The Financial Intelligence Centre's feedback on the comments received through the consultation process on draft public compliance communication 112 guidance on the identification of money laundering and terrorist financing risks and associated customer due diligence for clients of authorised users of an exchange in terms of the Financial Intelligence Centre, 2001 (Act 38 of 2001)

Paragraph	Comment	Response comments
PCC Summary	**<u>Commentator A</u>** Commentator A opinion is as follows: 1. The PCC Notice must include the previous Exemption 4(b) and 2 in the motivation. Authorized users do not believe that Exemption 4(b) is covered in PCC 43 which deals with a shared client. 2. "Counterparty" is a previously defined term in the Financial Markets Act (FMA) and the Margin Rules and has a different meaning in both these pieces of legislation. The commentator therefore suggests that the definition of "counterparty" must be amended and propose the terms "Primary Client" and "Underlying Client Accounts" be used. As the term "Counterparty" is defined in other legislation it is felt that using the term "counterparty" to suit the purposes of this PCC will only create confusion. An amendment is therefore vital. 3. S21 does not apply to the Underlying Client Accounts of the Primary Client, as there is no business relationship between the Authorised User and the Underlying Client Accounts. As such, no Customer Due Diligence (CDD) information can be obtained and validated from these Underlying Client Accounts and no monitoring and reporting on those activated can take place. Consequently, the commentator is of the opinion that S21 does not apply to underlying client accounts as these are not clients of the Authorised User, no cash and shares are in the	1. It is not the intention to bring back the exemption 4 through this PCC. Exemption 4 principles are covered in PCC 43 regarding shared clients. This PCC makes it clear that this is a risk consideration regarding the accountable institution's own client. Further, this PCC talks broader than AI to AI relationships- and includes foreign entities and other entities that do not meet the SA definition of AI. The principles contained in exemption 4 cannot be applied in the context of this PCC as the very basis of application is not founded. given the move to a risk-based adoption to the FIC Act. 2. The term primary and secondary cannot be used as this concept does not apply in the context of this PCC. There is no primary and/or secondary. Rather there are entities which are AIs or foreign financial institutions and their clients in respect of which they have a CDD obligation, which includes understanding the associated ML/TF risks. The term counter party is a generic term and does not infer meaning outside the ordinary dictionary meaning and is to be understood within the context of this PCC. Operationally, this term can be deemed anything as determined by the AI, this term is the simplest manner for conveying the message. Terms such as underlying client have been explicitly avoided owing to unintended consequences that could arise.

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	control of the Authorised User and no business relationship has been established. As a result, S21 cannot apply. Furthermore, no risk rating, monitoring, or reporting can be performed on any of these underlying accounts. The authorised user will ensure compliance with S20A and ensure that there are no anonymous accounts in their books. The name of the client, bank details CSDP and jurisdiction will be obtained for all underlying accounts of the Primary client. 4. The commentator notes that the Authorised User cannot perform continuous transactional monitoring for a non-controlled "Primary client". This category of client and their customer profile does not allow continuous monitoring and mechanisms to identify any potential suspicious transactions due to their trading patterns across multiple authorised users and FSPs. 5. The commentator is of the opinion that it will be beneficial to include the definitions of controlled client and non-controlled client within the ambit of the business of an Authorised User. 6. Please note that the following terms are all synonymous and can be used interchangeably. They have the same meaning as: • Asset Manager; • Investment Manager; and • FSP • Institutional Asset manager (IAM) • Intermediary • Person/Client	3. This PCC does not infer that the 'underlying client' as expressed by the commentator is the client, nor that CDD documentation and or monitoring be required. This comment is expressed within the ambit of the FIC Act prior to the 2017 amendments. With the adoption of a risk-based approach, there has been a fundamental shift in the application of CDD and it is imperative that the effective application of CDD be performed within the context and understanding of ML/TF risk. This PCC seeks to clarify this and assist AIs in the understanding of CDD. 4. Monitoring of transactions to inform STR is required in respect of clients in terms of S21C 5. This PCC covers the principle of applying understanding ML/TF risk to CDD, and to aid in understanding where an AI has a CDD obligation in respect of a client. The PCC intentionally does not included definitions of particular client categories as this is operational in nature and is required by the AI to understand how the ML/TF risks and CDD is applied to their client categories. 6. Discussed above, there will not be a change to primary or secondary.

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	The above are all referred to in the document as the "Primary Client" (Counterparty). The commentators' comments are as follows: If the authorised user performs CDD on their primary client (i.e. the counterparty) as per their documented RMCP and performs their own Risk assessment as part of the approved RBA of their primary client, the requirement for "sufficient information" to be obtained with respect to the Underlying Client Accounts i.e. client of the counterparty, is not understood. It is the view of the commentator that no information is required to be obtained from the primary clients (counterparty's) underlying client accounts i.e. the client. They are not the client of the Authorised User and do not have a business relationship with the Authorised User. Therefore there is no legal justification for Underlying Client Accounts to provide the Authorised User with any information.	This PCC sets to aid AIs in understanding the application of ML/TF risk in relation to CDD. See comment 1. In order to make a determination as to the ML/TF risk, the AI is required to obtain sufficient information in order to make this determination. The FIC Act sets the minimum CDD criteria and is not prescriptive. Therefore, the AI is to determine what information is sufficient to obtain in order to make this determination. The PCC does not indicate that this information must be obtained from the client of the counterparty; and can be obtained from the counterparty client if so required.
PCC Summary	**Commentator B** There are in fact only 2 ways in which an Authorised User may interact with a client, namely: • directly, (i) where there are no underlying customers of a client or (ii) where there are underlying customers of a client; or	The proposed diagrams were to be read within context of the PCC for illustrative purposes only. This PCC does not seek to bring in new categories of clients, but merely uses the diagram to illustrate the meaning – specifically relating to the relationship the AI would have in relation to their CDD objectives towards a particular entity. "Direct" demonstrates that there are no other persons involved and the only

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	• indirectly, (i) where a client is representing a third party or (ii) where a client is represented by a third party. The 3rd scenario, i.e. "a direct interaction where there is a counterparty and the client of the counterparty involved", is still a direct relationship between the Authorised User and a client. It being specifically noted in the diagram on page 5 of the draft PCC 112, i.e. that there is no business relationship between the Authorised Dealer and the underlying customer of the client. The position being put forward in the draft PCC 112, in respect of this direct interaction/engagement is that the Authorised User must understand the nature of the business of its client and that such client may have underlying customers. In such event, per the recommendations set out in the draft PCC 112, the Authorised User is to give due consideration to the underlying customer (if present) of a client, in order to appropriately risk rate its client. Accordingly, any reference to involvement would be incorrect as there is no 'involvement' by the underlying customer of a client contemplated in the 1st and 3rd (last scenario). The mere reference to the word 'involvement/involved' would in all likelihood result in varying interpretations and thereby lead to unnecessary confusion, ambiguity, and legal uncertainty.	entity to consider for ML/TF purposes would be their client (and other associated person if an entity or PEP identification) A major focus of this PCC is to correct the current market practice/interpretation. Thisdiscussion must be read in the context of understanding of risk

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	RECOMMENDATIONS Commentator recommends that the draft PCC 112 be amended to: • cater for direct and indirect interactions/engagements as provided for in the comments and as contemplated by the FIC in paragraph 1.2 which states: "This PCC seeks to assist authorised users in applying effective risk management and CDD in direct and/or indirect engagements with their clients, as counterparties."; and • that any reference to involvement by an underlying customer of a client to the Authorised User, be deleted.	
Paragraph 1.3.	**<u>Commentator A</u>** The commentator is in agreement that the counterparty is the Primary Client with whom the Authorised User enters into a business relationship i.e. the other accountable institution who is an authorised FSP as defined under the FAIS Act. The statement "In so doing, disruption or interruption to stock broking trade will be limited" does not make sense. Further clarity is required. It must be noted that the timing of the booking/allocation of a trade to the Primary Clients – Underlying client accounts will in some cases have a timing issue which was previously covered under Exemption 2. The information regarding the underlying accounts is only received after the instruction is received by the Primary	ML/TF risk must be determined prior to CDD – as this informs what is required from a CDD perspective. In having this process done in advance, it will prevent a hold up of a trade taking place- ie. There is no need to wait for the administration behind CDD which will prevent a timeous trade. If information that informs the ML/TF risk of a client is received only afterwards, this does not amount to a proper or adequate review of the clients ML/TF risk (ie. how can you determine risk and CDD after the transaction has taken place?) Exemption 2 – timing of CDD. This principle is replaced by ML/TF risk understanding, without which CDD cannot be established. The

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	Client and is executed by the authorised user and therefore cannot be done prior to the execution of the trade.	exemption allows one to receive a mandate prior to the conclusion of transaction – this PCC says no different.
Paragraph 2.3.	**Commentator A** The commentator is in agreement with the statement that, "An authorised user must understand and assess the ML/TF risks introduced by each of its clients". The commentator is of the opinion that the following statement should be removed as it has no basis. "the authorised user must understand and assess what inherent ML/TF risks the client of the counterparty presents." The Authorised User must understand and assess what inherent ML/FT risk the "primary client" i.e. the counterparty presents, as only the business relationship has been established with the Primary client and not with the underlying the client of the Authorised User, who is the "Primary client" and not the "Underlying client accounts" i.e. client of the counterparty. The Authorised User has no access to any CDD information or other related information that will enable the Authorised User to perform the inherent risk assessment of the underlying client accounts of the primary client i.e. the counterparty. It is further noted that the Authorised User never establishes a business relationship with the Underlying Client Accounts. Therefore there are no CDD, transactional monitoring etc…requirements that are applicable.	This is the behaviour, and misinterpretation that the FIC is seeking to correct through this PCC. This interpretation in respect of the client (where there is an 'underlying client' as detailed in the comment, and specifically not used in the draft PCC) is incorrect. Where the counterparty client has a client that is not party to a transaction – this information is critical to understand the ML/TF risk associated with the client. The text in the PCC that follows does not require CDD to be obtained, rather sufficient information to make a determination in terms of risk.

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Paragraph 3.2.	**<u>Commentator B</u>** Whilst the draft PCC 12 confirms that the Authorised User does not have a CDD obligation, the use of the words "would need" borders on the prescriptive and suggests (especially through the use of the word "would") the obligatory nature of understanding the risk of the client of the counterparty which is contrary to the nature and purpose of a risk-based approach. RECOMMENDATION The commentator recommends that the sentence "… they would need to obtain sufficient information about the client of the counterparty in order to …" be amended to read "…they [would] *may* need to obtain sufficient information about the client of the counterparty, *subject to the risk-based approach adopted by the authorized user*, in order to …". [ ] = deletion * = insertion This will provide for legal certainty in that the draft PCC 112 is not prescriptive as to obligation of obtaining of information in light of the amendments to the FIC Act that allows for the implementation of a risk-based approach, thereby moving away from prescriptive rules.	AIs are required to obtain information that will assist them in making a determination of the ML/TF risks. As such, there is a certain amount of information that needs to be obtained. This is an expansion on the client risk factor as detailed in GN7. Failure to obtain sufficient information would lead to inadequate understanding and assessment of risk. This PCC is not prescriptive in detailing what information must be obtained by the AI to make such a determination, and gives the FIC's interpretation of what factors should be considered in respect of the client

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Paragraph 3.3.	**<u>Commentator B</u>** Notwithstanding the use of the words "could include" which may not imply a mandatory requirement, the list of information to be considered especially on the information of the client of the counterparty still suggests a regulatory expectation that the defined and specific information be collected. This is contrary to the purpose of a risk-based approach which is enshrined in the amendments to FICA and the move away from prescriptive rules. By listing defined and specific questions to be considered especially insofar as the counterparty's client, the draft PCC 112 indirectly requires the fulfillment of these due diligence questions as the perception may be created that if an institution followed its own risk-based approach and its own on-boarding requirements with the exclusion of these probing and prescriptive questions that the suggestion be that the institution has misunderstood the risk. RECOMMENDATION The commentator recommends that the sentence "This information could include:" be amended to read "This information, *which is subject to the risk-based approach followed by the authorised user*, could, *for example*, include:". [ ] = deletion	The list of information is not exhaustive and provides information that could assist the AI in their understanding and implementation of an effective RBA within their RMCP. This is clarified in the PCC. The nature of this PCC is to assist in the understanding of the application of risk factors relating to client in the AU scenario of a client of the counterparty and to correct a misinterpretation of CDD.

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	* = insertion This will provide for legal certainty in that the draft PCC 112 is not prescriptive as to the information that must be obtained by Authorised Users in light of the amendments to the FIC Act that allows for the implementation of a risk-based approach, thereby moving away from prescriptive rules. Alternatively, the FIC should give consideration to advising/giving guidance as to the minimum standard information requirement for the underlying customers, thereby creating a minimum standard approach for the market. A risk based approach will still be applicable and further information can then be obtained where necessary. Without a minimum standard information requirement, there is a potential regulatory risk, where limited information or no information is obtained by the Authorised User in respect of their RMCP.	