

Note on Prevention for Anti Money Laundering (PMLA rules 2002)

The Prevention of Money Laundering Act, 2002 (PMLA) was brought into force with effect from 1st July 2005. Necessary Notifications / Rules under the said Act were published in the Gazette of India on July 01, 2005 by SEBI.

The PMLA guideline requires all intermediaries to adhere to these guidelines and try and implement the requirements while dealing for their clients apart from the stringent client identifications. Some of the other requirements are as given hereafter:

Important Definitions:

1. *"intermediary" means a stock-broker, sub-broker, share transfer agent, banker to an issue, trustee to a trust deed, registrar to an issue, merchant banker, underwriter, portfolio manager, investment adviser and any other intermediary associated with securities market and registered under section 12 of the Securities and Exchange Board of India Act, 1992;*
2. *"proceeds of crime" means any property derived or obtained, directly or indirectly, by any person as a result of criminal activity relating to a scheduled offence or the value of any such property*
3. *"scheduled offence" means - i) the offences specified under Part A of the Schedule; or ii) the offences specified under Part B of the Schedule if the total value involved in such offences is thirty lakh rupees or more;*

Principle officer

The company has appointed Mr. S.S. Gulati as Principal Officer for framing, updating and monitoring the internal controls, policies and procedures as per the requirements of Prevention of Money Laundering Act – 2002 (hereinafter referred to as Act).

Customer Due Diligence

New account opening procedures

The overriding principles in the identification and verification processes are Know Your Client ("KYC") and Know Your Business ("KYB"). These principles, as well as being essential elements in combating money laundering and terrorist financing, enable LKP to service its clients better. They are also essential in terms of recognition of suspicious activity. It is NOT the case that all unusual clients, transactions or circumstances need to be reported, just those that are suspicious, but it is a good place to start. It may be that upon further enquiry, the unusual elements are found to be fine, but if not, they need to be reported to Principal Officer for further consideration.

As a general rule, new client forms must be completed in relation to all new clients. Copies of identification evidence as requested on the form must be obtained as soon as possible. Customer identification and verification depending on nature /status of the customer and kind of transactions that

are expected by the customer. Independent verification of the client's identity and address should be undertaken. If it is impossible to identify the client, then he should be turned away. continuously scan all existing accounts to ensure that no account is held by or linked to any of the entities or individuals included in the list.

In the case of corporate clients or partnerships, certified copies of incorporation documents should be obtained and at a minimum, the identity of at least one of the executive directors or equity partners should be checked in accordance with individual identification procedures. Steps should be taken to identify those with ultimate control over the company (e.g. shareholders). If possible a visit should be rendered to the potential client, as it is a good action to meet the risk face-to-face.

For existing clients processes include:

- a. Review of KYC details of all the existing active clients.
- b. In case of non individuals client additional information about the directors, partners and major shareholder is obtained.
- c. Obtaining of financial documents from all clients on yearly basis.

Clients of special category (CSC)

- I. Non-resident clients.
- II. High net-worth clients,
- III. Trust, Charities, NGOs and organizations receiving donations,
- IV. Companies having close family shareholdings or beneficial ownership,
- V. Politically exposed persons (PEP). Politically exposed persons are individuals who are or have been entrusted with prominent public functions in a foreign country, e.g., Heads of States or of Governments, senior politicians, senior government/judicial/military officers, senior executives of state-owned corporations, important political party officials, etc. The additional norms applicable to PEP as contained in the subsequent clause 5.5 (Page 19 of the Master Circular) shall also be applied to the accounts of the family members or close relatives of PEPs,
- VI. Companies offering foreign exchange offerings,
- VII. Clients in high risk countries (where existence / effectiveness of money laundering controls is suspect or which do not or insufficiently apply FATF standards, where there is unusual banking secrecy, Countries active in narcotics production, Countries where corruption (as per Transparency International Corruption Perception Index) is highly prevalent, Countries against which government sanctions are applied, Countries reputed to be any of the following – Havens / sponsors of international terrorism, offshore financial centers, tax havens, countries where fraud is highly prevalent.
- VIII. Non face to face clients.
- IX. Clients with dubious reputation as per public information available etc.

RISK CATEGORIZATION OF CLIENTS:

High Risk Clients:

1. Trust accounts
2. Clients who are refusing to provide their financial details / source of income.
3. Non - Individual Clients having close family shareholdings i.e. less than 5 shareholders or if a single person shareholding is more 75% of the total shares.
4. Loss making Non- Individual clients or if reserves and surplus balance is less than Rs. 5 lac.
5. Clients against whom any action has been taken by SEBI/Stock Exchange or any other regulatory authority.
6. Corporate / Partnership Firms / any other entities with track record of less than 2 years.
7. Individual clients whose employer is a politician, income tax / custom department / any other governmental department.
8. NRI clients.
9. Corporate clients not disclosing the identity, address of Directors, not giving financial statements.
10. Clients residing in highly sensitive areas. For example, naxalite regions, areas where dealing in narcotic drugs, immoral traffic, corruption, etc is highly predominant. Thi: includes person residing in UAE, Chandrapur (India), Kashmir (India), Leh-Ladakh, Pakistan, Kuwait, Irar & Iraq, Bangaladesh.
11. Client having bank account with countries where secrecy of the account is maintained.

Medium Risk Clients:

1. Individuals whose annual income ranges for last three years is Rs. 25,00,000 and above and who have nc submitted any financial documents.
2. Client whose account is operated by PQA holder other than LKP.
3. Clients who has given trading authorization in some other person's name, (excluding sub broker)
4. House wife Accounts.
5. Clients who have not given the nature of business or nature of business are lending, investment, finance credit etc.

Low Risk Clients:

All clients not meeting the above criterions are low risk clients.

EXAMPLES OF REASON FOR SUSPICION AND OF SUSPICIOUS TRANSACTIONS

The examples given herein below have been structured around the business processes within our industry. The 1 of examples is not exhaustive. The examples below should be read in the context of the particular transaction.

The regular monitoring of all customers — both new and longstanding — must include consideration of whether accounts are being used for questionable purposes.

While it is impossible to list all the transactions or circumstances that might raise a suspicion of money laundering, the following questions should be closely considered:

Is the customer willing to accept uneconomic terms without apparent reason?

Is the transaction inconsistent with legitimate business activity?

Is the transaction inconsistent with the normal pattern of the customer's activity?

Is the transaction inconsistent with the customer's account-opening documents?

Has the customer requested that the transaction be cleared in a way that is inconsistent with normal practice?

Has the customer received wire transfers from, or sent wire transfers to, countries that have not previously been associated with the customer's business?

Is the customer or the customer's business activity associated with countries recognized by regulators as high-risk money laundering centers?

New business

False identification documents

Identification documents which could not be verified within reasonable time

A person for whom verification of identity proves unusually difficult or who is reluctant to provide details

Non-face to face clients or doubt over the real beneficiary of the account

Accounts opened with names very close to other established business entities

A person where there are difficulties and delays in obtaining copies of meaningful accounts or other documents of incorporation;

Involvement of countries where production of drugs or drug trafficking may be prevalent, or which have particular problems with organised crime, terrorism, corruption or fraud.

A client with no discernible reason for using the firm's service (e.g. clients with distant addresses who could find the same service nearer their home base, or clients whose requirements are not in the normal pattern of the firm's business and could be more easily serviced elsewhere)

An investor introduced by an overseas bank, affiliate or other investor, when both investor and introducer are based in countries where production of drugs or drug trafficking may be prevalent;

Dealing patterns

Transactions not in line with the investor's normal trading activity / Unusual activity compared to past transactions.

Buying and selling of an investment with no rationale purpose or in circumstances which appear unusual (e.g. churning at the client's request)

Usually trading in low-grade securities ie. "penny" stocks

Trades with no economic rationale or bona fide purpose

Doubtful sources of funds
Appears to be a case of insider trading”
Investment proceeds transferred to a third party
Transactions reflect likely market manipulations
Suspicious off market transactions
Use of different accounts by client alternatively
Sudden activity in dormant accounts
Activity inconsistent with what would be expected from declared business.
Account used for circular trading
Large number of accounts having a common account holder, introducer or authorized signatory with no rationale
Unexplained transfers between multiple accounts with no rationale

Abnormal transactions

Involvement of apparently unrelated third parties;
A number of transactions by the same counterparty in small amounts of the same investment and then sold one transaction, the proceeds being credited to an account different from the original account;
Any transaction in which the nature, size or frequency appears unusual (e.g. early termination of packaged products at a loss due to front end loading, or early cancellation, especially where cash had been tendered and/or the refund cheque is to a third party);
Transactions not in keeping with normal practice in the market to which they relate (e.g. with reference to market size and frequency, or at off-market prices);
Other transactions linked to the transaction in question which could be designed to disguise money and divert it into other forms or to other destinations or beneficiaries.
Value just under the reporting threshold amount in an apparent attempt to avoid reporting
Large sums being transferred from overseas for making payments
Inconsistent with the clients apparent financial standing
Inconsistency in the payment pattern by client
Block deal which is not at market price or prices appear to be artificially inflated/deflated.

Politically Exposed Persons (“PEPS”)

These types of person are essentially senior figures with significant political influence, their immediate family members and close associates. They often have control over government funds. Should you receive enquiries from one, or someone you suspect may be one, please contact the Principal Officer for further information as to the enhanced due diligence required in relation to such people.

Intermediaries

There are many clearly legitimate reasons for use of an intermediary. However, the use of intermediaries also introduces further parties into transactions thus increasing complexity and preserving anonymity. Any apparently unnecessary use of an intermediary should give rise to further enquiry.

Employees and agents

Changes in employee characteristics (e. g. lavish life styles or avoiding taking holidays);
Changes in employee or agent performance (e. g. salesman has a remarkable or unexpected increase in performance);
Any dealing with an agent where the identity of the ultimate beneficiary or counterparty is undisclosed, contrary to normal procedure for the type of business concerned.

Ongoing training to Employees / Hiring New Staff

1. Employee training under the leadership of the Principal Officer pertains to Importance of PMLA Act & its requirement.
2. Organizing suitable training programme wherever required for new staff, front-line staff etc.

Payment

A number of transactions by the same counterparty in small amounts of the same investment and then sold in one transaction;

Payment by way of third party cheque or money transfers where there is a variation between the account holder, the signatory and the prospective investor.

Delivery

Settlement to be made by way of bearer securities from outside a recognised clearing system;
Allotment letters for new issues in the name of persons other than the client.
Involvement of third parties for receipt / delivery of securities