



The AFSA's report on the outcome of its 2022 Anti-Money Laundering Thematic Review of Fintech Firms licensed in the AIFC

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Contents

I.	Executive summary	3
a.	Background	3
i.	The Questionnaire	3
ii.	Objectives.....	4
iii.	Scope	4
iv.	Types of firms.....	4
v.	Limitations	5
b.	Summary of findings	5
II.	Key highlights	6
a.	Observations	6
b.	Findings and recommendations	7
III.	Conclusion	9

I. Executive summary

a. Background

In 2022, the Astana Financial Services Authority (the "AFSA") conducted an anti-money laundering thematic review (the "Review") of the AIFC Fintech Firms licensed under the AFSA's Fintech Lab ("FTL") regime. The Review was aimed at assessing the consistency of FTL firms with the AIFC Anti-Money Laundering, Counter-Terrorist Financing and Sanctions Rules ("AIFC AML Rules"), the provisions of the 'Law of the Republic of Kazakhstan on counteracting legalisation (laundering) of proceeds obtained through criminal means and financing of terrorism' (the "AML Law"), and FATF Recommendations.

The Review was undertaken in two stages:

- I. Review of responses to the questionnaires seeking information on each FTL firm's AML framework supported by the documented evidence.
- II. Desk-based reviews, including the review of the documentation provided by each FTL firm.

This Report provides findings and observations based on the reviewed and analysed responses to the Questionnaire and the associated documentation to support AFSA's further evidence-based consideration. Throughout the Report, specific findings and observations are referred to that were common to the inspected firms but without listing the entire inventory of issues or breaches identified. Therefore, not all of the findings and observations noted in this Report may be relevant to all Relevant Persons. Please note that this is not a comprehensive guide to the AML/CFT framework. Rather, the users of this Report should consider their own circumstances to meet the relevant AML/CFT statutory and regulatory requirements.

i. The Questionnaire

The Questionnaire comprised 135 questions and 11 sections to assess the firms' key pillars of AML/CFT Programs and understanding of the AML/CFT risks.

The Questionnaire was circulated to 14 Fintech firms residing in the AFSA's FinTech Lab. However, only 10 responses are considered for the purpose of this Report due to a failure by the remaining four firms to respond in full which, in turn, reduced the AFSA's ability to get as wide a picture as to whether the firms were in compliance with the AIFC AML/CFT Rules and other related regulations. Therefore, the AFSA issued a restrictive notification to these firms indicating their inability to undergo the Review

and, as a result, imposing limitations on their business activity in the AIFC until they fulfill their obligations to facilitate the assessment.

To address the Review's findings and observations, and resolve the underlying issues, the inspected firms provided to the AFSA their corrective action plans that included specific, measurable, achievable targets and realistic deadlines that focus on the causes.

ii. Objectives

The objective of the Review was to identify the overall maturity level of AML Compliance Programs of FTL firms, their AML risk governance frameworks, AML hygiene practices and resilience measures.

iii. Scope

The AFSA undertook a gap analysis of the firms' existing regulatory compliance environment to assess their conformity to AIFC AML Rules, AML Law and relevant FATF Recommendations.

Also, the Review evaluated the firms' four pillars of an AML/CFT Compliance Program, being:

- 1) A system of internal policies, procedures, systems and controls (first line of defence);
- 2) A designated compliance function with a Compliance Officer/MLRO (second line of defence);
- 3) An ongoing employee training program; and
- 4) An independent audit function to test the overall effectiveness of the AML program (third line of defence).

iv. Types of firms

The Review included five types of business activities undertaken by the Fintech firms, as follows:

- 1) Crowdfunding;
- 2) Money services;
- 3) Crypto exchange;
- 4) Crypto brokerage; and
- 5) Managing investments

v. Limitations

The Review was conducted in the form of a limited-scope thematic review, which was limited only to the firms' AML/CFT compliance programs and their understanding of the AML/CFT risks involved with their business activities. Therefore, the Review did not cover analysis of the firms' threshold transaction reports (TTRs) and suspicious transaction reports (STRs). The AFSA's inspection team did not conduct a review of closed (or open) transaction monitoring or screening alerts to determine whether they were adequately reviewed and addressed with sufficient rationale and documentation. Accordingly, the review does not include an overview of firms compliance with their TTR / STR reporting obligations.

b. Summary of findings

Overall, the firms' AML/CFT compliance arrangements generally reflect the nature, scale and complexity of their businesses. However, some procedures reviewed fall short of clear description. Therefore, we instructed the firms to enhance their internal audit capacity to provide assurance testing or monitoring compliance and effectiveness of the AML policies, procedures, systems and controls.

The firms that had client operations (as at the review dates] provided evidence of their business and customer risk assessments. Also, the firms demonstrated their understanding that a weak risk assessment may impact their day-to-day operations, the level of customer due diligence applied, and their decisions about accepting or maintaining client relationships.

In some instances, however, the firms provided only qualitative statements, which were general in nature with no evidence that they were backed by available internal data to determine the inherent risk scores of clients. This increases subjectivity when risk scoring/rating the inherent money laundering risk exposure of a Relevant Person. Therefore, we recommended the firms to improve their risk-sensitive approach to mitigating and managing money laundering risks by stipulating more evidence-based assessment methodologies and/or risk-scoring models.

Some relevant AML policies reviewed did not stipulate a clear process for documenting decisions, such as a procedure for recording the rationale for not reporting activity as a result of the findings of any investigation.

As regards the procedure for PEP identification, the firms tended to over rely on the automated screening systems and commercial data bases.

The firms provided their AML/CFT-specific training programs that were generally of consistent quality and tailored to particular roles. However, not all firms ensured AML training for new employees and/or did not evidence the application of follow-up tests to AML training and maintenance of the attendance list requiring signing-off.

II. Key highlights

a. Observations

Overall, the inspected firms demonstrated a sufficient level of understanding of their inherent risk environment with adequate controls to address the exposure to ML/TF risks. The firms provided documented evidence of their efforts to manage and mitigate vulnerabilities related to their customer base, products, delivery channels and services offered (including proposed new services) and the jurisdictions within which they or their customers did business.

Some firms did not respond in full as required, or provided delayed responses to the Questionnaire, which resulted in less data than the AFSA would have liked on the overall design efficiency of the controls employed. In some instances, the reviewed documents lacked evidence of formal internal approval.

It was also observed that some firms simply restated the AIFC AML Rules and other regulations without tailoring them to their specific business activities and with no further provisions or verifiable information included to demonstrate how the relevant AIFC AML Rule and/or guidance were to be implemented in practice with regard to the financial services business undertaken.

In this regard, it should be re-iterated that the AFSA expects Relevant Persons to develop and implement policies, procedures, systems and controls, as well as governance oversight, which are tailored to the specific needs and risks of its business and to provide practical direction and guidance to staff to enable them to comply with applicable AIFC Rules and internal policies. Without this, decision-making about how to achieve compliance is subject to the unilateral judgment of the concerned employee, which typically leads to inconsistencies amongst employees, lack of alignment with management's expectations and a failure to comply with AIFC Rules and regulations.

b. Findings and recommendations

1. Some firms did not provide the supporting evidence of a formal appointment of the MLRO by the firm's relevant governing body and/or approval of the designated MLRO position. Along with this, we noted that a number of firms had not appointed a Deputy MLRO to fulfill the role of the MLRO in his or her absence or incapacity. Also, the AFSA urged firms to clearly spell-out in a relevant document a statement enabling a firm's MLRO to act on his/her own authority and to act independently in carrying out his/her responsibilities.
2. In a number of instances, it was noted that there poorly documented and maintained record keeping practices. Some firms were unable to demonstrate that their senior management had accepted the apportionment of responsibilities. Also, in certain cases, firms did not record the date of approval of their corporate documents and there was no approving body or person specified on the documents.
3. Generally, the firms understood their responsibilities and obligations under the outsourcing arrangements when one or more elements of their CDD (other than the ongoing CDD) are being delegated to a service provider (including within a Group) per AML Rule 9.2.1. However, we observed insufficient evidence of the appropriate due diligence in assuring themselves of the suitability of the service provider.
4. A few firms stated that their internal audit functions were carried out by the Compliance function. At this point, it should be noted that the AFSA expects a Relevant Person's internal audit function to remain independent from the responsibilities of management in order to maintain objectivity, authority, and credibility. A Relevant Person's compliance function is positioned to monitor on a continuous basis (as the second line of defence), whereas internal audit monitors compliance only on a periodic basis (as the third line of defence).
5. Despite having an established Compliance and Audit Committee, a number of firms did not evidence any supporting documentation describing the established committees, such as charters or terms of reference, minutes of their meetings, an authority matrix or other document setting out the roles, responsibilities and powers.
6. It is a Relevant Person's obligation to assess, manage and mitigate business and customer risks. However, a number of firms did not consider their inherent risk factors that impact their business for the purpose of formulating their AML compliance programs. Therefore, it is strongly encouraged that firms have a regularly

updated business-wide risk assessment in place which is used as a basis from which to design and update anti-money laundering controls. It was also noted that a weak risk assessment may impact the Company's day-to-day operations, the level of customer due diligence applied, as well as decisions about accepting or maintaining customer relationships.

7. In addition, it was noted that several firms lacked clear procedures to ensure accurate and timely monitoring, and ongoing review and update of the policies, procedures, systems and controls adopted by a Relevant Person under AIFC AML Rule 4.1.1. It is an internationally recognised practice in risk management to evaluate that controls are both designed appropriately and are operating effectively. Simply listing potential control measures that may, or may not, address the identified risks without testing whether or not they are effective, does not provide much value in determining whether such controls adequately address AML/CFT .

8. Although being appropriately applied in practice, some firms did not provide sufficient evidence of any communication procedure as regards informing the Board of directors (or a committee of the Board) and senior management of compliance initiatives, known compliance deficiencies, suspicious transaction reports filed, and corrective action taken.

9. A small number of firms failed to demonstrate a relevant procedure established to address internal referrals from employees regarding potentially suspicious activity.

10. In some instances, the firms were unable to clearly demonstrate their risk classification frameworks. The reviewed methodologies were not clear, and the risk scoring models were difficult to comprehend.

11. It was recommended that some firms improve their controls and monitoring systems for the timely detection and reporting of potentially suspicious activity and large transaction reporting.

12. As a common finding, the firms' relevant policies or procedures did not clearly stipulate a process for documenting decisions and recording the rationale for not reporting activity as a result of the findings of any investigation.

13. Having actively employed automated systems, some firms did not apply additional verification via other available sources. In addition, the firms were unable to demonstrate a procedure for monitoring open-source information in media regarding clients (i.e., "non-documentary" verification procedures).

14. As regards identification of PEPs and their close associates, firms tended to over rely on their automated screening systems. This approach fails to take into account that such systems may not be able to identify similar or variant spellings of names, digit rotation, character manipulation or name reversal, etc. Also, the specialist databases deployed may not be calibrated to spot those individuals who fall under the PEP category in its wider definition (such as close family members). In addition, it is not good practice to consider a customer as being not a PEP simply because his/her name does not appear on a database search.

15. Further, it is recommended that firms consider what mixture of manual and automated screening is most appropriate in ensuring quality control checks over both methods. It is an internationally recognised practice in risk management to test that the proposed controls are both designed appropriately and operating effectively. The business and the compliance function may establish risk-based quality assurance reviews and monitoring and testing activities to ensure the functions are being performed appropriately. This may include a review of the CDD collected to ensure completeness, monitoring reports of CDD completeness to ensure the procedures and systems are working as expected and performing tests to assess whether the monitoring and the business performance are satisfactorily measuring and ensuring compliance.

III. Conclusion

The AFSA firmly maintains that a firm's compliance culture, governance and risk awareness are crucial in having a the robust AML regime. A firm's strong "tone from the top" is expected to ensure that AML is a top priority of the organisation. The AFSA has a zero tolerance for money laundering and, therefore, encourages the Relevant Persons' senior management to demonstrate high standards of compliance with their AML obligations by exercising due skill, care and diligence.

The AFSA also expects that Authorised Person deal with the AFSA in an open and co-operative manner, genuinely displaying the commitment to adhere to the AFSA's values and standards regarding the prevention and mitigation of money laundering, terrorist financing and other existing risks of financial crimes.

The AIFC AML Rules set minimum standards for the Relevant Person's conduct. Therefore, the AFSA expects Relevant Persons to develop and implement policies, procedures, systems and controls, and governance oversight, which is tailored to the specific needs of their business and to provide practical direction and guidance to

staff to enable them to comply with applicable AIFC Rules and internal policies. As previously mentioned, without this, decision-making about how to achieve compliance is subject to the unilateral judgment of the concerned employee, which may create inconsistencies amongst employees, lack of alignment with management's expectations and failures to comply with AIFC Rules and regulations.

The AFSA will continue to monitor Relevant Persons' AML frameworks and practices following a risk-based approach and in engaging with firms directly on an entity-level where necessary.