of those programs on effectiveness of the national AML/CFT systems.

Another topical issue of the current period is the use of new payment methods. This issue will be the focus of the EAG consultations with the private sector. The purpose of the consultative forum is to facilitate the exchange of ideas between experts representing oversight authorities and financial institutions of the EAG member-states. I believe that such dialogue will make a great contribution towards improving the AML/CFT system of countries in the Eurasian region.

Dr. K.P. Krishnan

## Assessors training workshop was held in Moscow

*On 10–14 March 2014, the EAG Secretariat jointly with the International Training and Methodology Centre for Financial Monitoring hosted a workshop for experts from FATF and FSRBs (EAG/MONEYVAL/MENAFATF) which was dedicated to the preparations for a new round of mutual evaluations of national AML/CFT systems. The previous, third, round of evaluations took place from 2005 to 2010. Since that time, the FATF has revised its standards and drafted a new methodology for assessing.*

The purpose of the FATF's on-site evaluation visits is to monitor compliance by the member-states with the FATF Recommendations and to assess its results. The new methodology for assessing provides for the analysis of two key criteria: technical compliance and effectiveness. The ratings awarded to the country following its mutual evaluation will affect the type of the following process this country will be subject to, underscoring the importance of having enough highly qualified evaluators capable of executing such an important task. This methodology is used by all FATF-style regional bodies, and for this reason among the priorities outlined by the elected in November 2013 EAG Chairman, K. P. Krishnan, was to provide each EAG member-state with a pool of professional assessors.

Accordingly, it was no surprise that the number of persons attending the workshop was significant – about 60. The event brought together representatives of the FATF



and three FSRBs: MONEYVAL, MENAFATF and EAG. The training was conducted by FATF Secretariat employees Vincent Schmoll and Tom Neilan, representative of the International Monetary Fund Steve Dave and MONEYVAL

expert Michael Stellini. The emphasis was placed not only on the analysis of changes following a mutual evaluation and theoretical explanations, but also on the practical aspects, with extra focus on the evaluation of effectiveness,

a topic which previously had not been singled out as a separate area, but instead was considered in the context of other procedures.

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### Vincent Schmoll, Senior Policy Analyst, FATF Secretariat

**– You have participated in the first FATF mutual evaluation of Russia. What do you think, has positively changed in the Russian AML/CFT legislation positively changed since that time?**

– Since the first mutual evaluation of the Russian Federation,

its AML/CFT legislation has continued to change. It was already evident from the results of the second evaluation, which was adopted in June 2008, and even more so afterwards with the effort made to address deficiencies identified at that time. For example, Russian authorities were confronted with the particularly challenging task of establishing appropriate measures for dealing with beneficial ownership. Russia was able to enact legislation last year that remedied the deficiencies

in this and a number of other areas. In general therefore, I would say that Russian AML/CFT legislation has evolved in a positive direction during the past ten years.

**– You are acting as an instructor for the training. How do you estimate the participants' average knowledge and ability? What is your opinion on the activity and the level of training of participants from the EAG and its Secretariat?**

– I would say that the knowledge and ability of the trainees from EAG and its Secretariat at the last training is on par with those of other FSRBs. We have all had experience with conducting the evaluations of the last round. We therefore share the same challenges in adapting to a new evaluation system that must look beyond pure technical compliance with the FATF Recommendations so as to estimate the effectiveness of our AML/CFT systems. I believe that the EAG participants in the most recent training were able to learn a lot but also contributed to the discussions by raising important issues derived from their previous experience in conducting evaluations.

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All participants were split into five teams, each of which subsequently had to prepare draft evaluation reports based on a mock evaluation mission. Discussion of the risk assessment was based on a real-life risk assessment report of New Zealand.

During the workshop, participants went through all real-life stages: risk assessment, analysis of technical

compliance and interviews with the representatives of "government agencies" and "private sector". All of these procedures constitute the basis of the 4<sup>th</sup> round of FATF mutual evaluations, which began in 2014 with the evaluations of Spain and Norway. The Russian Federation will undergo this procedure approximately in 2016-2017.

The workshop ended with the teaching staff expressing hope that the training

would help the attendees prepare for participation in mutual evaluations and thanking the organizers from the Russian Federation represented by the ITMCFM and EAG Secretariat for creating comfortable working conditions. Rick McDonnell, FATF Executive Secretary, expressed his support for the above statement, noting the high level of the workshop organization. "I think both the trainers and participants did a great job preparing for the workshop and

contributing to it. With every new event, the quality of our trainings improves, while the materials used in them become ever more accurate and on-topic".

Workshop participants who have undergone training will now join the teams of evaluators from the FATF and three FSRBs (EAG, MONEYVAL and MENAFATF) and may be invited to participate in the 4<sup>th</sup> round of evaluations.

**Mishra, the representative of the Indian delegation**

**– How does India prepare for the next round of the FATF mutual evaluations? What work is being done to implement the provisions of the legislation to meet the new standards of FATF?**

– India has amended the anti-terrorism legislation, namely, the Unlawful Activities (Prevention) Act and the anti-money laundering legislation, namely, the Prevention of Money Laundering Act in 2013. The amendments to these legislations have brought them into the compliance zone of the revised standards of FATF.

As the FATF standards are represented in numerous legislations, Rules and Regulations, the Government has also formed a committee to examine the concerned laws, Rules and Regulations closely in order to identify if there are any gaps in our legislation based on the FATF Recommendations.

The CFT and AML laws as well as the other laws are being implemented not only to combat money laundering and financing of terrorism but to ensure financial integrity and security of the financial sector in India. We are also in the process of initiating our second National Risk Assessment. Further, regular outreach programmes and interaction with all stakeholders take place at regular basis. We are also examining the various nuances of treating direct and indirect tax crimes as predicate offence for money-laundering.

**Sofiene Marouane, Sr. Officer Technical Assistance & Typologies MENAFATF**

– The MENAFATF Secretariat would like to seize this opportunity to thank the EAG and the Russian Federation for the kind hospitality and excellent facilities provided which greatly participated in the success of the event. Our sincere thanks also go to the FATF Secretariat, the IMF and to different experts. This training is of most importance as countries are requested to implement the amended recommendations and assessors to evaluate whether the required measures are implemented and effective. In addition, this training provided further clarifications and practical insight of the assessment methodology i.e. assessment of

both technical compliance and assessment of effectiveness.

MENAFATF has a very good relationship with the EAG as each FSRB holds an observer status in the other allowing it to attend the Plenary and Working Group meetings. Furthermore, MENAFATF and EAG are currently looking forward to enhance their cooperation through future common events and projects. In fact, a joint EAG / MENAFATF Typologies and Capacity Building Workshop is planned to take place in December 2014 which will be an opportunity to gather typology experts from both regions to share views and exchange experiences with respect to ML/FT trends and methods along with capacity building sessions on important and highly demanded themes. In the pipeline also a possible joint typology project which will focus on common AML/CFT issues.

**Rick McDonnell, Executive Secretary of the FATF**

**– How do you determine the contribution of the workshop into preparations for a new round of evaluations by the FATF and the FSRBs?**

– I believe that the workshop was highly successful in three ways. First, it provided experienced professionals with a detailed and practical understanding of the revised FATF standards. Secondly, it gave participants a "hands-on" learning experience in how to apply the new assessment Methodology. Thirdly, it provided an opportunity to discuss and come to some conclusions about what AML/CFT effectiveness compliance means in practice. As a consequence, the workshop was an essential contribution

towards ensuring that the new round of evaluations is carried out expertly and consistently.

**– What further steps will be taken in terms of assessor training?**

– The feedback we have received from participants at the Moscow workshop indicates a high level of satisfaction with the course but there are always lessons to be learned and this course is no exception. There is an old saying that "the more you teach the more you learn". We will be adjusting some of the training materials so that they are more explanatory in certain parts. We will be further elaborating the mock evaluation case example so that participants have more tailored information on effectiveness and more guidance on how to write the mutual evaluation report. And, of course, we will continue to provide training courses to other FSRBs and to the FATF itself.

**– What joint activities are scheduled with other FSRBs?**

– Apart from ongoing mutual evaluation training courses there are a number of other joint or complementary activities with the FSRBs including country training for countries about to undergo a mutual evaluation and assistance with training of assessors in courses organized by individual FSRBs. In addition there will be a natural continuation of the long-established participation our respective plenary and other meetings, joint typology exercises, Secretariat meetings and the Global Network Coordination Group meetings. In my view, each of these activities and all of them combined are demonstrating an increasing level of cooperation and operational maturity within the global network.



# FATF Private Sector Consultative Forum Meeting

Brussels, March 25-26, 2014 – the Financial Action Task Force (FATF) organized a Consultations with the Private Sector. The annual Consultative Forum was held to discuss implementation of the measures set out in the FATF Recommendations, seek input and feedback into ongoing FAFT work and hear about issues of concern or interest from companies operating in both financial and non-financial sectors

The meeting was hosted by the European Banking Federation (EBF), and supported by the European Association of Public Banks, the European Savings Bank Group, the European Association of Co-operative Banks, and Insurance Europe. Over 120 participants representing the private sector, civil society, as well as representatives of FATF members and observers attended the consultative meeting.

The Consultative Forum meeting discussed the most important and urgent issues on the FATF agenda that required dialogue with the private sector:

## 1. Risk-Based Approach

The FATF sought feedback on revised guidance for a risk-based approach for the banking sector. The revisions would bring the existing FATF guidance in line with the revised FATF Recommendations which were adopted in February 2012. These discussions were a key step to developing a common understanding of the risk-based approach, and how it applies both to private sector stakeholders and at country level, in particular by supervisors. The FATF also had preliminary discussions with representatives from money services businesses and legal professionals on the development of similar guidance for those sectors.

## 2. Virtual Currencies

The FATF met with experts on virtual currencies to discuss how virtual currencies and their exchangers operate, the associated money laundering and terrorist financing risks, and what measures may be and are being taken to assess and mitigate those risks. This feedback will be taken into consideration as the FATF continues to look at the issue of virtual currencies.

## 3. United Nations Sanctions Lists

The FATF met with experts from the United Nations and the private sector to discuss ways to improve the technical accessibility and usability of the United Nations sanctions lists in the context of FATF Recommendation 6 and 7 (targeted financial sanction related to terrorism and terrorist financing

and targeted financial sanctions related to proliferation).

During the session, the representative from the Wolfsberg Group gave a presentation on a new database system for sanctions which has been adopted by the US Treasury, following consultation with banks, IT specialists and public sector bodies. It seeks to address the deficiencies currently experienced by the existence of many different lists which are maintained by different UN bodies with varying formats and data.

Private sector representatives suggested that information about the sanctions lists should be more accessible, inter alia, to small firms which may not have sufficient resources for acquisition of expensive IT-systems to process and interpret the information.

## 4. Recent Developments in FATF Work

The FATF updated the members of the Forum about recent activities and developments, including outcomes of a recent dialogue between AML/CFT experts and Data Protection and Privacy experts which took place in Brussels earlier in the week, the adoption of detailed processes and procedures to conduct the 4<sup>th</sup> round of FATF mutual evaluations, and the publication of the following guidance and typologies reports which were developed with key input from the private sector:

- Guidance on New Payment Products and Services;
- Guidance on Politically Exposed Persons;
- Money Laundering and Terrorist Financing Vulnerabilities of Legal Professionals;
- Money Laundering and Terrorist Financing through Trade in Diamonds.

The Private Sector Consultative Forum plays an important role in fostering effective implementation of the FATF Recommendations by bringing together representatives of sectors which are subject to AML/CFT requirements (the financial sector and other designated businesses and professions), civil society, and policy makers to discuss issues of common interest. The FATF reiterates its commitment to continuing engagement with the private sector, and recognizes the value that such dialogue brings to the work of the FATF.

## Vladimir Nechaev The FATF President



– In my opinion, the important feature of this meeting, as opposed to the previous one, was not just the increased number of participants but also their active engagement in discussions. The consultations demonstrated the real two-way dialogue between the representatives of the private sector and the FATF member states and involved experience sharing and discussion on challenges and problems.

The consultations involved extensive discussion on application of the risk-based approach in the banking sector. The private sector representatives suggested the need to maintain the

right balance between financial inclusion and financial exclusion.

In general, the Consultative Forum meeting proved to be the efficient platform for dialogue between the private sector and government authorities. The discussions allowed the members of the FATF working groups involved in the development of the relevant guidance and typology reports to receive feedback and input from the reporting entities.

## Viktor Dostov President, E-Money Association



– The FATF Consultative Forum meeting held in March 2014 was featured by gradual shift from discussion of the revised Recommendations to more focused technical work. Active efforts are being undertaken to revise the FATF Guidance Papers and the preparation for the new round of mutual evaluations is underway. In this context, the information exchange with the private sector is as relevant and important as ever.

This year, the FATF put three broad enough issues on the table for discussion with the largest industry associations. Firstly, the detailed consultations on inclusion of the risk-based approach in the Guidance for the banking sector were held. The participants were given the opportunity to provide their comments and feedback on the previously revised version of the document. Besides that, it was announced that similar Guidance would be developed for non-bank financial institutions (NFI, NFB).

Secondly, the Forum members once again articulated their opinions about risks posed by the virtual currency sector. The FATF holds prudent attitude towards these issues and admits critical importance of innovations. Discussions on the key issues, i.e. whether virtual currencies should be considered as cash equivalent or as non-monetary assets, are not finished yet, and, hopefully, the dialogue will continue.

Thirdly, the FATF discussed the challenges and difficulties faced by the private sector in application of the UN sanctions lists. Although it is primarily the technical problem, its successful solution would allow for more effective implementation of the decisions of the world community and, at the same time, would enable financial institutions to save their resources and mitigate the risks.

The Consultative Forum meeting was as usual rich in events and discussions and once again proved its practical value for both private sector and regulators.



# New Financial Instruments are in FATF's Focus

The revised FATF Recommendations were adopted more than two years ago – in February 2012. Nevertheless, the efforts aimed at bringing multiple FATF documents in line with the revised Standards are still underway. In course of these changes, the adoption of new FATF Guidance for Risk-Based Approach to Prepaid Cards, Mobile Payments and Internet-Based Payment Services in 2013 has been almost unnoticed. Nevertheless, this document is of special interest and importance for Russia. Similar to many other countries, the Russian innovative retail financial services market remains one of the drivers of engaging the population in the non-cash economy.

In order to broaden the scope of the Guidance to the maximum possible extent, the FATF uses the term “new payment products and services (NPPS)” that has replaced the old term “new payment methods”. According to the FATF’s methodology NPPS offer an alternative to traditional financial services. NPPS can be used for transferring money as independent instruments, but also can extend functionality and scope of the services that have already existed in the market.

Such definition can be described as “mutually agreed” rather than “functional”. On the one hand, it lays the groundwork for the future and allow for covering technologies and products that have not emerged in the market yet. On the other hand, it does not mark the boundary between the “new” and “old” instruments which becomes less important. However, the FATF still proposes to distinguish between NPPS and the “new delivery mechanisms” mentioned in Recommendation 15. The most illustrative example is the bank account management methods. For nearly two decades, banks offer the online banking services. i.e. the method of generating and transferring electronic payment orders via the Internet. From the FATF’s standpoint this technology does not fall in the NPPS category, since it is just one of the mechanisms of “delivery” of the bank account (management) services.

On the other hand, the services related to accessing bank account through third party have become more popular in recent years. Such payment providers (defined in the EU as the “payment initiation services”) are not related to actual flow of funds, but just allow for online generation and transfer of payment orders to various credit institutions. In practice, a customer links several bank accounts and cards to one interface and simultaneously manages the funds available on them. Unlike in the previous example, such products fall in the NPPS category, since they are provided by independent operators.

Thus, identification of the NPPS criteria still poses a significant methodological challenge. The fact that a technology is

only partially covered by general banking regulation, i.e. extends beyond the “standard” instruments, may serve as the additional indicator for the supervisory authorities.

However, simple understanding of NPPS does not give the answer to the question about their special role for the AML/CFT purposes. The FATF draws attention to several factors. Firstly, NPPS may be featured by unique ML/FT risks due to their technical specificities. Secondly, NPPS are highly critical for ensuring financial inclusion. The FATF sector-specific Guidance mentions that use of the formal financial services by people contributes to the AML efforts. Lack of access to NPPS leads to increased demand for informal, and often criminal, funds transfer methods. In this context, both lack of regulation and excessively strict requirements may adversely affect the AML/CFT efforts.

The FATF Guidance describes three best known categories of NPPS: prepaid cards, mobile payment services (from both prepaid mobile and special accounts) and Internet-based payment services. All of them assume engagement of a significant number of entities and allow for making instant cashless payments with and without use of a bank account. More specific products, such as virtual payment cards, virtual currency-based payment systems, payment applications with various funding sources, are obviously not included in the Guidance. Nevertheless, even such limited analysis allowed for deriving several conclusions about threats that exist in the NPPS sector.

**The FATF has identified five most significant risks associated with new payment products and services.**

## 1. Non-face-to-face relationships and anonymity

According to the Guidance absence of face-to-face contact with a customer does not necessarily leads to higher risk. If a customer transfers money remotely with the use of a bank card, it does not mean that no information is available on such customer. On the other hand, face-to-face contact does not necessarily prevent impersonation fraud, e.g. when making cash payments. The Guidance suggests that these considerations should be used by the regulators. Countries may establish in their legislation such CDD measures that are not burdensome for customers and can be implemented without face-to-face contact. Where a customer has been identified in one credit institution, why doesn't he/she be allowed to use the details of the issued credit card for the purposes of non-face-to-face identification in other credit institution? A mobile phone (which is registered against presentation of

passport details), electronic (digital) signatures or standard authorization data in the government-provided online services can be used for the similar purposes.

## 2. Geographical reach

Since NPPS are the IT-based products and services, it is not surprising that, as in the IT sector, the boundaries between countries are gradually erased in the NPPS sector. However, in our opinion, this risk is not associated only with NPPS. International payments and settlements have become the every-day practice long before emergence of new payment services, and the currency and foreign exchange control mechanisms developed in connection with that are, in principle, sufficient for mitigating the risks. However, it is a different matter when we consider jurisdictions with certainly higher ML/FT risks, but even in such situations solution of the problem is quite simple. The specific features of most NPPS allow for flexible regulation of their geographical coverage – the most important thing is not to affect their functionality and not to unintentionally force customers to approach unregulated sector.

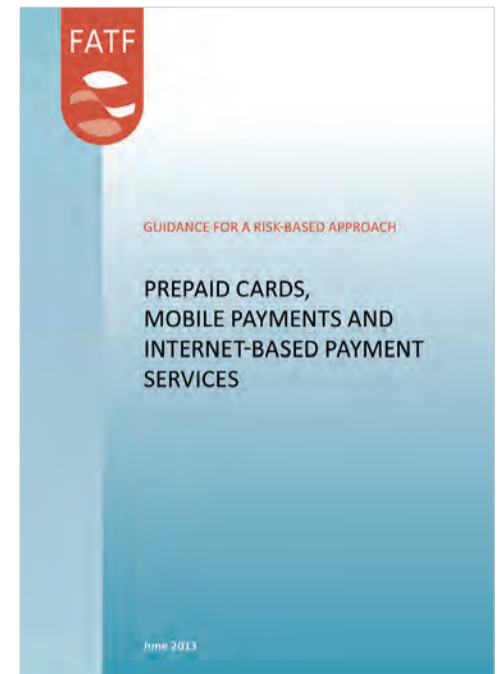
## 3. Methods of funding

From the AML/CFT perspective, there is a significant difference between funding an e-purse with the use of cash and through bank account. On the one hand, credit institutions should exercise caution when payment instruments are funded with the use of cash. But on the other hand, it is necessary to encourage customers to transfer funds from identified instruments (e.g. from a bank card or account) instead of withdrawing cash. In absence of such encouragement, customers would refuse to use NPPS and not cash, which will adversely affect the entire AML/CFT system. The simplest solution of this dilemma is to extend by law the functionality and establish higher transaction thresholds for cashless funding.

## 4. Access to cash

The reverse side of the funding problem is possibility to withdraw cash. In principle, cash withdrawal is not typical for payment systems, but customers cannot be completely denied this opportunity. Some customers use NPPS not for making purchases but for receiving remittances from their family members. In a particular situation, cash may be the only available means of payment. And finally, customers have the indefeasible right to receive their money.

It is noteworthy that the FATF has not criminalized cash transactions “by default”. It just proposes to establish thresholds consistent with the actual level of risk. In this context, a credit should be given to the Russian regulators that use



this particular approach. According to the law, since August 1, 2014, customers will be permitted to withdraw cash in amount of no more than 5,000 rubles per day (no more than 40,000 rubles per month) from non-personalized prepaid cards.

## 5. Segmentation of services

As the payment ecosystem becomes more and more complex, the regulators need to select the adequate approach to supervision of all its parties. It should be kept in mind that not all concerned entities are necessarily involved in transferring funds - only few of them deal directly with customers. Unfortunately, there is no “one-size-fits-all” solution of this problem. Practitioners will have to individually consider each of the NPPS categories and make decisions on establishing requirements for particular types of entities with due consideration for their proportionality and sufficiency.

The FATF Guidance on NPPS does not give all-in-one recommendation on how the innovative financial services sector should be regulated. It must be said, that no other FATF guidelines provide such recommendation. First of all, it shows how closely the innovative technologies are associated with the financial inclusion issues and, hence, with the AML/CFT issues. NPPS not just pose certain risks but are also the useful instruments for ousting informal and criminal financial services from the market. Therefore, the regulators should carefully and thoroughly plan each step aimed at amendment of the legislation. Refusal to apply the risk-based approach may not just have the adverse impact on the mutual evaluation process but can also entail much worse implications, i.e. expose the AML goals and efforts to threat.

*V.L. Dostov, Chairman,  
E-Money Association*