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Guernsey Financial Services Commission

FEEDBACK ON AML/CFT ON-SITE VISITS

JULY 2012

INTRODUCTION

The Guernsey Financial Services Commission ("the Commission") undertakes routine on-site inspections of the AML/CFT framework of financial services businesses and registered businesses ("businesses"). These inspections inform the Commission about the extent to which financial services businesses are in compliance with the AML/CFT regulations and the rules in the Handbooks.

SCOPE

The Commission's on-site programme is designed to:

- obtain a greater understanding of the activities undertaken by the business;
- review the risks identified by the business as to how it may be involved in money laundering or terrorist financing and assess the policies, procedures and controls which the business has put in place to manage and mitigate the identified risks; and
- provide a follow up process in respect of any deficiencies identified during off-site supervision.

PURPOSE

The purpose of this paper is to provide industry with a summary of findings, which may prove useful to businesses when identifying and managing risk and in considering their AML/CFT policies, procedures and controls. It is not intended to comprehensively describe all findings observed by the Commission during on-site inspections.

This paper complements the Feedback and Typologies 2008-2011 document issued by the Financial Intelligence Service, which provides feedback to financial services businesses on the reporting of suspicion of money laundering and terrorist financing.

Overview

The Commission's original intention was to provide sectoral feedback. However, after analysis of our on-site inspection findings it is clear that the findings across all sectors supervised for AML/CFT are similar. We have therefore consolidated our findings below on a finance-sector wide basis, even though all of the findings do not necessarily apply to all business sectors.

All Guernsey banks and a number of other businesses are part of international groups which have long-established AML/CFT policies, procedures and controls. This significantly aids adherence to local legislation and regulatory requirements. In most cases, compliance with Guernsey standards is achieved by suitable amendments and additions to group practice. Local businesses are also able to draw on group expertise and systems support. As a consequence of drawing on group expertise some have policies, procedures and controls which exceed the Bailiwick's minimum requirements

During 2011 the on-site teams undertook 94 on-site inspections which had an AML/CFT element. The Commission has formed the view that as a whole the industry is, in the main, operating in accordance with its obligations under the AML/CFT regulations and handbooks. All businesses have, in large part, successfully introduced approaches to the management of risk that classify customers, products, transactions and jurisdictions into high, standard and low risk in an appropriate manner. The overall assessment of risk then centres on a risk classification for each customer.

Summary of Findings

The remainder of this paper sets out both positive findings and some areas where more work was required to achieve consistent compliance with the AML/CFT provisions.

Business Risk Assessment

All businesses visited were observed to have undertaken and documented a business risk assessment, although undertaking a full business risk assessment leading to a specific strategy for dealing with ML/FT risk was problematic for some businesses.

On a number of occasions the Commission noted that businesses had adopted a generic business risk assessment, drawn from group experience, or obtained or derived from a parent organisation or third party consultant/adviser. These business risk assessments did not relate to the relevant risks inherent for their particular business models and their operating environment and, therefore, the businesses could potentially be exposed to its products and services being used to launder criminal proceeds or finance terrorism.

In some instances the business risk assessment did not identify risks which the business felt it had already mitigated. By omitting such risks from the business risk assessment a business is not able to demonstrate its consideration of ML/FT risk and identify the appropriateness of the measures it has adopted to manage and mitigate the risk.

There was some confusion as to which party was responsible for undertaking the business risk assessment where there were a number of parties involved in the management and administration of structures.

Relationship Risk Assessment

Generally, businesses had risk assessed their business relationships and occasional transactions. Some relationship risk assessments did not clearly demonstrate the basis for determining the particular ML/FT risk of a relationship, whilst others confused ML/FT risk with other risks or considered a very limited number of factors. Some businesses had difficulty in separating the concept of a business risk assessment for their business as a whole from a relationship risk assessment. The reason for a business risk assessment is to ensure that the AML/CFT policies, procedures and controls of a business are appropriate and effective, having regard to the assessed risk. Relationship risk assessments, which must be carried out for each individual relationship and occasional transaction, consider the extent of potential exposure to the risk of ML/FT.

High Risk

The Commission identified that some businesses did not have documented policies, procedures and controls for the risk rating of customers. In the absence of these policies, procedures and controls, customers that should have been classified as high risk were not and, consequently, enhanced due diligence was not undertaken to mitigate the associated ML/FT risk.

Some businesses encountered difficulties in ensuring that, where one aspect of the business relationship or occasional transaction was considered to carry a high risk of ML/FT, the overall risk of the business relationship or occasional transaction is to be treated as high risk. Examples seen included PEPs or business activities connected with high risk jurisdictions, whereby the financial services business was downgrading the risk to standard or even low, based upon their assessment of the customer and/or the risk posed, in breach of the rules in the handbook. Whilst knowledge cannot downgrade risk, it is very important for managing and mitigating risk.

There were instances where businesses had sought considerable information on potential relationships and, by documenting such information, the appropriateness and effectiveness of the mitigation could be assessed when high risk relationships were reviewed.

There were also instances where businesses adopted a policy of not accepting high risk business as a risk control measure, but failed to ensure that it had in place documented policies, procedures and controls for high risk customers. This created the potential for high risk customers to be taken on inadvertently, or low or standard risk customers to become high risk without adequate risk assessment or monitoring being in place.

Low Risk

Where financial services businesses adopted reduced or simplified customer due diligence measures for business which has been assessed as low risk, there were occasions when this assessment was made without taking into consideration the provisions of the regulations and the rules in the handbook. It was also identified that, on some occasions where a

determination had been made that it was low risk business, the reasons for that determination had not been documented.

Additionally, there was some confusion regarding the definitions of "introducer" and "intermediary" relationships providing for businesses to assign a low risk assessment to a relationship incorrectly.

Monitoring

In advance of the introduction of the regulations and the handbook for financial services businesses, most businesses had developed risk based programmes involving periodic reviews. These programmes have now bedded in and examples were seen where those risk-based reviews were timely and, where issues which could cause concern were identified, these were being followed up. However, there were also instances where delays had built up because of a lack of resources to carry out reviews or at senior management level for signing off reviews. Where a decision had been made to carry out monitoring upon trigger events there were occasions where there was no demonstration of any consideration of whether that model is appropriate on the basis of risk. This led to instances where insufficient enhanced monitoring had been undertaken when customers had been identified as high risk.

Record Keeping

In general, the record keeping requirements gave the Commission little concern. There were a small number of cases where policies, procedures and controls had not been updated in line with current legislation, rules and guidance, leading to staff not being fully aware of their obligations. Additionally, on occasions files which were retained overseas or by third parties were found not to be readily retrievable when the Commission requested to view them.

Training

Most businesses provided good general training to all staff, meeting the requirements of the regulations and the rules in the handbook. Businesses had often made use of external training sources and in some instances (particularly larger firms) AML/CFT training was being provided at a group level. However, there were instances where training was provided at group level, which had not been specifically tailored to meet the legislative requirements of the Bailiwick.

On occasions, the approach to training had not been formalised, particularly where training was provided by one or more staff of an organisation to other members of staff. The lack of a formal approach to training made it difficult for some businesses to evidence compliance with the requirements of the regulations and the rules in the handbook. The Commission also found several examples where directors and MLROs received the same training as staff on the basis that all the training given is additional training. This training may be appropriate for relevant employees as defined in the handbooks but is not sufficient to meet the additional training requirements for the MLRO and the Board and senior management. The handbooks require the MLRO to have additional training which must include in depth and specific training with regard to areas such as suspicion reports and production and restraining orders. The handbooks also require the Board and senior management to have additional training on the provisions of the relevant enactments and information on the offences and the related penalties, including potential director and shareholder liability.

Additionally, there were instances where the AML/CFT training logs had not been kept up to date. In particular, they did not evidence the nature of the training undertaken and the dates of this training.

UN Sanctions

Awareness of the sanctions legislation was found to be good and businesses had made suitable efforts to implement procedures which meet the requirements of the legislation. Nevertheless, some of the smaller businesses, where the majority of their customers were not local face to face customers, were encountering difficulties in fulfilling their obligations to monitor the sanctions lists as they did not have access to automatic checking software.