

General Cashier Directorate
Circular 279, 14 February 2012

GUIDE TO CONTROLS ON CASH HANDLERS

PREMISE

This Guide sets out the procedures for controls on cash handlers, i.e. persons that check the authenticity and fitness of euro banknotes in order to detect possible counterfeits and notes too worn for continued circulation.

The Bank of Italy, by order of the Governor dated 14 February 2012, has issued Provisions on Cash Handling Activities, in which the sources of law, definitions and rules governing this activity are specified.

The administrative procedures indicated in the Guide are subject to the provisions of Law 241/1990 as amended and of the Bank of Italy Regulation of 22 June 2010, which specifies the time limits and the organizational units responsible for the administrative procedures within the powers of the Bank of Italy pursuant to Articles 2 and 4 of Law 241/1990 (hereinafter, the “Regulation”).

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CHAPTER I – AUTHORIZATION FOR MANUAL AUTHENTICITY AND FITNESS CHECKING

1. Premise

This Chapter governs the procedure for examining applications submitted:

- by credit institutions and Poste Italiane S.p.A. for authorization to perform manual fitness checks at “remote branches” (Article 7.1 of Decision ECB/2010/14 and Part I, Chapter I, of the Bank of Italy Provisions on Cash Handling Activities);
- by credit institutions and Poste Italiane S.p.A. for authorization to perform manual authenticity and fitness checks in exceptional and temporary circumstances that significantly impair the supply of banknotes to the public (Article 7.2 of Decision ECB/2010/14 and Part I, Chapter I, of the Bank of Italy Provisions on Cash Handling Activities).

The Head of General Cashier is responsible for the procedure.

2. Start of the procedure

When the application is received the Bank verifies its correctness and completeness. Where the application is correct and complete, the Bank notifies the start of the administrative procedure to the applicant, the persons who by law must intervene, and third parties with an opposing interest.

The notification must be sent – by certified email or registered letter with advice of receipt – as soon as possible and in any case before one third of the time limit set for the conclusion of the procedure has elapsed. It must specify: i) the date on which the application was received; ii) the organizational unit responsible for the procedure; iii) the person responsible for the procedure and the time limit for its conclusion; iv) a statement that the applicant may have access to the acts of the procedure; v) the deadline (no later than half the time limit set for adoption of the measure) for presentation at the parties’ initiative of briefs and documents; vi) possible remedies in case of failure to issue the provision.¹

If the application is not correct or is incomplete, the applicant must be so informed within a time limit equal to half of that set for the conclusion of the entire procedure, with indication of the points of incorrectness or incompleteness and specification that the time limit for the conclusion of the procedure begins from the date of reception of the amended application.

An applicant’s presentation, in the course of the procedure, of new documents or information such as to modify essential elements of the application (Regulation, Article 2.4) is equivalent to a new application, and entails that the time limit for conclusion of the procedure begins from the date of reception of such documents or information.

3. The examination phase

3.1. Calculation of time limits

¹ Under Article 31 of the Code of Administrative Procedure introduced by Legislative Decree 104/2010, “once the time limit for the conclusion of the procedure has elapsed, interested parties may request ascertainment of the administration’s obligation to act.”

The provision must be issued within the time limit set in the Regulation, taking account of any period of suspension consequent to requests for additional information. For purposes of calculating the time limit:

- a) the time limit begins from the day of reception of the complete or corrected application (Regulation, Article 2.1);
- b) the day on which the final time limit for the procedure lapses is calculated; accordingly, the day coinciding with the final time limit can serve for the adoption of the authorization or the notification of rejection of the application.

3.2. Request for additional information

When in the course of the examination it becomes necessary to obtain additional information or certifications, a formal request to this effect must be made to the applicant. The letter of request must specify that the request suspends the time limit set for the procedure, which will begin to elapse again from the date of reception of the additional information requested. There can be only one suspension during a procedure, and it cannot last more than 180 days (Regulation, Article 10.6) from the date of the request for additional information.

When it is necessary to supplement the examination by inspection, the time limit for the procedure may be suspended under the Regulation, Article 10.5. The time limit begins to elapse again on the date the Governor approves the inspection report. The suspension cannot be for longer than 180 days (Regulation, Article 10.6).

3.3 Criteria for evaluating the application

The examination serves to verify:

- in the case of applications for authorization for “remote branches”:
 - that the branch, owing to its location and the characteristics of the transport infrastructures that serve it, is not easily reachable for constant and continuous supply of banknotes;
 - that the volume of transactions with the public at the branch is modest;
 - that the volume of euro banknotes dispensed by automatic cash dispensers at all the remote branches authorized by the Bank of Italy to perform manual authenticity and fitness checks does not exceed 5 per cent of the total dispensed nationwide by such dispensers;
 - that the branch is equipped with compliant machines for authenticity checking.
- in the case of authorization applications in connection with “exceptional and temporary circumstances”:
 - the extraordinary nature of the event;
 - the possible harm to the circulation of banknotes, taking account among other things of the size and importance of the parts of the national territory that would be cut off from the supply of cash.

4. Conclusion of the procedure

4.1. Acceptance of the application

When the outcome of the examination is positive, the procedure concludes with the issue of the authorization measure, the operative part of which will state that the conditions for authorization laid down in the regulations are satisfied.

The measure is accompanied by a note on the examination which:

- a) summarizes the time limits for the application and the relevant legislation;
- b) describes the findings of the examination for ascertainment of satisfaction of the conditions required by said legislation;
- c) sets out the proposal for acceptance.

The authorization measure is issued by the Governing Board under the Statute of the Bank of Italy.

The authorization contains, inter alia: i) any information obligations consequent to the adoption of the measure; ii) mention of the revocability of the authorization if the conditions under which it was granted should change; iii) the expiry date of the authorization in the case of an authorization measure in connection with “exceptional and temporary circumstances.”

The measure is notified to the applicant by the same means as the initial notification, i.e. certified email or registered letter with advice of receipt.

4.2. Revocability of the authorization

In the event of change in the conditions under which the authorization was granted, the measure may be revoked.

Revocation means that the authorization measure no longer produces its effects.

The revocation decision must be notified promptly to the applicant by certified email or by registered letter with advice of receipt, with advance notice via fax; both the advice of receipt and the fax transmission receipt are to be conserved.

4.3. Notification of impediments under Law 241/1990, Article 10-bis

If in the course of the examination it is found that the requisites for authorization are lacking, the person responsible for the procedure communicates these impediments to the application to the applicant. The decision is made by the Governing Board pursuant to the Statute of the Bank of Italy.

The law, although it does not set a deadline, establishes that the administrative authority must communicate the impediments promptly. Accordingly the findings of the examination should be submitted to the higher levels in the chain of command far enough in advance of the time limit for the procedure.

The notification – to be accompanied by a note on the examination – must be drafted with the greatest of care. It is necessary to specify the de facto elements and regulatory provisions that impede acceptance of the application.

The notification must be transmitted promptly via certified email or registered letter with advice of receipt, with advance notice via fax. The notification of the impediments to the applicant suspends the time limit for conclusion of the administrative procedure.

Within ten days from the reception of the notification the applicant may submit its observations in writing, possibly accompanied by documents. The time limit for conclusion of the procedure resumes elapsing from the date of presentation of the applicant's observations or, in their absence, the date on which the time limit for their submission lapses.

The decision is made by the Governing Board pursuant to the Statute of the Bank of Italy.

4.4. Rejection of the application

Where the examination as a whole brings out elements which – even after taking into consideration any observations transmitted following the notification of the impediments – make it advisable not to accept the application, a rejection measure will be adopted.

The rejection measure must be properly motivated, taking account among other things of the notification of the impediments, and must specify the legislative provisions and facts on which the rejection is based.

The measure is accompanied by a note on the examination which: i) summarizes the time limits of the application; ii) describes the findings of the examination as regards the ascertainment of the lack of the conditions required by the legislation; iii) formulates the proposal for rejection.

The rejection measure is taken by the Governing Board under the Statute of the Bank of Italy.

The measure shall be notified to the applicant within the time limit for conclusion of the procedure and by the same means as the initial notification, i.e. certified email or registered letter with advice of receipt, with advance notice via fax.

* * *

In exceptional circumstance the Bank may proceed also at its own initiative to issue authorization for manual cash handling.

CHAPTER II – INSPECTIONS

1. Premise

In its controls on cash handlers the Bank of Italy may order inspections.

The inspections are directed to analysis and assessment of the organizational and operational arrangements whereby the cash handlers process banknotes, in order, among other things, where necessary, to require prompt corrective action or else to prohibit the recirculation of the banknotes.

In particular, this involves:

- verification of the procedures and controls for checking the authenticity and fitness of banknotes;
- controls on the machines for authentication and sorting of banknotes, with special reference to the ability to check authenticity and fitness and to trace suspected counterfeits to the person who deposited them;
- verification of reliability of the data and information communicated to the Bank of Italy.

In order to curb the costs for cash handlers, inspections will be carried out according to the principle of proportionality, i.e. the graduation of controls as a function of the characteristics, size and complexity of the institutions inspected. Accordingly:

- as a rule the primary subjects of inspections are cash handlers that recirculate banknotes by means of automatic machines for authenticity and fitness checking;
- the inspector will adapt the course of the inspection as set out in the Methodological Guide (section 11) to the operational complexity of the cash handler and the severity of the problems, adjusting the depth of analysis accordingly.

Inspections at banks, electronic money institutions, payment institutions and Poste Italiane S.p.A. units that engage in cash handling are carried out in close coordination with the Banking Supervision Inspectorate.

For controls on cash handlers subject to inspection by the Finance Police pursuant to Article 53.2 of Legislative Decree Legislative Decree 231/2007 as amended, the Bank of Italy can avail itself of the cooperation of the Finance Police, as provided by Article 8.7 of Decree Law 350/2001, as replaced by Article 97.1 of Decree Law 1/2012.

2. Types of inspection

Inspections may regard the cash handler's entire recirculation operation ("broad spectrum" inspections) or single segments ("targeted" inspections). They may also be ordered to check on the implementation of initiatives of the cash handler or called for by the Bank of Italy ("follow-up" inspections).

3. Planning of inspections

The frequency and type of inspections are established according to the size of cash handlers and the severity of their problems. As a rule inspections are ordered according to a yearly plan. Inspections

not provided for in the plan are carried out when especially problematic situations arise that so require.

(...*omissis*...)

4. Letter of appointment

Inspections are carried out by employees of the Bank of Italy. They are ordered by means of a letter of appointment signed by the Governor or his representative. (...*omissis*...)

5. The inspection team

As a rule inspections are entrusted to at least two employees (the “inspection team”); the letter of appointment designates the team leader.

(...*omissis*...)

6. Start of the inspection

As a rule inspections are conducted at the head office of a business and/or at the units where banknotes are handled. (...*omissis*...)

7. Procedures and criteria for inspections

In order for inspections to realize their full information potential, in their activity the inspectors must hold to standards of:

- flexibility, defined as the scope of technical discretion within which the inspector makes the choices that best serve the purposes of the examination (e.g. documents to consult, persons to contact);
- objectivity, to guarantee the validity of any criticisms raised and uniformity of behaviour. In practical application of the principle of objectivity, facts should be distinguished from evaluations. Facts should be weighed in the light of the legislative framework, the operations of the cash handler, and the context found by the inspection. In evaluations, which are intrinsically subjective, the need is to minimize the risk of inconsistency of judgment, which is typically greater in the appreciation of qualitative phenomena. The Guide (section 11) is designed to mitigate this risk by providing for a standard course of analysis and indicating the elements of evaluation underlying each level of judgment. Where the reality differs from the Guide’s presumptions, the inspector should take care to adapt the analytical criteria to the concrete case;
- transparency vis-à-vis the cash handler and dialogue with its corporate representatives. This permits critical verification of the hypotheses made in the course of the inspection and the addition of new elements of knowledge not yet considered. The dialogue, to be conducted in observance of the participants’ respective roles and without disclosing any provisional assessments, will give the cash handler a better understanding of the criticisms and observations and so favour the preparation of corrective measures;

- containment of cash handlers' costs. The inspection should impose no unnecessary burden on the cash handler. Specifically, in selecting inspection methods (request for documentation, meetings), among equally effective tools the inspectors should choose those that impose lower costs on the cash handler;
- confidentiality and prudence are rules of conduct implicit in the delicate nature of the inspection function.

(...*omissis*...)

8. Termination of the inspection report

(...*omissis*...)

9. The inspection report

9.1. *Structure and content*

The findings of the inspection are to be set out in a report organized as follows:

I) “Criticisms and observations”: This part gives the overall outcome of the inspection and the problems that are to be brought to the attention of the cash handler. In particular, the “criticisms” are problems relating to non-compliance with law and regulations or to dysfunctions and shortcomings that affect the effectiveness and efficiency of cash handling activities and that therefore require prompt correction. “Observations” relate to operational areas that could evolve adversely or that in any case need improvement with a view to preventing dysfunctions in the banknote handling process.

II) “Confidential matters” (...*omissis*...)

9.2. *Criteria for drafting*

The inspection report must be an instrument of information that is readily usable both by the inspected cash handler (which must initiate measures to eliminate the shortcomings set out in the criticisms and observations) and by the General Cashier Directorate (which must weigh possible corrective measures and must in any case monitor the solutions planned by the cash handler).
(...*omissis*...)

9.3. *Security*

The inspection report is a document that is formed progressively. Although the working drafts cannot be classified according to the report's formal degree of confidentiality, they may contain significant information and provisional assessments that must nevertheless be kept confidential. The members of the inspection team must be especially careful in the phase of drafting and safe-keeping custody of these drafts, with adequate IT safeguards. Analogous precautions must be adopted for documentation acquired from the cash handler in the course of the inspection.

10. Post-inspection obligations

10.1. Revision of the report

The inspection team leader writes a draft inspection report, ordinarily by the end of the inspection; the draft is revised by one or more persons appointed by the General Cashier Directorate.

The revision of the draft – carried out together with the inspection leader and possibly also other members of the team – serves to provide a critique of the clarity and technical relevance of the criticisms and observations made, the completeness of information and assessments, and the text's conformity with quality standards for drafting.

10.2. Subsequent phases

(...*omissis*...)

10.3. Delivery of the report

The “Criticisms and observations” are to be delivered to the cash handler by registered letter with advice of receipt or else at a special meeting, ordinarily convened on the cash handler's premises. In the latter case they are delivered by the inspection team leader (or in case of impediment by his or her alternate) in the presence of the cash handler's legal representative pro tempore; as a rule the Head of the General Cashier or a delegate is present.

The inspector sets forth the criticisms raised and provides, where requested, clarifications on the matters subjected to criticisms.

Afterwards the inspector and, on behalf of the cash handler, the legal representative pro tempore initial the pages of the two copies of the “Criticisms and observations” (and annexes), and draft the minutes of delivery, with clear indication of the names of the persons present. The last page of the report is reserved for any observations that officers of the cash handler may wish to make concerning the findings of the inspection.

One copy of the report is delivered to the cash handler and the other kept by the General Cashier Directorate.

If it has been decided to initiate an administrative sanction procedure, the notification of the letter of charges to the cash handler is proceeded with.

11. Methodological guide

Inspections are conducted along the analytical paths traced out below. Cash handlers are far from being a homogeneous group. Alongside banks and Poste Italiane, there may be other intermediaries (electronic money institutions and payment institutions) as well as non-financial entities, the most important of which are companies whose core business is banknote processing (so-called service companies). Each of these categories may be further differentiated according to legal status and volume of business. It is up to the inspector to apply the proportionality principle in practice by appropriately adapting controls to the path of inquiry and depth of analysis to the reality of the entity inspected. In any case, the inspection must be capable of assessing the cash handler's overall ability to avert the risk of putting worn or counterfeit notes back into circulation.

For cash handlers authorized for the transport and custody of valuables, the scope of the inspection does not extend to assessment of vehicles, modalities and procedures for funds transport. Any areas of concern noticed incidentally by the inspector outside the subject of the inspection can be mentioned in the “confidential matters” section of the inspection report for possible transmission to the competent authorities.

11.1. Organization and operations

The inspector, taking account of the legal status and overall operations of the cash handler, will inform himself as to its board of directors, management and control bodies and the lines of command relevant to banknote handling.²

For this purpose the inspector will use the company organization chart or equivalent documents, plus meetings with corporate officers.

The inspector will assess the degree of formalization of lines of command and judge whether the arrangements in place are such as to prevent uncertainties over tasks and responsibilities.

At this stage, minutes of the recent meetings of the company’s governing bodies on matters of cash handling can provide useful information for understanding the overall framework of operations and orienting subsequent analysis (for example, if the minutes reveal specific problems with the activities being inspected).

Organization consistent with the operational context is important to maintain effectiveness and efficiency over time. Inspections serve to assess the efficacy of organizational solutions and also to evaluate the effects of any discrepancy between formal model and practice. The inspection will cover all the structures, handling systems and technological and human resources used in banknote handling; the examination of the rules governing company processes will be accompanied by checks on their implementation. The analysis will cover the following areas:

- production processes and control system;
- functionality of the machinery for authenticity checking and sorting;
- human resources;
- the administrative and accounting system;
- statistical reporting.

11.1.1. Production processes and control system

The inspector checks that the cash handler has mapped the relevant production processes and, for each, specified the procedures.

At this stage the inspectors examine the internal provisions and evaluate their functionality, completeness, how widely and well known they are among the staff, and the way in which they are complied with in concrete operations. To do so, the various steps in the production process will be reviewed. If operational practices inconsistent with the internal regulations are discovered, the inspectors must determine whether the divergence is due to an inadequate disciplinary framework (which must accordingly be revised) or involves factors that threaten the proper management of cash handling.

Where some production phases are outsourced, the analysis begins with the outsourcing contracts, which must comply with the dictates of the Bank of Italy. Next, it must be verified that the contracts

² For cash handlers already subject to the Bank of Italy’s supervision, this information is acquired in the pre-inspection phase from the relevant Directorates of the Bank’s Head Office or at the competent branch. For other cash handlers, prior to the inspection the documentation held at the General Cashier Directorate is consulted.

are properly executed. Special attention will be paid to assessing how effectively the inspected cash handler verifies compliance with the agreed levels of service.

In analyzing the control system, the inspector will make sure that controls are specified in appropriate guidelines and that the organization and procedures in place ensure effective control over the phases of banknote handling. In particular, the traceability of all banknote movements and of the actions of staff must be verified, as well as the safeguards adopted to preclude the possibility that the so-called service companies, in handling cash, could mix together banknotes from different handlers or replace the denominations of the notes delivered by each.

The performance of the control system is assessed by analyzing the capacity and speed with which shortcomings or inadequacies are detected and trigger corrective action.

11.1.2. Functionality of machinery for authenticity checking and sorting

The central feature of inspection of production processes is assessment of the cash handler's ability to prevent counterfeit or unfit notes from being put back in circulation. This can happen:

- a) where the handler recirculates notes without having them checked by "compliant machines" or, in the cases where manual controls are allowed, "trained staff";
- b) where authenticity and fitness checks are unreliable owing to malfunctioning of the "compliant machines" utilized or the inadequacy of the staff that carry out manual controls.

The analysis requires specific examination of the type and function of the technological resources that the cash handler uses.

Before beginning the examination, the inspector obtains from the General Cashier Directorate the list of machines transmitted by the cash handler. Machines are qualified as "compliant" when they have the same trade name and are equipped with the same software version (ordinarily visible on the machine itself) as those published on the site of the European Central Bank.

The inspection must verify that authenticity and fitness checking is carried out exclusively by "compliant machines" listed by the European Central Bank and that this equipment corresponds to the list transmitted by the cash handler to the Bank of Italy.

(...omissis...)

After verifying that the list of machines used has been transmitted to the Bank of Italy, the inspector examines the supply contracts, making sure that they contain:

- the supplier's attestation that the installation and operation of the machines comply with the standards laid down by a national central bank of the Eurosystem;
- the supplier's undertaking to control for continuing compliance with these requirements as part of ordinary maintenance;
- the supplier's undertaking to make prompt notification of any changes to software or the deletion of machines from the list published on the website of the ECB.

Subsequently the proper functioning of the "compliant machines" is checked, to make sure that they provide the same guarantee of security and reliability in ordinary operation as in the tests for entry and continued inclusion in the list of "compliant" machines.

To this end the inspector first checks that the version of the software installed on the machine corresponds to that indicated on the ECB website and that the machine operators know how it

works, know the procedures to follow in case of detection of suspected counterfeits or anomalies in the functioning of the machinery and are fully aware of the risks connected with malfunction.

The inspector will subject the “compliant machines” to the following tests:

a) test for detection of possible counterfeits, performed on a sample of counterfeits supplied by the General Cashier Directorate, to be sorted along with the cash handler’s own authentic notes.

For every denomination of the sample counterfeits, at least ten authentic notes must be included in the set of notes for sorting.

The sample notes are to be fed into the sorting machines as a group, and facing in every possible direction.

The machine passes the test when it detects the counterfeits in each of the various directions in which the note may face.

(...*omissis*...)

b) test for separation of fit and worn banknotes

(...*omissis*...)

11.1.3. Human resources

Human resources are a critical factor in cash handling. In a highly automated production environment, staff members are called on to verify the performance of the “compliant machines” by monitoring their output. Further, given the peculiarity of the product, they must guarantee high levels of security in all phases of banknote handling.

The inspector will examine the methods of staff training and the way in which staff are informed of the provisions governing work processes, with specific reference to those relevant to fitness and authenticity checking. Based among other things on interviews with workers, the inspector also assesses their knowledge of the aforesaid provisions and evaluates the extent to which the operational environment is control- and security-conscious.

Where the cash handler is authorized to perform manual controls, the inspector will evaluate the way in which permanent training of the relevant staff is conducted.

11.1.4. Administrative and accounting system

The cash handler’s administrative and accounting system must permit timely and reliable registration of the banknotes handled, subdividing them, for each depositor, into notes acquired and notes being processed and, when the processing is concluded, distinguishing between suspected counterfeits, worn notes, and notes fit for recirculation. Account must also be made, again separately for each depositor, of the outward movement consisting of the shipment to the Bank of Italy of the suspected counterfeits and worn notes and the recirculation of the fit notes. This accounting, which can be likened to “warehouse” accounting, must match the accounts with each depositor.

The inspection analysis must assess whether the system has suitable safeguards for the confidentiality, integrity and availability of the data. In particular, an assessment will be made of the

provisions adopted for identifying the persons authorized to make accounting entries and to keep a record of the transactions effected by each.

Where a bank or Poste Italiane S.p.A. is authorized to perform manual controls at a remote branch, the accounting system must record the volume of banknotes recirculated by that process.

Once the structural features of the administrative and accounting system have been observed, the inspector verifies the correct performance of the accounting process and its reliability (the quality and consistency of entries and controls), retracing, for a sample, the entire accounting entry cycle.

11.1.5. Statistical reports

The inspection assesses the statistical reports production process, an assessment that is closely connected with the analysis of the administrative and accounting system.

The reliability of reports presupposes that the cash handling cycles are registered correctly and in a timely manner. Dysfunctions of the administrative and accounting system inevitably have repercussions on the quality of the reports.

The inspector will examine a sample of reports in order to verify:

- that the data reported are the same as those found in the company accounts;
- that the data are accurate and complete;
- that any rectifications are timely;
- that data are transmitted on time.

This verification will be more extensive and more detailed where the administrative and accounting framework is less reliable or where the reporting process is marked by management and control shortcomings.

CHAPTER III – CORRECTIVE MEASURES

1. Premise

In cases of non-compliance with the provisions governing the activity of cash handlers, the Bank of Italy is empowered to require cash handlers to adopt corrective measures.

The evidence of non-compliance may result both from inspections and from other information in the Bank of Italy's possession, e.g. information from cash handlers' periodic reports.

The type of measure will be decided according to the seriousness of the problems and the need for prompt action, and will be commensurate with the risk of recirculation of banknotes lacking the requisites of authenticity and fitness.³

Where there is a high risk of recirculation of banknotes lacking the requisites of authenticity and fitness, the request for corrective measures may be accompanied by an order, adopted under the provisions governing administrative procedures, prohibiting the recirculation of banknotes.

In the event of malfunctioning of banknote handling machines, the prohibition, which may apply to a single machine or to multiple machines, is part of the procedure established by the ECB for eliminating the malfunction and for the possible deletion of the machine from the list of those compliant with the ECB's standards.

2. Request for corrective measures

Requests for corrective measures take the form of a notification from the General Cashier Directorate to the cash handler, containing a warning or a request for elimination of irregularities.

The manner in which the notification is drawn up has an important bearing on making the intervention legally effective: the problematic aspects are described in the preamble to the operative part, which must indicate the steps that need to be taken to keep problems from arising, eliminate anomalies and avoid further worsening.

Similar drafting procedures are also to be followed, for reasons of legal effectiveness of the intervention, when it is decided to send the cash handler a simple letter containing suggestions or recommendations or both.

Where the necessity of a corrective intervention derives from the findings of an inspection, the procedure set out below is followed.

The intervention usually takes the form of a post-inspection letter. It is drawn up following assessment of the responses to inspectors' critical observations, so as to determine the cash handler's awareness of the problems and verify its ability to frame valid countermeasures. The letter draws on information contained in the inspection report, possibly supplemented by more recent information that may be available.

The post-inspection letter:

- summarizes the problems ascertained during the inspection;
- summarizes the contents of the company's responses and the Bank of Italy's assessments regarding the adequacy of the initiatives completed or under way and the appropriateness of

³ In case of non-compliance with the provisions governing the activity of cash handlers, in the request for corrective measures the positions adopted at Eurosystem level are also taken into account.

the timeframe proposed for their realization. In addition, it highlights any omissions or shortcomings in the company's responses and requests the necessary supplementary actions;

- indicates the critical areas calling for remedial action;
- sets the time limits for reports to the Bank of Italy on the state of implementation of the measures and the results achieved.

When the inspection finds evidence of particularly acute problems, the post-inspection letter, normally delivered at the same time as the dossier of "Criticisms and observations", serves to prompt the company's managers to move quickly to overcome the shortcomings detected; depending on the nature and scale of these, the cash handler may be asked to draw up an action plan, for submission to the Bank of Italy, setting out the concrete steps to be taken and their schedule.

(... *omissis* ...)

Where the situation found by the inspection entails a high risk of recirculation of counterfeit or unfit banknotes, it may be necessary to initiate the procedure for a measure prohibiting recirculation.

3. Prohibition of banknote recirculation

The prohibition of banknote recirculation will be considered:

- on an ordinary basis in the presence of:
 - a) situations where there is a high risk (e.g. owing to severe organizational problems) of recirculation of suspected counterfeit or unfit banknotes;
 - b) repeated serious violations of the obligations laid down by legislation and regulations on cash handling;
- as a matter of urgency when the monitoring tests conducted during an inspection of the banknote handling machines used by the cash handler have negative outcome. In such cases, the prohibition may be imposed for all or only for some banknote denominations. If the cash handler has multiple machines, the prohibition may apply only to those for which the monitoring test results were negative.

The person responsible for the procedure is the Head of the General Cashier. The measure is to be adopted by the Governing Board in accordance with the Statute of the Bank of Italy.

(... *omissis* ...)

Notification of the start of the procedure need not be made in order to adopt a prohibition measure as a matter of urgency during an inspection in case of negative results of the monitoring tests of banknote handling machines.

The right to adopt the prohibition measure on a precautionary basis in the case set out at a) and b) even before notifying the start of the procedure, pursuant to Article 7.2 of Law 241/1990 as amended, stands unaffected. The precautionary prohibition is to be adopted by the Governing Board.

(... *omissis* ...)

4. Subsequent checks

The General Cashier Directorate will check that a cash handler to which corrective measures have been addressed carries out the initiatives to eliminate the deficiencies and shortcomings detected during controls. To this end, the General Cashier Directorate may also order follow-up inspections.

CHAPTER IV – SANCTION PROCEDURE

To apply the pecuniary administrative sanctions provided for in Chapter VI of the Provisions on Cash Handling Activities, the procedure indicated below will be followed.

The Head of General Cashier is responsible for the procedure.

1. Start of the sanction procedure

To initiate the sanction procedure, the irregularities or instances of non-compliance by cash handlers with the provisions governing the sector found in the course of inspections or by means of other controls are submitted for assessment to the Advisory Group on Cash Handler Irregularities.

The Group is convened, at the suggestion of its chairman, by the Banknote Quality and Counterfeits Division of the General Cashier Directorate.

The following are members of the Group:

- the Head of the General Cashier or another designated staff member, in the capacity of chairman;
- a representative of the Licensing and Resolution Directorate of the Directorate General for Financial Supervision and Regulation;
- a lawyer of the Legal Services Directorate, for legal assistance.

The Group is supplemented by:

- a) the inspection team leader and the revisers of the report, for examination of the irregularities or instances of non-compliance found during the inspection;
- b) the Financial Supervision and Regulation Directorates and the Bank of Italy branch manager, according to their supervisory tasks, if the irregularity concerns supervised persons.

As a rule, branch representatives participate in meetings by teleconference.

Taking account of specific needs for information or expertise in relation to the nature of the case to be examined, representatives of other functions or operating units may participate in the Group.

The functions of secretariat are performed by the Banknote Quality and Counterfeits Division.

In assessing irregularities, the Group will also take into account the approach decided at Eurosystem level for the application of administrative sanctions for non-compliance with Decision ECB 2010/14.

At the completion of the examination, the Group may propose:

- a) a supplemental inquiry;
- b) the start of the administrative sanction procedure;
- c) not to order the start of the sanction procedure. Where the circumstances warrant it, the Group may propose that the cash handler nevertheless be issued a warning.

The Group's conclusions, formally recorded in the minutes, are to be submitted to the Head of the General Cashier for approval.

The General Cashier Directorate identifies those irregularities which, because of their nature or their relatively low degree of technical and legal complexity, do not have to undergo collegial examination by the Group for the initiation of the sanction procedure.

In such cases the Head of the General Cashier, on the basis of an overall assessment of the available data and information and of the approach decided at Eurosystem level, may:

- a) order the start of the sanction procedure; or
- b) decide not to take further initiatives. Where the circumstances warrant it, he may nevertheless order that the cash handler be issued a warning.

The General Cashier Directorate submits the notification of charges of irregularities for the start of the sanction procedure for the approval of the Director General for Currency Circulation, together with a summary of the inspection findings and an analytical note on the irregularities detected.

For violations found during inspections, the time limit for notifying the start of the sanction procedure elapses from the conclusion of the on-site controls (completion of the verification of irregularities). For irregularities not detected during inspections, approval by the Director General completes the verification.⁴

The possibility of issuing a measure prohibiting banknote recirculation together with the start of a sanction procedure against a cash handler will be unaffected.

The notification of charges⁵ is to be sent to cash handlers having their registered or administrative office in Italy within ninety days and to those having their registered office abroad within three hundred and sixty days of verification. In the case of irregularities detected during an inspection, the notification will be made when the inspection report is sent.

The counter-arguments and any requests for hearing, including requests for an extension, on the part of the company or entity concerned must be presented to the General Cashier Directorate within thirty days from the notification of charges.

2. The examination

The General Cashier Directorate, the organizational unit responsible for the procedure, handles the formalities for the examination phase of the procedure.

The General Cashier Directorate submits the documentation to the Commission on Cash Handler Irregularities, which evaluates the cases for which administrative sanctions are applicable, examining the records of the procedure.

The Commission is chaired by the Director General for Currency Circulation; the Heads of the General Cashier, the Banknotes and the Licensing and Resolution are members.

The Commission is supplemented by the Directorates' Heads in the Directorate General for Financial Supervision and Regulation and by the Bank of Italy branch manager, according to their supervisory tasks, if the irregularity concerns supervised persons.

The Commission, after evaluating the irregularities found, the counter-arguments, the minutes of any hearings and every other element of inquiry, concludes its examination by proposing the imposition of sanctions or the closure of the sanction procedure. In evaluating irregularities, the Commission takes into account the specific corrective measures adopted vis-à-vis the cash handler under the provisions in force and the approach decided at Eurosystem level for the application of administrative sanctions in case of non-compliance with Decision ECB/2010/14.

⁴ The approval of the Director General is affixed to the note accompanying the notification of charges.

⁵ The notification of charges must indicate, among other items, the organizational unit responsible for the sanction procedure, to which the counter-arguments and records of the procedure are to be sent, including any requests for extension, access or personal hearing. The notification of charges must also indicate the organizational unit where the documents of the examination may be viewed.

At the conclusion of the examination, the proposal for the application of administrative sanctions or for the closure of the procedure, signed by the Director General for Currency Circulation, is transmitted together with the records of the procedure to the Governing Board.

The Bank's General Counsel or, in case of absence or impediment, the Head of Legal Services gives the Governing Board an opinion on the legitimacy of the proposal.

(... *omissis* ...)

3. The decision

The decision to impose sanctions or to close the procedure is taken by the Governing Board in accordance with the Statute of the Bank of Italy.

The Governing Board may request supplementary examination; it may also depart from the results of the examination, indicating the grounds for this in the final measure.

CHAPTER V – REFERENCES TO OTHER AUTHORITIES

Where the controls performed on cash handlers turn up evidence which might be of interest to other authorities in relation to the tasks assigned to them by law (for example: the Ministry of the Interior in the case of cash handlers holding an authorization issued under Article 134 of the Consolidated Law on Public Security; the Financial Intelligence Unit (FIU) for the fight against money laundering and terrorist financing) or which could have implications under criminal law, the procedures set out below will be followed.

1. Notification of the judicial authorities

In cases having potential implications under criminal law, the Head of the General Cashier submits the acts to the Commission on Cash Handler Irregularities.

The same rules apply as those for the convening, composition and functioning of the Commission in connection with the administrative sanction procedure.

The Commission, after examining every useful element (e.g. inspection report, reports, etc.) and evaluating any defensive arguments put forward by the intermediary or cash handler may order that no further action be taken or, where the circumstances warrant it, may propose that the judicial authorities be notified.

(... *omissis* ...)

Where cases that are the subject of criminal reports or complaints involve supervised persons, the Coordination and External Relations Directorate of the Directorate General for Financial Supervision and Regulation will be informed thereof.

2. Notification of other authorities

Whenever inspections or off-site controls find matters possibly of interest to other authorities or supervisory bodies other than the judicial authorities (for example: Ministry of the Interior, Finance Police), the Head of the General Cashier, after evaluating all the evidence available, may:

- decide to take no further action, when it is determined that no aspect falls within the competence of other authorities; or
- send reports to the competent authorities.

In the case of information regarding irregularities which could be significant for the Financial Intelligence Unit, the General Cashier Directorate will transmit the information directly to the Unit.

Reports concerning supervised intermediaries will be made known to the Bank of Italy directorates or branches competent for supervising the intermediary and to the Consumer Protection and Anti-Money Laundering Directorate of the Directorate General for Financial Supervision and Regulation as regards reports to the Financial Intelligence Unit.

The possibility for the General Cashier Directorate to convene the Commission on Cash Handler Irregularities where the cases require a more thorough examination or involve particularly complex aspects will not be affected.

CHAPTER VI – COOPERATION WITH HEAD OFFICE DIRECTORATES AND WITH BRANCHES

The General Cashier Directorate will inform the Directorates of the Directorate General for Financial Supervision and Regulation and those of the Directorate General for Markets and Payment Systems and the branches of every fact found during controls on cash handlers having relevance for the supervision respectively of banks, Poste Italiane S.p.A., electronic money institutions and payment institutions or for the oversight of payment systems. Where aspects having relevance for the application of supervisory regulations and provisions are found, the General Cashier Directorate will inform the Regulation and Macroprudential Analysis Directorate

The information linkages with the Coordination and External Relations Directorate and Consumer Protection and Anti-Money Laundering Directorate of the Directorate General for Financial Supervision and Regulation are specified in Chapter V.

CHAPTER VII – STRUCTURE AND UTILIZATION OF THE INFORMATION ON CASH HANDLERS

1. Premise

To perform controls on cash handlers and monitor banknote recirculation in Italy, the General Cashier Directorate makes use of the data and information reported by cash handlers and other information on cash handling acquired, for example, during inspections.

(... *omissis* ...)

Where monitoring points to the necessity of intervening vis-à-vis cash handlers at which anomalies have been found, it is necessary, after a thorough examination of the problems, to activate the instruments provided for in Chapter III, including for interventions deriving from the exceeding of the threshold set by Article 7 of Decision ECB/2010/14 on the distribution of banknotes checked manually by remote branches authorized by the Bank of Italy (... *omissis* ...).

2. Information archives on the activity of cash handling

The archives holding data and information are described below.

2.1. General Register of Cash Handlers

The Register, which stores the information on the identification forms with which cash handlers report their activity, has two sections:

Section I – Register of reporting entities.⁶ Takes in information on cash handlers that operate machines for the authentication and fitness sorting of banknotes and/or distribute banknotes to the public through cash dispensers, or that have self-checkout terminals with a cash-withdrawal function not used for purposes of banknote recirculation. For each operator the register records:

- corporate name;
- ABI code (for banks only);
- type of operator;
- GS1 code (GLN of registered office);
- address of registered office;
- description of activity performed;
- machines used for the authentication and fitness sorting of banknotes;
- organizational structure of cash handling activity;
- phases of cash handling activity outsourced and identity of outsourcer;
- reference person for relations with the Bank of Italy.

The register receives data from the Banknote Circulation and Transport Division, using the information entered in Reporting Form A as per Annex 4 of the Provisions on Cash Handling Activities and in statistical reports.

The Banknote Circulation and Transport Division checks the completeness and congruence of the data reported; requests for data supplementation or correction are made via the reference person indicated by the cash handler. The information contained in Form A is transferred to the register by means of a specific function of the Cash Portal application. The same procedures are followed to update the archive for changes to the data or cessation of activity.

⁶ Cash handlers required to send periodic statistical reports to the Bank of Italy.

(... *omissis* ...)

Section II – Register of cash handlers that carry out manual checks only. Receives information on cash handlers that only run manual checks on banknotes and therefore recirculate them only via a physical branch. These operators are not required to use machines for banknote recirculation.

For each person the register contains the following information entered in Reporting Form B as per Annex 4 of the Provisions on Cash Handling Activities:

- corporate name;
- ABI code (for banks only);
- type of operator;
- address of registered office.

The Banknote Circulation and Movement Division inputs data to and manages Section II using the same procedures as for Section I.

2.2. Register of “remote branches”

The register is for cash handlers authorized to fill cash dispensers located at branches in remote places and having a modest volume of payment transactions with banknotes that have undergone manual fitness checking.

The register receives data inputted by the Banknote Circulation and Movement Division upon the grant of authorization to use the Cash Portal. It records:

- the GLN of the reporting entity;
- the GLN and the address of the remote branch;
- the basis for recognizing its status as a remote branch (for example: population of the municipality in which it is located or distance from a branch of the Bank of Italy that provides cash handling services to institutional customers);
- data on operations (for example, volume of cash dispensed by cash dispensers at the branch).

(... *omissis* ...)

2.3. Archive of periodic statistical reports

The archive contains the periodic statistical reports on banknote recirculation that each cash handler transmits to the Bank of Italy using the functions of the Cash Portal, as indicated in the Guide for the Compilation of Cash Handler Statistical Reports.

The information concerns:

- places where banknotes are counted: GLN of the reporting entity, GLN of the counting place, type of locale (counting room, bank branch, other), address;
- stock of authentication and fitness sorting machines (number of machines – subdivided by model – installed in each counting place; number of cash dispensers in use; number of customer-activated terminals enabled only for cash deposit and not directly involved in the recirculation process);
- data on operations (quantity of banknotes handled and outcome of processing; for the breakdown, see the Guide for the Compilation of Cash Handler Statistical Reports).

The application used for inputting the data checks the reports, verifying their completeness and congruence (controls for formal and substantial correctness). Errors are notified to the reporting

entity with a specific message. The General Cashier Directorate, as system owner and manager of the application, provides user support, checks that all the reporting entities have forwarded data and sends reminder notices when necessary.

Access to the data modification function is limited strictly to the personnel of the reports support group in the Banknote Circulation and Movement Division, who operate with the reporting entity's direct authorization (granted via an e-mail request for modification) and leave a record of the activities carried out.

(... *omissis* ...)

2.4. Archive of anomalies found by the Bank of Italy's branches

(... *omissis* ...)

3. Utilization of the information for controls on cash handlers

The data and information acquired on cash handlers undergo processing that serves to keep the information set on operators up to date and to derive indications for the performance of controls.

3.1. The cash handler's dossier

(... *omissis* ...)

3.2. Control indicators

(... *omissis* ...)

3.2.1. Operations indicators

(... *omissis* ...)

3.2.2. Quality indicators

(... *omissis* ...)

4. Utilization of data for aggregate processing

(... *omissis* ...)

CHAPTER VIII – TESTING OF BANKNOTE HANDLING MACHINES

Banknote handling machines undergo the following types of test to ascertain their ability to sort banknotes: initial test, annual test, retest, and bilateral test.

These tests differ from the monitoring tests performed during inspections in that, as a rule, they are requested directly by the manufacturers of the machines or are designed to check the machines' ability to detect a new type of counterfeit.

In detail:

- the initial test is requested by the machine's manufacturer in order to have it entered in the list of machines passed by the European Central Bank;
- the annual test is performed, again at the manufacturer's request, in order check whether the machine has maintained its banknote fitness sorting ability as determined in the initial test;
- a retest is carried out at the initiative of the national central bank whenever an insidious new counterfeit appears, to ascertain the machine's ability to detect it;
- a bilateral test is carried out by a national central bank at the request of a cash handler or of a trade association of cash handlers, to ascertain whether it is possible to continue to use a machine that has not undergone the annual test by its manufacturer because, for example, the manufacturer has gone out of business or no longer produces the machine in question.

(... *omissis* ...)