Moneyval Feedback Presentation
Thursday, 11 February 2016

Good morning ladies and gentlemen and welcome to this seminar co-hosted by the Commission and the Guernsey Border Agency on the findings and recommendations from the Moneyval report.

I am Fiona Crocker, Director of the Commission's Financial Crime Supervision and Policy Division and I want to start with what the report's findings mean for the Commission, including where changes are likely to be required to the Handbooks.

Phil Hunkin, Head of the Economic Crimes Division at the Guernsey Border Agency will then pick up on the implications of the findings for law enforcement and Richard Walker, Director of Financial Crime Policy at the Policy Council will close with the government's view.

There will then be time to ask questions and Advocate Kate Rabey from the Law Officers will be joining us for that session. Kate is Guernsey's Head of Delegation at Moneyval. Refreshments will be available afterwards.

As an aside and so that you don't feel that you have to take notes today, my slides and presentation will be published on the Commission's website shortly after this event.

Before I cover those areas which are relevant to the Commission and which will shape our "to do" list, I want to dwell for a few moments more generally on who Moneyval is, why Guernsey joined and the good outcome from Moneyval's evaluation.

Moneyval is a committee of experts on the evaluation of measures to tackle ML and TF. It was formed by the Council of Europe to ensure that its members have effective controls in place to meet international standards issued by the FATF. It does this on a continuous basis through a process of evaluations and follow up of its members on areas for remediation.

Guernsey, together with the Isle of Man and Jersey who were previously assessed by the IMF, joined Moneyval for this reason because there was no means by which we could show on the international stage how we had addressed recommendations which the IMF had made.

The Bailiwick was assessed by Moneyval against 25 of the 49 FATF recommendations considered to be key or where we were marked down by the IMF. Moneyval concluded that we were fully compliant against 13 FATF recommendations; largely compliant on 11 recommendations and partially compliant on just one.

A huge amount of work went into this which began in earnest a year before Moneyval's week-long visit in October 2014, and continued long after as the assessors continued to question and

challenge our AML/CFT defenses until the plenary in September 2015 brought it to a close. The assessment was wide ranging and in-depth and to secure such a good outcome for the Bailiwick it had to be a real team effort.

The 4 of us up here today may represent the principal players in team Guernsey but far more individuals and organisations in both the public and private sectors have been involved. So for those of you in the audience with whom we worked or we called upon for help with the evaluation - thank you - your effort was worth it!

Within the report there are some very positive comments about both the various AML/CFT agencies in the Bailiwick and about our industry which we do not, as a Bailiwick, often receive from external parties. They also touched very favourably upon the knowledge and understanding that firms had of their AML/CFT obligations and the robustness of client take on measures.

This is particularly encouraging because it encompasses fiduciaries, accountants, estate agents and lawyers. They are an important part of our industry but it is often here where other jurisdictions are marked down because supervision of these sectors has not been embedded, or because it is fragmented across a number of supervisory agencies.

I wish I had time to dwell on all of the good stuff unfortunately I don't however I would very much encourage you to read it.

The report is divided into a number of sections covering the legal system, preventive measures, legal persons and arrangements and national and international co-operation. It is hefty document running to 322 pages.

If you want to dip into the report, the parts of the assessment relevant to supervision and the Handbook can be found within the section on 'Preventive Measures' under Recommendations 5, 12, 17, 23 and 29. If you prefer a quick snapshot of all the ratings and recommendations they are in the tables on pages 280 to 294 of the report.

The significant high level findings from the report for the Commission are:

- That Moneyval determined that the Commission had the resources and powers to supervise and did so effectively – the Bailiwick was compliant against the FATF's two supervisory Recommendations;

- That for FATF Recommendations 5 and 12, which are the ones relevant to the AML/CFT measures in the Handbooks and their implementation by industry, we were largely compliant with the Standard;

- And finally, for Recommendation 17, which covers sanction penalties where the Bailiwick was marked down with a partially compliant rating because of 2 matters.

I will cover the recommendations that relate to supervision first. This will be brief in relation to how we supervise because no recommendations for change were made to either our role as gatekeeper to the industry in relation to the authorisation and licensing measures we have to prevent criminals from controlling firms; or to how we apply risk-based supervision through PRISM. Therefore no changes as a result of the Moneyval assessment are anticipated here.

I will now deal with the Partially Compliant rating for recommendation 17. This markdown was partly because the assessors considered that the maximum financial penalty available to the Commission of £200,000 was not dissuasive or proportionate to the size of our finance industry and that consequently the fines were not an effective deterrent to non-compliance. A similar finding was made by the IMF on their last inspection in 2010.

As the Bailiwick's immediate response to this to raise the level of penalties has already been well aired and is in train I will leave any comments there and instead pick up on the second issue which was the lack of sanctions across the Bailiwick for a firm failing to report suspicions.

The reporting of suspicions has been an area of focus during our onsite visits – and I hope that is evident from the latest enforcement case we published which identified that the fundamental deficiencies within the firm concerned included delays in reporting suspicions to the FIU and the lack of scrutiny of unusual transactions.

We have a very good dialogue with both the FIU and the Guernsey Border Agency and we share information through the proper legal channels using the relevant gateways in the regulatory laws. We have, since the Moneyval visit, taken steps to enhance our information sharing arrangements and to keep up regular dialogue. Needless to say the reporting of suspicions continues to be an area of focus for our onsite assessments.

I will now move to the findings and recommendations relevant to the Handbook.

Given the good outcome on the ratings and positive commentary about all of us in the report I appreciate that it may now seem at odds to hear that there are some deficiencies for the Bailiwick to address to strengthen its AML and CFT measures which have been made as part of Moneyval's assessment of our compliance with Recommendations 5 and 12.

Broadly these deficiencies fall into two categories. Firstly, those which relate to assessing risk for higher risk customers, and those deficiencies considered to be gaps in the regime on the application of due diligence measures to certain types of customers which could expose the Bailiwick to the risk of money laundering or terrorist financing.

My aim is to raise with you what those issues are so that you can see what is on our agenda. It is not my purpose today to present solutions to all the recommendations because there are some recommendations, particularly around changes Moneyval proposes to the Handbook, which will take a bit of thought and discussion to get right.

I also want to make it very clear from the outset that the Commission has no intention of making any changes which put the AML/CFT requirements in Guernsey over and above international standards set by the FATF.

I will start with assessing risk for higher risk customers. Under our regime it is only mandatory to apply enhanced due diligence measures to foreign politically exposed persons, customers connected with non FATF compliant jurisdictions and those customers assessed as high risk by the firm **whereas** the FATF expects enhanced measures to be applied to non-resident customers, private banking relationships and trusts and companies which are personal asset holding vehicles.

Clearly, for some firms here, a large number of their customers will bear one or more of these traits.

Moneyval has therefore raised the issue that, the list of higher risk customers to which enhanced due diligence measures must be applied, omits categories of customer which are relevant to some Guernsey firms.

The assessors then formed the view that, because enhanced measures for these types of customer were not mandatory, firms' customer risk assessments were not sufficiently taking into account the accumulation of risks arising where these higher risk factors are present within a relationship which may present overarching money laundering or terrorist financing risks.

As a result of this, the assessors concluded that the customer due diligence measures which were then applied may not be commensurate with the actual risk.

This is not a new issue as the assessors picked up the recommendation which was made by the IMF that the list of customers to which enhanced measures must be applied should be expanded.

Changes were made in 2013 in response to the IMF's proposal but those changes stopped short of the types of customer identified by the FATF to whom enhanced measures must apply. There is recognition in the report that these types of customers do not apply to all firms and also that many firms classify significantly more of their clients as high risk than that required by regulation.

However, the assessors conclude from firms' policies and procedures that, customer relationships which cumulatively have the factors identified by the FATF as high risk, would not be classed as such unless there was another risk factor such as the customer being connected with a country with significant corruption levels.

As it is the risk assessment which determines the extent of the due diligence measures which are then carried out by the firm, the assessors then question whether sufficient due diligence might be done for those relationships which contain those high risk characteristics.

They do elaborate on their particular concerns about some of these types of relationships, for example, they identified that for firms undertaking due diligence on customers which are trusts or companies, there will be little on public record about their activities; and as most trusts are established as discretionary trusts, that there is therefore a lack of certainty over who will benefit and when.

They also noted that some firms had excessively high risk appetites and cite from the procedures for one firm which set out that if there was no legitimate economic or other rationale for the relationship the client would still be accepted.

They have therefore recommended that the list of higher risk clients to which enhanced due diligence must be applied, should be expanded: to include these categories relevant to Guernsey; that the authorities should ensure that customer risk assessments take sufficiently into account the accumulation of risk within a relationship with these factors present; that certain due diligence measures should be required for high risk relationships; and finally that firms should be encouraged to more clearly define their risk appetite including specifying where, based upon an assessment of risk, a relationship would be refused or ceased.

The due diligence measures which they propose are that firms should, for high risk relationships: have sight of trust deeds, subsequent deeds and letter of wishes for trust relationships in order to mitigate some of that uncertainty over the timing and identity of the

recipient of a distribution from the trust; and that firms should seek on a more frequent basis documentary evidence on the source of funds and source of wealth of high risk customers.

They raise one further recommendation that firms' client files should properly record the intended purpose and rationale for relationships, including 'Why Guernsey?' to assist risk assessment and monitoring as they had identified that a number of firms were undertaking remediation exercises to plug gaps in their records on this.

I suspect that for many here expanding the list of higher risk customers to which enhanced measures must be applied will be the most significant outcome from the evaluation.

However some firms may already be applying measures defined in the Handbooks as enhanced such as senior management approval or obtaining extra information on the relationship to a wider range of customers than those rated high risk.

We are faced with the issue that if the list is not expanded, Guernsey will not meet international standards, but this time we are not faced with the Bailiwick leading on this issue.

Other jurisdictions, including those which have a similar client profile to us such as Jersey, have made changes. We can therefore draw upon what other jurisdictions, including those which have recently been assessed, have done.

In determining how this should be addressed please remember my assurance that the Commission intends only to change what is absolutely necessary to meet the agreed international standards and what we have been asked to do.

The second type of findings can be categorised as gaps in the regime where there is no application by a Guernsey firm of due diligence measures to beneficial owners and underlying principals of certain types of customer.

These concerns principally fall under the simplified due diligence measures in chapter 6 of the Handbook regarding low risk relationships. I have to warn you that this will get rather technical.

The first relates to the circumstances to which the intermediary provisions can be applied. Our intermediary arrangements allow, in certain areas, a professional financial intermediary based in an Appendix C country acting for third parties to be treated by the Guernsey firm as the customer to identify and verify rather than the underlying customer or customers of the intermediary.

Although the intermediary will be undertaking due diligence on its customers, the Guernsey firm will not know the beneficial ownership of the underlying funds coming into Guernsey which they will be handling. It is the FATF's general rule that the customer must be subject to full customer due diligence measures including the requirement to identify the beneficial owner.

Whilst the FATF accepts that where the risks are low, due diligence measures can be reduced those measures can never be disapplied by the firm which is what the assessors identified was happening within the Intermediary provisions.

Our intermediary arrangements are used in the banking and fund sectors in Guernsey. They are commonplace in many other countries too and are endorsed in AML guidance which has been issued by the international standard setters such as Basel and IOSCO.

The assessors do not propose wholesale change to these provisions, but they have recommended that the Handbook rules be amended so they do not provide discretion to refrain from any mandatory due diligence measures including on the underlying beneficial owner of a regulated or authorised collective investment scheme, which has only a very limited number of investors.

The assessors were concerned that because the intermediary provisions mean that the Guernsey firm does not have to do any customer due diligence on the beneficial owner of the funds being invested into the scheme, this could be exploited by a party establishing a regulated scheme through which to launder criminal money and because of the intermediary provision there would be no due diligence checks carried out in Guernsey on the underlying investors.

They saw this risk principally arising in closely held private schemes and recommended that the intermediary provisions should not be available to schemes with a very limited number of investors.

As Guernsey does have a number of funds with a small investor base we will ensure that proposed changes to the rules and guidance in the Handbook are well aired with the funds sector to minimise unintended consequences.

There is a further issue with our intermediary provisions. Generally they can only be applied when the intermediary is based in a country on Appendix C but there are two exceptions where the intermediary is a subsidiary of an Appendix C business acting as nominee or pension trustee.

Potentially this means that if those subsidiaries are located in jurisdictions outside Appendix C where they are prevented from applying the FATF compliant controls of their parent, the AML/CFT controls of the subsidiary might be defective. Moneyval therefore proposes that this discretion for non-Appendix C subsidiaries should cease.

They also identified potential weaknesses where the simplified measures can be followed for customers who are companies listed on a regulated market. These markets are defined in the Insider Dealing Order but there are no measures in that Order or the Handbook which ascertain whether these markets have adequate disclosure requirements around ownership.

They raise this because of the uncertainty which could arise over a company's ownership or control if there are inadequate disclosure requirements.

Moneyval therefore recommends amending the Handbooks to limit the application of simplified due diligence measures to companies which are listed on a stock exchange where the disclosure requirements have been assessed.

Moneyval also propose that there should be a requirement upon firms dealing with trusts to identify the owners of corporate trustees located in Guernsey or in Appendix C jurisdictions because the present provisions exempt firms from having to identify the owner of the corporate trustee.

They take the view that it is essential that the Guernsey firm knows who ultimately controls trust assets and to be aware of potential relations that might exist between the controller of the trustee and the settlor and beneficiaries. The recommendation proposes identifying this party – but it stops short of requiring verification.

There is however one further area which has been identified as a gap in the Bailiwick's regime but this falls outside the Handbook. It relates to the exemption from licensing for individuals holding up to 6 directorships.

This is an exemption in the Fiduciaries Law whereby an individual who holds up to 6 qualifying directorships does not need to hold a personal fiduciary licence. This issue was also raised by the IMF

Whilst a fiduciary licence is not required for their activities, they are required to comply with the Proceeds of Crime Regulations and Moneyval proposes that the Commission should take measures to ensure that these unlicensed individuals effectively comply with the AML/CFT requirements.

Just to clarify this recommendation does not affect individuals who hold directorships by virtue of their employment with a licensed firm. There are automatic statutory exemptions where an individual employed by a licensed firm holds a number of directorships of client companies or regulated funds. In addition it does not apply to Bailiwick residents acting as a director of their own company or of a local trading company such as a restaurant or garage.

The recommendation presents an interesting challenge to supervise, for effective compliance with the AML/CFT requirements, a category of individuals who are not licensed. Therefore, whilst we will work with the AML/CFT agencies to identify the risks this exemption poses, it might fall for consideration about the level of ML and TF risks it exposes the Bailiwick to when the island undertakes the national risk assessment this year, which the Policy Council is coordinating and the Commission will play a key role.

However this is one - together with the recommendations regarding the intermediary provisions on collective investment schemes – which also crosses over into issues outside the Commission's remit regarding more generally beneficial ownerships of trusts and companies. Clearly for those recommendations which spill into other areas there needs to be joined up thinking by the various Bailiwick agencies involved.

As you have heard most of our to do list will be focused on the Handbooks, but I will touch again on supervision. Whilst there are no changes to make to how we supervise some of Moneyval's recommendations around firms' risk appetite, customer risk assessments and remediation work on client files are indicators of the types of issues we might be raising with you as part of our supervisory activities.

They also propose that we consider promoting some good practices which they saw firms applying. These practices include firms obtaining copies of the tax opinion or advice for relationships established for tax planning purposes and firms establishing the source of wealth and the source of funds for medium risk relationships, which both sound sensible measures for enhancing knowledge about the customer.

I hope I have given you a heads up on the topics for supervision where feedback and guidance might be forthcoming in the future. In time we will also pick up through supervision how effective changes to the Handbooks have been to address Moneyval's recommendations.

So in summary Moneyval's main recomendations for the Commisison are: increasing the maximum financial penalty it can apply; ensuring that within the Bailiwick sanctions are applied for cases of failing to report; amending the AML/CFT regime to ensure that CDD

measures are commensurate for higher risk catgeories of clients relevant to Guernsey; and that gaps in the CDD requirements which may make us vulnerable to ML and TF risk are closed.

I have outlined where changes to the Handbooks will need to be made and indicated where supervisory focus can be expected.

It is our intention to start addressing the recommendations where we can. That means for recommendations where changes are required at the level of rules, guidance and supervision we will incorporate them into our existing activities or into the ongoing project to revise rules and guidance in the Handbook.

However, some recommendations such as expanding the list of higher risk clients require changes to the Regulations before amendments can be made to the rest of the Handbook.

As the Policy Council is responsible for the Regulations, representatives of the Policy Council, Law Officers and Commission have begun to work on updating that legal framework to meet the FATF 2012 standards, which is where this work instigated by Moneyval will be brought in.

We are working closely with the Policy Council and the Law Officers to ensure that should those changes to the Regulations be advanced this year that this is co-ordinated with the other changes the Commission propose to the Handbooks to streamline the consultation process into one exercise. That consultation is likely to occur towards the end of this year.

Therefore, should there be areas which relate to the Handbook I would be very pleased to hear your views. I put to you all as a suggestion that this can be through your relevant industry associations such as the AGB, GAT and GIFA.

This is important because some recommendations do mean changes to the AML/CFT requirements you work under. As a Bailiwick we have international standards to meet but I do want to take on board your views as it is important that the changes that are made to meet standards are the right ones for the Bailiwick.

I will be very pleased to take questions on these recommendations a little later after you have heard from Phil and Richard. I now hand you over to Phil.