THE COMPLIANCE COMMISSION OF THE BAHAMAS

CUSTOMER DUE DILIGENCE GUIDE

A RISK BASED APPROACH

For

Real Estate Brokers and Land Developers

August 15th, 2019

What is CDD (Customer Due Diligence)?

CDD is the process used by DNFBPs, and other financial firms to collect a series of information on prospective clients primarily at the time of onboarding in order to assess any risk they may bring to the business, such as Money Laundering, Terrorist Financing or any other identified risks.

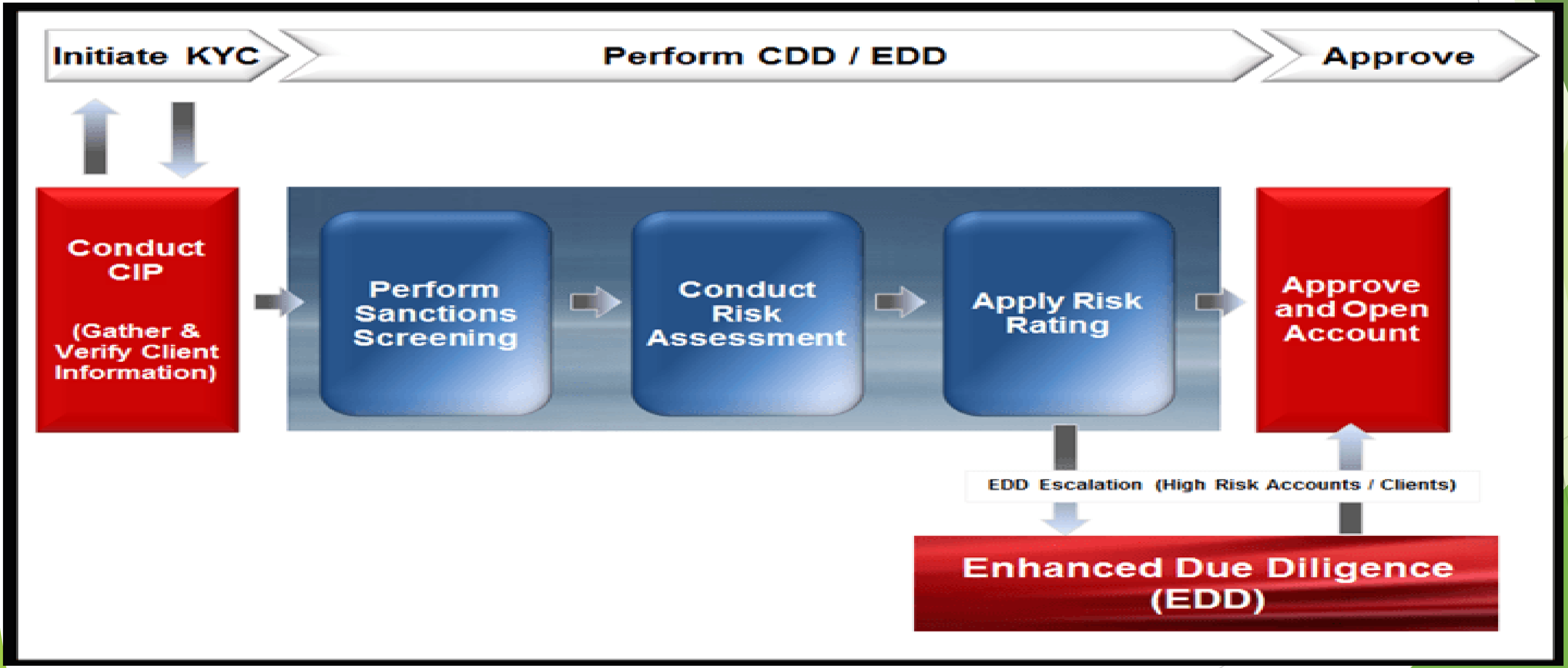
Conducting proper customer due diligence is essential to maintaining proper organizational oversight and is also a legal requirement in the Bahamas as per (FTRA Part II section 6-14)

What is CDD (Customer Due Diligence)?

Customer due diligence is one of the best defense a DNFBP can maintain to protect itself against possible threats of money laundering/terrorist financing and other financial crimes. CDD is also referred to as “know Your Customer,” and it includes the following:

- (1) **Customer Identification** (collecting and verifying customers information and documentation) e.g. KYC form ,
- **(2) Screening customers** (against UN Sanctions list), to determine if a potential customer is known to be of heightened risk and thereby posing a risk to the DNFBP.
- (3) **Risk Assessment/Risk rating:** (measuring risk and assigning rating).
- (4) **ECDD** (performing enhanced measures, monitoring etc. for higher risk customers).

AML/KYC ONBOARDING LIFECYCLE PROCESS FLOW



Why Is CDD Carried Out?

- Primarily CDD is carried out to protect the reputation of your firm and DNFBPs in general. In addition to protecting the reputation of DNFBPs, an effective CDD Program will assist in protecting the financial sector over-all from threats of ML/TF and other identified risks and will allow you:
- (1)To gain **insight** on potential customers, enabling the organization to know just how much of a risk a customer presents with the more prominent risks being Money Laundering and Terrorist Financing.
- (2)To gain a sound **understanding** of the customer's normal and anticipated activity throughout the life of the relationship.

When Is CDD Carried Out?

- DNFBPs should undertake Customer Due Diligence measures, including identifying and verifying the identity of their customers, when: (a) entering into a business relationship or transaction with a customer (b) prior to an occasional transaction taking place (c) where a facility holder is being added to an existing facility (d) where a facility holder seeks to conduct a cash transaction or an occasional transaction involving $15,000 or more on behalf of a third party, using his facility, including situations where the transaction is carried out in a single operation or in several operations that appear to be linked

When Is CDD Carried Out?

For Real Estate Brokers, identification should occur before a contractual relationship is established, that is, when;

- There is a listing agreement;
- There is an agreement of purchase and sale;

The reason for this is, a DNFBP must decide whether a client fit its established risk appetite, and this can only be done if the appropriate CDD procedures/measures were undertaken. Deciding to take a client on without

proper vetting heightens considerably the risk of taking on undesirable clients. Once your customer has been identified and verified there is no requirement to verify their identity again unless there is a material change in the operation of the facility or transactions i.e. a trigger event occurs.

When Is CDD Carried Out? Cont’d

Potential Trigger Events could include:

- Change in ownership of the facility (Beneficial owner changes)
- The product or service that you supply to the customer changes.
- Concerns are raised regarding previous information collected and its validity.
- Activity which give rise to suspicions of money laundering and/or Terrorist Financing or any identified risk.

CDD Guidance on Co-brokering – Real Estate Brokers & Land Developers

Co-brokering takes place when two brokers work together on a sale. One represents the buyer and the other the seller or vendor and work for different companies. One broker brings the buyer and the other listing broker represents the vendor. The buyer is brought to the real estate transaction by a co-broker in a co-brokerage. The broker representing the buyer is responsible for obtaining the CDD on the buyer prior to the agreement for sale. The broker representing the seller must have the CDD on the vendor. In this arrangement there is no requirement for both brokers to exchange CDD information i.e. the listing broker does not have to provide the buyer broker with copies of the CDD and the buyer broker does not have to provide the listing broker with copies of the CDD.

CDD Guidance on Co-brokering – Real Estate Brokers & Land Developers cont’d

The listing broker and the co-broker representing the buyer will exchange letters stating that they have conducted CDD on their client in accordance with the AML/CFT laws, regulations and guidelines in The Bahamas and their records are available to the Competent Authority for review. The co-broker and the listing broker will only be responsible for their own CDD obligations and not exposed to liability that may emerge in the cases where one party did not meet the CDD obligations.

The Benefits of CDD

- CDD **verifies** that the customer is who he/she claims to be;
- **establishes** that the customer actually does own and control the funds; and you gain an understanding of why the relationship is being established and how it will be used in the future.
- Used to **monitor** the relationship/transaction to ensure that the original understanding of the customer's identity and business remains accurate.
- CDD provides the basis for both **preventive** measures in keeping criminal out of the financial systems and also for
- **investigative** measures when trying to identify suspicious transactions.
- Helps to **protect** the reputation and integrity of DNFBPs
- **Reduces** the vulnerabilities of the DNFBPs to ML/TF and other identified risks.

The Benefits of CDD cont'd

- **CDD (an on-going process)** The DNFBPs approach to due diligence should not be **static**, on-going monitoring should be carried out to allow one to detect trigger events which may **impact** the risk and the level of due diligence that is required. On-going monitoring should include the (1)nature of the business relationship as well as (2) targeted financial sanctions and (3)politically exposed person screening

Types/Levels of CDD

- (1) Simplified Due Diligence, (2) Standard Due Diligence ("SDD") and (3) Enhanced Due Diligence ("EDD")
- The amount of CDD measures may be adjusted, to the extent permitted by applicable regulatory requirements, in line with the ML/TF risk. This means that the amount or type of information obtained, or the extent to which this information is verified, must be enhanced or heightened where the risk associated with the business relationship is higher. The type of enhanced due diligence measures applied should be effective and proportionate to the risks also called **RBA (The Risk Based Approach).** It may also be reduced where the risk associated with the client is lower.

Simplified Due Diligence

- Simplified or reduced CDD is the **lowest** level of due diligence that can be completed on a customer.
- Simplified CDD is reserved for those instances where the customer and Product/services combination falls into the lowest risk category where there is little opportunity or risk of ML/TF
- Often customers that are required to disclose information regarding their ownership structure and business activities or companies that are subject to the Anti Money Laundering Regulations are seen to be lower risk.

  Example:

- **Public companies** listed on a stock exchange and subject to disclosure requirements (either by stock exchange rules or through law or enforceable means), which impose requirements to ensure adequate transparency of beneficial ownership.
- **Public administrations** or enterprises(Government).

Simplified Due Diligence cont’d

- When executing simplified due diligence, there is **no** requirement to **verify** your customer's identity as you would with a standard or enhanced due diligence approach.
- If however at any point during the relationship with your customer additional intelligence becomes available, which suggests that the customer or product may pose a higher risk than originally thought a more enhanced level of due diligence should be conducted.

Standard Due Diligence (SDD)

- In the **majority** of cases, standard due diligence is the level of due diligence that will be used. These are generally situations where there is a potential risk but it is unlikely that these risks will be realized.
- **Example** of a standard-risk customers, i.e. those who are permanently resident in the country, with a salaried job or other transparent source of income, only the standard information provided may need to be verified (e.g.ID to confirm name, dob and nationality etc.).
- Standard due diligence requires that the DNFBP **identify** the customer as well as **verify** their identity. In addition, there is a legal requirement to gather information to enable you to understand the nature of the business relationship. This due diligence should provide you with confidence that that you know who your customer is and that your service or product or service is not being used as a tool to launder money or any other criminal activity.

Standard Due Diligence (SDD) cont'd

- As with simplified due diligence there is a requirement to **monitor** your client and the transaction/relationship, this will highlight any potential trigger events that may result in further due diligence being required.
- **'Standard due diligence' should be applied to all clients, unless 'simplified' due diligence or 'enhanced' due diligence is appropriate**

See attached sample KYC Form which includes all required identification/verification information as per FTRA Part III

Enhanced Due Diligence (EDD)

- **Enhance Due Diligence** is required where the customer and product/service combination are considered a greater risk. This higher level of due diligence is required to mitigate the increased risk. A high-risk situation generally occurs where there is a greater opportunity for money laundering or terrorist financing through the **service or product** you are providing your customer. What the enhanced due diligence entails will depend on the nature and severity of the risk.
- In principle compared to Standard Due Diligence, EDD requires more detailed and extensive information, additional measures to be undertaken and a more comprehensive assessment of all involved risks and mitigation measures.

See Appendix C in CDD Guide for Examples of Risk Control/ Mitigation Measures

Enhanced Due Diligence (EDD) cont'd

<u>Situations that signify high risk scenarios:</u>

- **Non- Face to face** business relationship and interactions with your customers.
- **Non-resident** customers.
- When the Client or Beneficial Owner is a Politically Exposed Person **(PEP)**(susceptible to bribery, corruption & ML because of position).
- You know or suspect Money Laundering or Terrorist Financing.
- **Trusts of Fiduciary** relationships(offer anonymity & movement of funds commonly linked to ML/TF).
- Where the applicant for business acts or appears to act in a representative capacity (an agent of a principal).
- Where the client comes or operates from a jurisdiction considered to be **high** risk (having weak or ineffective AML/CFT measures).

Enhanced Due Diligence (EDD) cont'd

<u>**Situations that signify high risk scenarios cont'd**</u>

- **Corporate** vehicles that are unnecessarily and unjustifiably complex multi-tiered entities (i.e., those companies whose management and ownership rights are in turn held by other companies, which are themselves located in foreign jurisdiction(s), and/or those that have more than three layers yet cannot provide a professional opinion justifying an underlying legal or economic rationale).
- Where the client's activities/business or Industry are high risk e.g. **cash intensive clients**, customers purchasing high value goods such as cars, jewelry, real estate

Enhanced Due Diligence (EDD) cont'd

High Risk Scenarios regarding Purchaser Profile and behavior

- These scenarios below help Brokers/developers to perform a risk-analysis for potential purchasers. It is not a complete list of all scenarios with possible links to money laundering or terrorism financing neither does it imply that the scenarios are necessarily linked to such activities.
- While each scenario may not be sufficient to suggest that money laundering or terrorism financing is taking place, a combination of such scenarios may be indicative of a suspicious transaction.

Enhanced Due Diligence (EDD) cont’d

High Risk Scenarios regarding Purchaser Profile and behavior cont’d

- Purchaser is linked to negative news or crime (e.g. he is a designated entity on the United Nations Security Council Resolutions or he is named in a news report on a crime committed.).
- Purchaser provides an address that is unknown, believed to be false, or simply a correspondence address, e.g. a post office box number which might not provide details of the actual address.
- Purchaser buys multiple properties in a short time period and seems to have few concerns about the location and price of each property.
- Purchaser asks about the anti-money laundering and counter financing of terrorism reporting requirements.

Enhanced Due Diligence (EDD) cont’d

High Risk Scenarios regarding Purchaser Profile and behavior cont’d

- Purchaser’s known business activity and purpose **do not match** the real estate transaction, (e.g. purchaser is a non-profit organization, but the property is purchased for investment which requires a large loan)
- Purchaser appears hesitant or **declines** to put his name on any documents that would connect him with the property.
- Purchaser appears to be acting as **proxies** for the purchase of the properties and makes attempts to conceal the identity of the beneficial owner.

Enhanced Due Diligence (EDD) cont'd

High Risk Scenarios regarding Purchaser Transactional Patterns

- Purchaser arrives at a property show unit near to **closing** hours or attempts to make a purchase with a significant amount of **cash**, or negotiable instruments which do not state the identity of the payer (e.g. bank drafts).
- Payments from purchaser are financed by an unusual source, e.g. from an offshore bank located in a jurisdiction identified as high-risk and non-cooperative by FATF.
- Purchaser pays the initial deposit with a cheque from a third party, other than a spouse or parent.

What “High Risk” Does not mean

- A high-risk customer does not mean that the person(s) are or will automatically be involved in ML/TF or other criminal activity but that there is an increased opportunity to be involved.
- Additionally any one of the above scenarios alone does not necessarily mean an individual is corrupt or the situation is automatically high risk. However DNFBPs should managed these risk scenarios by understanding and addressing the potential ML/TF risks associated with these customers and their transactions.

Risk Based Approach (RBA) to CDD

- The Risk Based Approach (RBA), is the method the DNFBPs takes to perform its CDD, based on the level of **risk** that the business faces by taking on each client. Whether that be in relation to:
- **(i)**Type of customer/facility holder; **(ii)** type of products/services/transaction the customer is using or conducting; **(iii)** the geographical areas/jurisdictions of the customer's operations and **(iv)** delivery channels to the customer.
- Once the risks have been identified they can then be mitigated by implementing adequate **policies and procedures** that are proportionate to the risk levels. Having adequate policies and procedures in place also provides a certain level of protection in investigations regarding Money Laundering or Terrorist Financing.

CONCLUSION

Reminder to all Brokers /Developers /Agents

- No one Knows' Your Customer better than you do.
- You have the experience and knowledge of Real Estate and the industry – Don't ignore **Red Flags!!!!!**
- Don't get loss in the process – Apply and tailor procedures & Policies based on the scope of your business risk level.
- Be Guided by the law but listen to your **Gut** instinct when performing CDD.
- Remember we (regulators, brokers/Land developers/Agents) are all together in this fight to protect our Real Estate Industry our jobs and our Country.


That's all Folks!