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**Private and confidential**  
Mr Allen Wicomb  
Committee Secretary  
Standing Committee on Finance

Our ref L21511-21792

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Dear Sir

## **Commentary on the Financial Intelligence Centre Amendment Bill, 2015**

### **1 Introduction**

We thank you for the opportunity to provide commentary on the Financial Intelligence Centre Amendment Bill, 2015 (the Amendment Bill). At the onset, we would like to state that we have noted the numerous enhancements to the current Financial Intelligence Centre Act (Act No. 38 of 2001), which amendments will have a positive impact not only in aligning the South African Anti-Money Laundering (AML) and Combatting the Financing of Terrorism (CFT) regulatory framework to international better practice, but to improve the efficiency with which South Africa combats Money Laundering (ML) and the Financing of Terrorism (TF).

The remainder of this document focuses on areas where we suggest further enhancements or clarification on certain aspects. The topics addressed below are:

- The scope of section 42(2)(a) of the Amendment Bill;

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Registration number 1999/012876/07

Policy Board:  
Chief Executive: TH Hoole

Executive Directors: N Dlomu, M Letsitsi, SL Louw, NKS Majaba,  
M Oddy, M Saloojee, CAT Smit

Other Directors: ZH De Beer, LP Fourie, N Fubu,  
AH Jaffer (Chairman of the Board), FA Karreem,  
ME Magondo, AMS Mokgabudi, GM Pickering,  
JN Pierce, T Rossouw, GCC Smith

The company's principal place of business is at KPMG Crescent,  
85 Empire Road, Parktown, where a list of the directors' names is  
available for inspection.

- The definition of Beneficial Owner; and
- The definition of Domestic Prominent Influential Person.

We will furthermore only be providing this written submission and will not be in a position to make oral presentation to the committee.

## **2 Scope of section 42(2)(a)**

### **2.1 *International guidance on AML/CFT Risk Based Approach***

International guidance distinguishes between the following two elements of a comprehensive AML/CFT risk assessment, both of which inform an organisation's Risk Based Approach (RBA). The elements are:

- A customer risk assessment; and
- Business risk assessment.

The international guidance on ML/TF risk assessments, can most profoundly be found in the three documents discussed below. What is important to note from the extracts below, is that limiting a ML/TF risk assessment only to the customer due diligence process (ie the customer risk assessment) will result in an incomplete ML/TF risk assessment and an inadequate RBA.

### **2.2 *Financial Action Task Force***

The Financial Action Task Force (FATF) issued a document styled "*Risk Based Approach guidance for the banking sector*", in 2014. The sections emphasised by us in the extract below, indicates that an AML/CFT risk assessment goes beyond only a customer risk assessment, and should include a business risk assessment:

***"56. In identifying and assessing the ML/TF risk to which they are exposed, banks should consider a range of factors which may include:***

- The nature, scale, diversity and complexity of their business;***

- *Their target markets;*
- *The number of customers already identified as high risk;*
- *The jurisdictions the bank is exposed to, either through its own activities or the activities of customers, especially jurisdictions with relatively higher levels of corruption or organised crime, and/or deficient AML/CFT controls and listed by FATF;*
- *The distribution channels, including the extent to which the bank deals directly with the customer or the extent to which it relies (or is allowed to rely on) third parties to conduct CDD and the use of technology;*
- *The internal audit and regulatory findings;*
- *The volume and size of its transactions, considering the usual activity of the bank and the profile of its customers."*

### 2.3 **Basel Committee on Banking Supervision**

In January 2014, the Basel Committee on Banking Supervision issued a document styled "*Sound management of risk relating to money laundering and financing of terrorism*". Paragraph 15 of this document states inter alia that (our emphasis):

*"In conducting a comprehensive risk assessment to evaluate ML/FT risks, a bank should consider all the relevant inherent and residual risk factors at the country, sectoral, bank and business relationship level, among others, in order to determine its risk profile and the appropriate level of mitigation to be applied."*

The above extract clearly indicates that the ML/TF risks that an organisation is exposed to on a "*business relationship level*" (ie referring to its customers) is but one factor to consider when determining the ML/TF risk profile of an organisation, and that organisation wide risks should also be determined, ie risks on country, sectoral and bank level.

## **2.4 *The Wolfsberg Group***

In September 2015, the Wolfsberg Group issued a frequently asked questions document on risk assessments, including ML/TF risk assessments. This document also quotes the paragraph from the Basel document referred to above, and then continues to use the words “*enterprise-wide risk assessments*”, ie clearly moving away from only focusing on customer level risk assessments as the sole focus of a ML/TF risk assessment. The document further elaborates on this term, pointing out that organisations may elect to perform a business risk assessment on an enterprise-wide level, with further categorisations focusing on regions or divisions in the organisation. It furthermore provides guidance on, after determining the inherent ML/TF risk profile of the organisation, how to assess the effectiveness of the AML/CFT controls, in order to finally determine the residual ML/TF risk profile of the organisation. The determination of the residual ML/TF risk profile of an organisation is something that does not form part of a customer risk assessment and clearly emphasises the importance of a more comprehensive ML/TF risk assessment.

## **2.5 *Summary on international guidance***

The necessity and benefits of a robust ML/TF customer risk assessment process, as part of the customer due diligence process, cannot be disputed. The outcome of the customer risk assessment process informs the level of due diligence to be performed, both at onboarding and whilst performing continuous monitoring of the relationship.

However, a comprehensive AML/CFT Risk Management and Compliance Programme encompasses much more than merely a customer due diligence process during onboarding and continuous monitoring, which is why the enterprise-wide risk assessment is required to develop a ‘fit-for-purpose’ AML/CFT Risk Management and Compliance Programme, commensurate with the specific risks of each organisation.

The benefits of an enterprise-wide ML/TF risk assessment are therefore definitely not subordinate to those of a customer risk assessment. Some of the benefits are:

- Enabling senior management to have a comprehensive understanding of the ML/TF profile and risk distribution in their organisation (both on an inherent and residual level) and whether it is acceptable within the risk appetite of the organisation;



- Based on the above, determining whether the Risk Management and Compliance Programme as envisaged by the Amendment Bill, is robust enough and commensurate with the inherent ML/TF risk profile of the organisation; and
- Enabling those responsible for AML/CFT oversight, to assess whether the organisation's limited resources (people, processes and systems) are applied efficiently, with more emphasis on those areas of the business with higher risk.

## **2.6 *Guidance Note 1, section 42(2)(a) of the Amendment Bill, and the Memorandum on the objectives of the Financial Intelligence Centre Amendment Bill, 2015***

Guidance Note 1 introduced the concept of an RBA when performing customer due diligence in South Africa.

The Amendment Bill deals with the scope of an RBA in section 42(2)(a), which requires organisations to identify, assess, monitor, mitigate and manage the risk that the provision by the accountable institution of products or services may involve or facilitate ML activities or the financing of terrorist activities and related parties.

It is open for interpretation whether the requirements set out above, focus only on the customer due diligence process, or includes an enterprise-wide ML/TF risk assessment. However, based on the "*DRAFT MEMORANDUM ON THE OBJECTS (sic) OF FINANCIAL INTELLIGENCE CENTRE AMENDMENT BILL, 2015*" issued in conjunction with the Amendment Bill, it appears that the focus is unfortunately solely on the customer due diligence process. This inference is based on the following:

- Seven objectives of the Amendment Bill are listed in the draft memorandum referred to above. The only objective that refers to an RBA can be found in objective 2 which states:

*"2.2.2 Providing for the adoption of a Risk-Based Approach to Customer Due Diligence*

*Provision is made in the Bill for the application of a risk-based approach to customer due diligence, which entails that an accountable institution should identify, assess, and understand its AML/CFT risks.*” (Our emphasis);

- Paragraph 3.27 of the draft memorandum deals with the introduction of section 42(2)(a) in the Amendment Bill. It again links the risk assessment process only to the customer due diligence process, by stating:

*“The customer due diligence measures mentioned above are linked with an accountable institution’s application of a risk-based approach through the institution’s AML and CFT compliance and risk management programme.”*

Even the invite received from your committee, only makes mention of an RBA in the context of customer due diligence, as it describes one of the objectives of the Amendment Bill as: *“to provide for a risk based approach to client identification and verification”*.

## **2.7 KPMG experience and summary on the scope of section 42(2)(a)**

We know from experience that organisations struggle with the concept of distinguishing between that nature and objective of a ML/TF customer risk assessment and a ML/TF business risk assessment and the value that both types of risk assessments contribute to the overall management of the ML/TF risk in an organisation.

Leaving any room for interpretation in the new FIC Act, on whether or not section 42 includes the requirement for an enterprise-wide risk assessment, will severely negate the introduction of a comprehensive and effective RBA in the South African AML/CFT regulatory framework and nullify the effort that has been made to align our regulatory framework to international better practice in this regard.

An enterprise-wide ML/TF risk assessment is not an element of an effective AML/CFT management programme, **it is the foundation on which such a programme should be developed**. Therefore, in the absence of an enterprise-wide ML/TF risk assessment, the development of a Risk Management and Compliance Programme, as envisaged in the Amendment Bill, may become an academic exercise, as opposed to a processes aimed at developing a programme tailored for each particular organisation’s ML/TF risk profile.

**3. Definition of Beneficial Owner**

The newly introduced definition of a Beneficial Owner, includes reference to “*connected persons*”. We are of the opinion that the term ‘connected person’ can be interpreted differently by individuals and organisations and as such, should be defined in the new Act.

**4. Definition of Domestic Prominent Influential Person**

Sub-paragraph (b) of the definition of Domestic Prominent Influential Person (PIP) refers to certain officials of companies, if a company provides a to-be determined Rand amount annually, of goods and services, to an “*organ of state*”.

It is not specifically noted in the definition, if the term “*organ of state*”, refers only to organs of state in the Republic of South Africa, or also foreign organs of state and we recommend that this be clarified. We furthermore recommend that the term “*organ of state*” should include foreign organs of state.

In a Transparency International Report dated 20 August 2015 and styled “*2015 Progress Report, Exporting Corruption*”, South Africa was found lacking in its commitment to investigate and prosecute cross-border corruption, ie referring to allegations of South African companies bribing foreign officials in order to secure contracts or licenses and concessions.

Including foreign organs of state in the definition of a PIP, will lay a preventative foundation, to address potential cross-border corruption by South African companies.

Please do not hesitate to contact us should you require further clarification on the above.

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Yours faithfully  
KPMG Services



Per: Tersia Rossouw  
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