



**ISLE OF MAN
FINANCIAL SERVICES AUTHORITY**

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Source of Funds & Source of Wealth
AML/CFT Guidance notes
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1. Foreword

This document is issued to cover the period whilst the Anti-Money Laundering & Countering the Financing of Terrorism Handbook ('the Handbook') is being updated. When the new Handbook is published the information contained in this document will be amalgamated into the main body. The Handbook contains guidance on all other areas of the Anti-Money Laundering and Countering the Financing of Terrorism Code 2019.

2. Statutory Requirements of the AML/CFT Code 2019

2.1 Source of Funds

Paragraph 4 – Procedures and Controls

- 4(2) The procedures and controls referred to in sub-paragraph (1) must –
- (a) have regard to the materiality and risk of ML/FT including whether a customer, beneficial owner, beneficiary, introducer or eligible introducer poses a higher risk of ML/FT;
 - (b) enable the relevant person to manage and mitigate the risks of ML/FT that have been identified by the relevant person when carrying out the requirements of this Code; and
 - (c) be approved by the senior management of the relevant person.

Paragraph 3 – Interpretation

“source of funds” means the origin of the particular funds or other assets involved in a business relationship or occasional transaction and includes the activity that generated the funds used in the business relationship or occasional transaction, and the means through which the funds were transferred.

Paragraph 8 – New Business Relationships

8(3) Those procedures and controls are –

...

- (e) taking reasonable measures to establish the source of funds, including where the funds are received from an account not in the name of the customer –
 - (i) understanding and recording the reasons for this;
 - (ii) identifying the account holder and on the basis of materiality and risk of ML/FT taking reasonable measures to verify the identity of the account holder using reliable, independent source documents, data or information; and
 - (iii) if the account holder is assessed as posing a higher risk of ML/FT, satisfying the requirements in paragraph 15.

Paragraph 11 – Occasional Transactions

11(3) Those procedures and controls are –

...

(e) taking reasonable measures to establish the source of funds including, where the funds are received from an account not in the name of the customer –

- (i) understanding and recording the reasons for this;
- (ii) identifying the account holder and on the basis of materiality and risk of ML/FT taking reasonable measures to verify the identity of the account holders using reliable, independent source documents, data or information; and
- (iii) if the account holder is assessed as posing a higher risk of ML/FT, satisfying the requirements in paragraph 15.

2.2 Source of Wealth

Paragraph 4 – Procedures and Controls

4(2) The procedures and controls referred to in sub-paragraph (1) must –

- (a) have regard to the materiality and risk of ML/FT including whether a customer, beneficial owner, beneficiary, introducer or eligible introducer poses a higher risk of ML/FT;
- (b) enable the relevant person to manage and mitigate the risks of ML/FT that have been identified by the relevant person when carrying out the requirements of this Code; and
- (c) be approved by the senior management of the relevant person.

Paragraph 3 – Interpretation

“**source of wealth**” means the origin of a customer’s entire body of wealth and includes the total assets of the customer;

Paragraph 14 – Politically Exposed Persons

14(3) A relevant person must take reasonable measures to establish the source of wealth of –

- (a) a domestic PEP who has been identified as posing a higher risk of ML/FT; and
- (b) any foreign PEP.

Paragraph 15 – Enhanced customer due diligence

15(2) Enhanced customer due diligence includes –

...

- (a) taking reasonable measures to establish the source of the wealth of a customer;

15(3) A relevant person must conduct enhanced customer due diligence –

- (a) where a customer poses a higher risk of ML/FT as assessed by the customer risk assessment;
- (b) without limiting paragraph 13, in the event of any unusual activity; and
- (c) without limiting paragraph 26, in the event of any suspicious activity, unless the relevant person reasonably believes conducting enhanced customer due diligence will tip off the customer.

3. Introduction

The Code requires, at paragraphs 8 and 11, that a relevant person must take reasonable measures to establish the source of funds for all customers when entering a new business relationship or carrying out an occasional transaction.

Paragraph 14 of the Code requires relevant persons to take reasonable measures to establish the source of wealth for all foreign PEPs and domestic PEPs identified as posing a higher ML/FT risk. Paragraph 15 requires relevant persons to take reasonable measures to establish source of wealth where a customer poses a higher ML/FT risk per the customer risk assessment, in the event of unusual activity and in the event of suspicious activity unless the relevant person believes this will tip off the customer.

The requirement is to take “reasonable measures to establish” source of funds and, where necessary, source of wealth, rather than requiring relevant persons to “verify” such. These two terms are distinct. Whereas “verify” would require the use of reliable, independent source documents, data or information in every case, “reasonable measures to establish” allows greater flexibility according to the particular materiality and risk of ML/FT of the business relationship / occasional transaction. Those “reasonable measures to establish” in any given case may therefore range from obtaining information to verifying that information using reliable, independent source documents, data or information, and all the steps in between to enable a relevant person to manage and mitigate their identified ML/FT risks.

“Funds” and “wealth” are two different concepts in the Code in accordance with guidance issued by the FATF. Guidance regarding these concepts can be found below.

4. Source of Funds

Source of funds concerns the origins of the particular funds or other assets involved in a business relationship / occasional transaction (e.g. the amounts being invested, deposited or wired as part of the business relationship / occasional transaction). Source of funds is a twofold concept. It covers:

- the activity(ies) that generated the funds to be used or which concern the business relationship / occasional transaction, e.g. the customer’s salary, returns on investments, inheritance, sale of assets, income from trading etc.; and
- the means through which the customer’s funds are transferred e.g. from a bank account in the name of X.

Some categories of relevant person may not receive the funds that concern the business relationship / occasional transaction, due to the nature of the services provided.

An example of such a business includes where a legal professional undertakes an activity listed at paragraph 2(6)(h) of Schedule 4 of the Proceeds of Crime Act 2008. The legal professional does not have to receive the funds themselves, nor do the funds have to pass through their client account, for the requirement to take reasonable measures to establish the source of funds concerned in the transaction to apply.

A further example can be found with estate agents. The funds for conveyancing transactions go from one advocate’s client account to another advocate’s client account and do not pass through the estate agent, but the estate agent is still required to take reasonable measures to establish source of funds.

4.1 Taking reasonable measures to establish source of funds

The Code requirement to take reasonable measures to establish source of funds is risk based in accordance with paragraph 4(2).

“Taking reasonable measures to establish source of funds” means knowing and understanding the **activities which generated** these specific funds, **who provided or will**

provide the funds in the business relationship / occasional transaction and the means through which the funds were **transferred**.

The depth of research and evidence required to establish source of funds is subject to the materiality and risk of ML/FT. Therefore, the level of work undertaken should vary according to the circumstances of each business relationship / occasional transaction, and be sufficient to enable the relevant person to manage and mitigate identified ML/FT risks.

For example, at the lower risk end of the spectrum it may be reasonable to ask the customer themselves for information about their source of funds without seeking further corroboration or evidence. Conversely, for higher risk customers it may be necessary to further corroborate or verify the information provided in relation to source of funds using reliable, independent source documents. As there are varying degrees of risk associated with business relationships / occasional transactions, there will be varying degrees of what is reasonable between these two extremes. Ultimately, it is a matter for each relevant person to decide what are “reasonable measures” for each business relationship / occasional transaction (or where relevant, category of business relationship / occasional transaction) and be able to justify their decisions and the measures taken.

The flexibility in taking “reasonable measures to establish” source of funds, applies to both the activity(ies) generating the funds to be used in the business relationship / occasional transaction and in respect of the means of transferring the funds (which must be sufficient to ensure reconstruction of the transaction in accordance with paragraph 33(c) of the Code). The particular circumstances of the case will dictate whether it is necessary to apply the same level of measures to the activity(ies) as to the means of transfer, or whether a different level is reasonable. Appropriate information and evidence should be obtained and retained on file.

Where a relevant person is **not** satisfied that the source of funds has been established, the business relationship / occasional transaction must proceed no further, the relationship must be terminated and the relevant person must consider making an internal disclosure. Further information regarding reporting requirements can be found at part 7 of the AML/CFT Handbook.

4.2 Requirements where funds are received from a third party’s account

Where funds are received from an account not in the name of the customer (“third party funding”), there are **specific measures** that must be undertaken in order for the requirement to take reasonable measures to establish source of funds, to be satisfied.

Where third party funding is involved the Code requires relevant persons to understand and record the reasons for this. Relevant persons must take a risk based approach (using the principles above for source of funds) and where appropriate make further enquiries about the relationship between the third party account holder(s) (i.e. the providers of the funds) and the customer and consider beneficial ownership requirements. Consideration must be given to identifying the third party account holder(s) and taking reasonable measures to verify their identity. In the context of paragraph 8(3)(e)(ii) of the Code, “identifying the account

holder” does not necessarily mean seeking specific identity information such as name, date and place of birth, address etc. for each third party. Depending on the transactions concerned, it may be sufficient to ensure a general understanding that the transactions are in line with expected activity.

Where it appears that the customer is acting on behalf of someone else there is further guidance relating to how to determine this under part 4 of the AML/CFT Handbook.

4.3 Ongoing monitoring and source of funds

However a business relationship is treated, relevant persons must ensure they comply with the ongoing monitoring provisions at paragraph 13 of the Code detailed at section 3.4 of the Handbook, including consideration of source of funds where considered necessary.

Though it may well be necessary, in some cases, for a relevant person to have detailed, evidenced in-depth knowledge of each and every transaction involved in a business relationship, it may not be necessary in all cases. What is reasonable, will be a matter for relevant persons to decide in each case. Depending on the relevant person’s ML/FT business and customer risk assessments, and their ability to manage and mitigate ML/FT risk, there may be cases where only certain discrete transactions within the business relationship need to be examined in depth (the depth of such examination also being relative to the materiality and risk of ML/FT). There may also be cases where only a broader understanding of the customer’s source of funds is necessary.

Such determinations at the outset of a business relationship may be subject to change as the business relationship continues and relevant persons must always be mindful of changing circumstances which may become apparent through, for example, ongoing monitoring and / or business and customer risk assessment reviews.

5. Source of wealth

Source of wealth is distinct from source of funds and describes the origins of a customer’s entire body of wealth i.e. total assets / net worth. Relevant person are required to take reasonable measures to establish the source of wealth for all foreign PEPs, all higher risk domestic PEPs and for other customer types where a customer poses a higher ML/FT risk per the customer risk assessment, in the event of unusual activity and in the event of suspicious activity unless the relevant person believes this will tip off the customer.

Generally, information obtained should give an indication as to the volume of wealth the customer has or controls and how such wealth was acquired (i.e. those activities which have generated a customer’s funds and property). It is recognised that it may not always be possible for a relevant person to obtain a complete overview of a customer’s entire body of assets, for example in cases where the wealth has been generated across a wide range of activities and over a longer time period. Further, sometimes such information is not voluntarily disclosed, although failure to voluntarily disclose such information, when requested, could also be considered a red flag for ML/FT.

Relevant persons may also be able to gather general wealth information about a customer from commercial databases or other open sources.

5.1 Taking reasonable measures to establish source of wealth

Reasonable measures to establish source of wealth is about building a broad understanding of a customer's overall sources of wealth.

Source of wealth requirements at paragraphs 14 and 15 of the Code must be conducted using a risk based approach in accordance with paragraph 4(2) of the Code. The procedures and practices put in place to satisfy these requirements must enable relevant persons to manage and mitigate their identified risks of ML/FT.

Therefore "reasonable measures" in establishing source of wealth for each relevant customer may vary according to the circumstances. Unlike the source of funds requirements, which are applicable to all customer relationships, source of wealth starts from a high risk threshold because it is particular to higher risk customers only.

This higher risk starting point must be taken into account when considering what source of wealth information, and methods used to establish source of wealth, would be reasonable. However, even with a higher risk starting point, the measures relevant persons take to establish source of wealth should reflect the degree of high risk associated with the business relationship, and also what factor(s) are driving that risk level. For example, at the highest level of risk, taking reasonable measures to establish source of wealth means that a relevant person should consider verifying the source of wealth on the basis of reliable and independent data, documents or information.

Where a relevant person is not satisfied that source of wealth has been established where necessary, the business relationship or occasional transaction must proceed no further, and consideration must be given to terminating that relationship and to making an internal disclosure. Further information regarding reporting requirements can be found at part 7 of the AML/CFT Handbook.

6. Researching and verifying source of funds and/or wealth

When researching source of funds and source of wealth, relevant persons should focus on what can be reasonably explained, rather than on what might be expected.

Sources of information which are useful for verifying the accuracy of a customer's declaration about source of funds and / or wealth include, but are not limited to:

- an original or certified copy of a recent pay slip;
- written confirmation of annual salary signed by an employer;
- an original or certified copy of contract of sale of, for example, investments or a company;
- written confirmation of sale signed by an advocate or solicitor;
- an original or certified copy of a will or grant of probate;

- written confirmation of inheritance signed by an advocate, solicitor, trustee or executor;
- an internet search of a company registry to confirm the sale of a company;
- publicly available property registers, land registers, asset disclosure registers (particularly in the case of PEPs);
- VAT and income tax returns;
- copies of audited accounts;
- public deeds;
- independent media reports.

Discrepancies between customer declarations and information from other sources could be indicators of ML/FT activity and should never be disregarded.