



THEMED EXAMINATION PROGRAMME 2011: ANTI-MONEY LAUNDERING AND COMBATING THE FINANCING OF TERRORISM

SUMMARY FINDINGS

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1 Introduction

- 1.1 The Anguilla Financial Services Commission (“the Commission”) attaches great importance to the effective implementation of the revised regime for anti-money laundering and combating the financing of terrorism (“**AML/CFT**”) introduced in 2009.
- 1.2 Therefore, in 2011, the Commission decided to undertake a series of themed on-site examinations to assess the extent to which regulated entities are operating in accordance with their obligations under the Proceeds of Crime Act (“**POCA**”), the Anti-Money Laundering and Terrorist Financing Regulations (“**the Regulations**”) and the Anti-Money Laundering and Terrorist Financing Code (“**the Code**”).
- 1.3 The purpose of this paper is to provide industry with a summary of findings. It is not intended comprehensively to describe all risks that may be associated with non-adherence to legal and regulatory obligations and not all practitioners face all the issues described below. However, the observations made reflect areas of risk that have been noted by the Commission as potentially of relevance and are provided for general guidance.

2 Scope

- 2.1 The Commission’s on-site programme was designed to cover a range of financial services business types including company managers, trust companies, insurance

companies, money services businesses and banks.

- 2.2 Following completion of an initial off-site questionnaire by the sample practitioners, eleven on-site examinations were undertaken between July and October 2011 concentrating on corporate governance and related issues.
- 2.3 Commission officers reviewed, on a sample basis, the records, files and written procedures maintained by the practitioners and held discussions with management and staff involved in strategic, operational and compliance matters. Where appropriate, specific areas for improvement were identified with individual practitioners and plans for remediation put into effect.

3 Preliminary observations

- 3.1 There were a significant number of areas where practitioners exhibited a low level of compliance with the legislative framework with only a minority of those examined achieving acceptable standards. The findings are based upon a relatively small sample and the Commission acknowledges that they may not be representative of the financial services sector as a whole. The major areas of failure are outlined in section 4.
- 3.2 However, service providers' record keeping policies conformed to the current AML/CFT legislative requirements and some two thirds required customers to complete application forms and provide appropriate identification.
- 3.3 In addition, practitioners had complied with the requirement to appoint money laundering reporting and compliance officers ("MLRO/MLCO") although they tended to be unaware of the requirement to apply to the Commission for the approval of these appointments.

4 Major areas requiring improvement

- 4.1 Some practitioners failed to document adequate AML/CFT policies and procedures, notably in relation to customer due diligence.
- 4.2 Only a minority of practitioners had completed a formal risk assessment and implemented a risk based approach in relation to customers, products and services and geographical location.
- 4.3 The Commission observed that, although AML/CFT training may have been provided, a number of relevant staff did not have adequate knowledge of the AML/CFT framework.
- 4.4 The Commission was surprised at the low level of suspicious activity reporting observed.

5 Factors for consideration

Based on the findings of the examinations, supplemented by information gathered from other meetings with industry practitioners and its review of various files, the Commission wishes to draw the attention of financial services businesses to the following issues:

5.1 Risk Assessment

5.1.1 Section 3 of the Code makes mandatory the preparation of a formal risk assessment leading to a specific strategy for dealing with AML/CFT issues, including risk mitigation measures. This should be adopted by the Board of Directors and kept under regular review. The Commission expects that this document will contain a realistic assessment of the risks posed by various types of business.

5.1.2 The risk assessment should take account of the service provider's organisational structure, its customers, jurisdictions with which its customers are connected, its products and services and how those products and services are delivered. In particular, such assessments should consider:

5.1.2.1 The risk appetite of the financial services business itself;

5.1.2.2 The need for clear distinction between the assessment of risk level and the impact of mitigation measures; and

5.1.2.3 The potential features of financial services business in Anguilla that should properly be assessed as "higher" risk: for example, non "face to face" business, reliance on third party introducers, private banking, international business companies, customer insistence on excessive secrecy, overly complex ownership structures.

5.1.3 It is acknowledged that "higher" risk does not automatically mean that a relationship should not be established or that offences have been, or will be, committed. Equally, thorough and diligent research and/or other mitigation can be used to reduce the risk and justify actions taken by service providers.

5.2 Customer Due Diligence

5.2.1 There are two separate phases to customer due diligence. The first is the gathering of facts and the second is a commonsense assessment to determine risk.

5.2.2 The Commission would expect practitioners, dealing with predominantly international issues, to identify a substantial portion of their business as "higher" risk in absolute terms. It is then essential that sufficient due diligence is undertaken.

5.2.3 Such due diligence should include proper attention to the need to seek source of wealth information in addition to identifying the source of funds.

5.2.4 The definition of politically exposed person includes "*a known associate of*" a person

entrusted with a prominent public function. It is important to remember that there are some jurisdictions where this definition would include many prominent business people.

5.2.5 The Commission has seen evidence of service providers relying on certificates completed by clients that simply assert that funds come from clean sources and are not being placed to avoid the impact of liquidation and similar circumstances. In some instances, these certificates are required to be notarized. Whilst this may be a useful discipline, in practice, it likely affords little protection and runs the risk that employees will fall into the habit of accepting such certificates as a substitute for sufficient enquiry or assessment. Service providers should not place reliance on client certification which is unsupported by adequate detail. They should establish the source of funds or wealth, according to the risk level of the activity, and seek evidence in appropriate circumstances.

5.2.6 It is important to focus on the substance of due diligence, as distinct from its form. The Commission has identified a number of circumstances where service providers seem content with the form of due diligence. For example:

5.2.6.1 Repeated use of formulaic reasons for a customer's use of Anguilla as a jurisdiction. Simply repeating that the customer wants to use Anguilla because it has a reliable legal environment and is secure is insufficient. Whilst these facts may be true, they are not a comprehensive explanation for a customer's decision to use an off-shore jurisdiction; and

5.2.6.2 Taking undue comfort from the fact that a potential customer does not feature in third party databases, such as World Check. Valuable as such checks are, provided they are not conducted on a "precise match" basis, they should often be supplemented by checks on public domain data through an internet search engine and reference to the lists of public warnings published by appropriate regulatory agencies.

5.2.7 Even the use of a range of measures cannot guarantee that a service provider has complete and correct information. However, risk is limited by the widest possible enquiry supplemented by objective consideration, assessment and challenge of available information.

5.3 Placing reliance on third parties

5.3.1 The legislative framework allows service providers to place reliance on third parties for elements of due diligence. The motivation for this is to avoid burdening customers with supplying the same information to a number of counter-parties. However, the need for service providers to carry out on-going monitoring probably mandates that they should still collect the information from their introducers.

5.3.2 The Commission believes that this would best be accomplished by introducing a comprehensive introduction certificate and intends to pursue the production of such

with the financial services industry.

5.4 Impact of the “objective test”

5.4.1 Sections 128 and 129 of the POCA require a person to disclose knowledge or suspicion of money laundering to the authorities where he or she:

*“knows or suspects, or **has reasonable grounds for suspecting**, that another person is engaged in money laundering”.*

5.4.2 The words highlighted in bold introduce what is commonly known as the “objective test”. This means that a person can be guilty of an offence by not disclosing information where an ordinary person (with relevant experience in financial services) would consider sufficient grounds for disclosure existed.

5.4.3 Service providers should be aware that this is a wide-ranging and significant change and only limited opportunities are offered to employees in financial services to have a “reasonable excuse” for not disclosing. It is no longer sufficient for them to claim that they did not know or suspect.

5.5 Higher Risk jurisdictions

5.5.1 The Commission requires practitioners to exercise care when dealing with business originating from jurisdictions characterised by some or any of the following features:

5.5.1.1 Common use of complex structures to conceal true ownership;

5.5.1.2 Informal corporate control structures;

5.5.1.3 Importance of political patronage links in securing corporate ownership or valuable franchises;

5.5.1.4 Endemic corruption, evidenced for example in Transparency International’s Corruption Perception Index and other publically available resources;

5.5.1.5 Emphasis on form over substance in the legal, accounting and regulatory environments;

5.5.1.6 Limited depth of the financial system; and

5.5.1.7 Significant physical risk in business conflict resolution.

5.6 Other vulnerabilities

5.6.1 The Commission wishes to emphasise that Anguilla may be targeted by unregulated investment and forex broking and dealing. These activities may be linked to insider dealing in securities, “penny share” schemes such as “pump and dump” and boiler room scams. The Commission will want to see the measures practitioners have put in place to mitigate these risks.

- 5.6.2 There is a substantive risk that claims of legitimate asset protection may conceal attempts to protect the proceeds of crime, especially fraud, or assist in fraudulent preference.
- 5.6.3 There is always a possibility that individual service providers will be blinded to the risks involved by the prospects of the significant income to be obtained.
- 5.6.4 The same may be true of external introducers and intermediaries, whatever the jurisdiction in which they operate and however strong their AML/CFT regime may appear to be. The reliability of the chain of introduction is only as strong as its weakest link, which may be a single individual, no matter how prestigious the firm for which he or she works. Service providers are reminded that, where an introducer has produced one piece of business that has proven problematic, it may be prudent to exercise increased due diligence and caution in assessing all business from that source.

6 Conclusions

- 6.1 The level of compliance with the POCA, the Regulations and the Code was disappointing and worrying, given that the regime had been in place for two years. It appears that the jurisdiction may be exposed to significant risk. In addition, it is worthwhile for practitioners to bear in mind that a potential client, or introducer, does not have to have been convicted of a criminal action to pose a threat to the reputation of Anguilla.
- 6.2 The Code specifies minimum standards with which every service provider must comply. However, it is important to remember that a service provider should always consider whether, on a case-by-case basis, additional measures are appropriate.
- 6.3 Against this background, the Commission will be extending this initial sample of practitioners with a further programme of AML/CFT compliance visits during 2012. The Commission expects that practitioners will be able to demonstrate a high level of general compliance and will be particularly concerned to evaluate their approach to the specific issues outlined above.
- 6.4 Finally, it is important to recognise that Anguilla, as a jurisdiction, and its service providers have given a commitment to meet accepted standards in the international efforts to combat money laundering and the financing of terrorism. The Commission will seek to ensure that this desire to comply is given due force in practice. It is optimistic that the examinations to be conducted in 2012 will produce a more positive assessment of standards of compliance.

Anguilla Financial Services Commission
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