Guernsey Financial Services Commission

Industry Seminar – 18 November 2015

Financial Crime Supervision and Policy Division Presentation

Fiona Crocker, Director

Good morning

I would very much have liked to have shared with you today, the findings from Moneyval's evaluation of the Bailiwick's defences against money laundering and terrorist financing and what that will mean for future supervision.

Regrettably however, that will have to wait as we have not yet received Moneyval's final report although we are hopefully just days away from its publication.

As it is over a year since Moneyval's assessment team was here I will explain why it is taking some time for the results to come out and then talk about my Division's other supervisory and policy activities which have had to be accommodated around Moneyval.

There have been some key developments outside of Moneyval regarding the project to update the Handbooks to enable the use of technology in the due diligence process, and on the introduction of an annual financial crime risk return which, going forward, will provide on a regular basis key data for assessing current financial crime risks in Bailiwick firms for use in supervision and project and policy initiatives.

However, I will start with Moneyval and why there has been this delay when the IMF took eight months from its assessment of our AML/CFT measures in May 2010 to publication of its report in January 2011.

A key difference with this assessment has been the peer review process itself. Like the IMF team, the Moneyval assessors consisted of expert representatives from fields of criminal law, law enforcement and supervision but unlike the IMF assessment there is then a peer review process.

This forms a key part of the closing stages, whereby the final draft report, and its proposed ratings and recommendations are considered, and can be challenged or endorsed by the member states of Moneyval at one of the thrice yearly scheduled plenaries at Strasbourg's Council of Europe.

It is only at these plenaries that the report, its recommendations and the ratings for compliance against the Financial Action Task Force standards for combatting money laundering and terrorist financing are finalized.

It is a process for which there is an important caveat - the provisional ratings of compliance that you go into plenary with can go down as well as up. Once that process is over those ratings stay with a jurisdiction until its next assessment.

Completion of this reporting process had tentatively been scheduled for April this year but it became apparent by March, that for reasons which had nothing to do with any particular issue arising from the assessment, that the timetable was not going to be met and that the next scheduled sitting of the plenary when our report could be presented was September.

We have now been through that plenary process and the final part remains the report's publication. We recently reviewed the final draft version of the report and I hope that very soon it will published. After that we look forward to discussing with you what the report's recommendations means for supervision so please watch your emails for an invitation.

We are not the only jurisdiction affected by delay. Jersey was assessed in January this year and had an initial date for plenary in September but that timetable has moved out to December.

And in case you are wondering about the Isle of Man, as it joined Moneyval at the same time as the Channel Islands in December 2012, whereas both Guernsey and Jersey chose to be assessed against the FATF's 2003 recommendations, it elected to be assessed against the 2012 recommendations, and that round of visits by Moneyval only began this year.

The Isle of Man's assessment is due to take place in the first half of next year, and it will be very interesting to see how that goes because it will be the first international finance centre of substance to be assessed not only against the updated 2012 standards but with a new methodology which focuses much more on the effectiveness of a jurisdiction's regime rather than just its technical compliance where the emphasis is on the legislative framework in place.

As the evaluation was in-depth looking into every sector of financial and professional services in Guernsey, the report will be the evidence which shows how seriously Guernsey plc takes preventing money laundering and terrorist financing and the measure of our compliance with international standards.

The themes for this year's industry seminar are productivity and prosperity. It isn't always easy to reconcile these concepts to complying with AML/CFT obligations which take commitment and resources, but the Bailiwick does need a good report to underpin our efforts and our position within the international community, because without a good report our collective efforts to secure a bright future for the Bailiwick will be that much harder.

Take the following two EU initiatives:

Guernsey wants an AIFMD passport thorough which to offer its funds to a European marketplace and it is sometimes forgotten that that marketplace includes the UK.

ESMA - the European Securities Markets supervisor has commented that a jurisdiction's AML rules might be relevant to the European Commission's decision to extend the passport to a non-EU jurisdiction. The Moneyval report will provide evidence for such an assessment.

On the other hand our ease of access to European financial services might depend upon whether or not EU member states require their firms to apply enhanced due diligence measures to our business. Current proposed guidance on transposing the 4th AML Directive for member states from the European supervisory authorities suggests that one of a number of factors that a member state should require its firms to consider are the evaluation reports of that third country against the FATF standards.

It is for external purposes such as these that our work on Moneyval was priortised over the other work of the Financial Crime Division so we could ensure that the report accurately reflects our AML/CFT requirements, accurately reflects the application of those measures, and because we wanted to ensure that the assessors took into account all relevant factors.

Work on this assessment has been very much a 'team Guernsey' effort and because it covers criminal prosecution, policy, law enforcement and supervision it has involved the law officers, government, the Guernsey Border Agency, the Financial Intelligence Unit and the Alderney Gambling Control Commission as well as the Commission.

It also included industry with 23 firms from financial and professional services whose controls where subject to some scrutiny by the assessors.

The assessment of a jurisdiction against the FATF standards is undertaken in accordance with an established methodology and rating system from the FATF.

The ratings are such that a jurisdiction either complies, largely complies - where there are some minor deficiencies - partially complies because there are major deficiencies or does not comply with a specific FATF recommendation. There is no score which cuts through the middle of being largely complaint on one hand and partially compliant on the other.

It is the compliant and largely compliant ratings which we have aimed for, as special follow up measures can be attached where ratings are partially compliant and non-compliant requiring a jurisdiction to address identified deficiencies.

Where those deficiencies are very serious, public statements about a jurisdiction are issued calling upon countries to treat business emanating from that jurisdiction as high risk - those countries included Iran and North Korea but it has previously included Greece and, as we saw until very recently, for business from Bosnia- Herzegovina which was subject to a public statement from Moneyval.

The Division's work on Moneyval included detailed analysis of the initial findings, lengthy written submissions on earlier versions of the report, liaison with firms who Moneyval met regarding observations that the assessors were making on the application by industry of certain AML/CFT measures and two lengthy meetings with the assessment team in advance of the plenary in September.

The final report will be rather different to the one which was first received.

Although the assessment was against the FATF's 2003 recommendations rather than the later set issued in 2012, it did feel closer to the 2012 standards – not least because the firms they met were asked for copies of their business risk assessments for which it is only under the 2012 standards that the FATF expect jurisdictions to require such assessments by their financial and professional services firms.

The assessment was a follow-up to the IMF's assessment so this time it was against 25 rather than the full 40 recommendations +9 special recommendations for terrorist financing in the 2003 standards.

These 25 recommendations were those considered to be key and core FATF recommendations and those recommendations where Guernsey was rated partially compliant by the IMF in its assessment of the Bailiwick's controls in 2010.

In light of the changed times we are now in, Moneyval also included an assessment of compliance against the FATF standards regarding transparency of beneficial ownership of companies and trusts for which four years ago Guernsey had been rated compliant and largely compliant by the IMF.

Neither are core or key recommendations but it was an opportunity to assess transparency issues on foundations and limited liability partnerships which were added to the Guernsey offering after the IMF's visit.

I would like to assure you that there are no reasons to feel pessimistic about the outcome from Moneyval but it would be unreasonable to expect them not to raise any issues with our regime. For issues which are identified they will require us to report on progress on addressing them in the interim period before the next assessment which is unlikely to take place before 2019.

For example did the revisions which were made to the Handbook rules to address the IMF recommendation in our last assessment, to expand the list of higher risk customers to which ECDD must be applied and to include private banking and non- resident customers, go far enough in Moneyval's eyes?

Moneyval will have embarked upon its assessment with a view to drawing a conclusion on this point together with other areas the IMF raised such as the level of discretionary financial penalties that the Commission can apply and the exemption from fiduciary licensing for individuals holding up to 6 directorships.

Once we are out of this closed period before the publication of the report I will able to explain how we intend to address the recommendations which are made.

I hesitate to use the word opportune but in many ways now is a good time for any such recommendations to be made because we have already started looking at what changes could be made to the regime to bring it into line with the FATF's 2012 recommendations.

In addition, this work is occurring at the same time as many other jurisdictions, including our competitors, are working on updating their regimes against the FATF standards or against the 4th AML Directive, and also when we can look at comparable finance centres. We can also look to other jurisdictions to see what views were expressed in their FATF or Moneyval assessment about a particular topic.

I referred earlier to the IMF's recommendation regarding expanding the list of high risk categories of customer. A similar finding had been made in respect of Jersey which took steps to address this when it decided to update its regime. Clearly the outcome of Jersey's Moneyval assessment will be of interest.

In respect of any corresponding changes to the regulations, the Commission will work with the Policy Council over the changes to be made, the timing for which, including consultation with industry, can hopefully be established now that the Moneyval evaluation has concluded.

As I indicated earlier the revised timing of the Moneyval assessment meant that we had to flex our aims for other work principally in deciding to put on hold the project for wholesale revision to the FSB and PB Handbooks. Instead we advanced a smaller project to update the Handbooks to cover the use of new technologies in the due diligence process.

We will shortly publish the new and revised rules and guidance which will hopefully give firms the confidence to explore whether it is viable to use technologies such as e-certification and e-verification even where this is delivered through apps on smartphones and tablets.

We received some very constructive feedback to our consultation on this during the summer for which I would like to thank you. We hope that the revisions to the Handbook will help those firms wanting to use technology in their client take on process generally and also where firms are considering technology in the delivery of financial products and services.

Generally the revisions we are making are to provide positive affirmation in the Handbooks that this technology can be used but we are stipulating that firms must understand what it is that they want to use and that a determination is made that its use will result in compliance with the regulations and amended rules on customer due diligence.

On this area we did have responses suggesting that the Commission or some other body could approve or vet a technology product or service instead. I appreciate the attractiveness of this but what we require from firms is essentially the same sort of due diligence that would be applied in the consideration of a proposal to outsource an aspect of their compliance controls or business activities.

There is also the matter that our role is to supervise financial services activities and not the systems firms use - we don't vet other systems and software providers.

We will be able to keep a watching brief on the take-up of technology in this area to see if the changes to the Handbooks have had the right effect. We are not asking to be notified by firms that they are about to start using it but we do ask firms in the financial crime risk return if they are using technologies like e-certification and e-verification.

Before I move to the financial crime risk return, we have made one further change to the Handbooks specifically arising from the feedback we had asking us to include the use of online utility bills.

We are including in the revisions new guidance on using online utility bills for verifying the address of Channel Island residents. Some respondents may have wanted this to be wider – but whilst other jurisdictions, including the UK still say no to the use of online utility bills for verification – we decided to allow this for lower risk relationships as a start and will keep an eye on how other jurisdictions address this in changes to their regimes.

As the wider project to revise the Handbook includes recasting it into a new format and structure, the revisions for using technology will be issued at this time as an annex to the existing Handbooks.

Our work centres on assessing the level of financial crime risk that a firm poses. This encompasses consideration of the inherent risk within a firm from the types of clients it has and products and services it offers to the extent to which this is mitigated by the quality of its controls. To this end we launched this year an annual financial crime risk return for all firms to complete.

As we supervise about 1,200 licensees this initiative was only made possible by the development, under the Sentinel project, of online services to collect data and of PRISM to analyse it.

Since the portal's launch a few weeks ago we have been receiving a gradual stream of completed returns. There is a longer lead-in time and staggered submission for this year with a deadline of 30 November for banks and fiduciaries and 31 December for investment, insurance, NRFSB and accountants, estate agents and lawyers. Thereafter the annual date for submission for all will be 31 October.

The data which is coming in from this return is automatically analysed for some universal indicators across all firms in relation to their client base and controls environment. It is principally for supervision and information derived from it is not being publicised but that data will help inform other work we undertake.

We will certainly be using it to assist in determining what themed supervisory work we want to do and upon which sectors we would want to concentrate this activity.

Financial crime risks have long been considered too at the application stage. John Dunford, who is the Deputy Director of the Commission's authorisation unit, is on stage and will be happy to take questions on this.

In essence these risks are assessed as part of the Commission's consideration of an application for a licence or registration. For some time applicants have had to furnish a draft business risk assessment together with their business plan and policies and procedures manual so the Commission can better understand the business proposal and its proposed controls.

This information is in addition to the disclosures in the application form and personal questionnaires which assist us in determining the bona fides of the applicant.

The Commission has, where the applicant has failed to satisfy it that it would meet the minimum licensing criteria, turned down applications in circumstances which include where the applicant could not explain the rationale for the proposed financial activity, where the indicators suggested that the proposals were an aggressive form of tax avoidance and potential exchange control infractions, where the proposed principals to direct the business lacked the requisite experience and expertise, or where the application has been so poorly crafted and the business proposal appeared poorly resourced so as to cause us concerns over how effectively the business will be run.

The onus in the regulatory laws is on the applicant satisfying the Commission that it meets the minimum licensing criteria. Therefore I think I need hardly explain that were we to find a draft business risk assessment which is inadequate or a firm's proposed procedures insufficient for mitigating the risks inherent within its target market, the application is unlikely to succeed.

We have also expanded our supervisory activities this year. Whilst we are on track to undertake onsite visits to 35 firms, we have also begun a programme of meetings with the money laundering reporting officers of our larger firms.

These meetings are held in conjunction with the meetings our colleagues in the relevant supervisory divisions' have with the firm's compliance and risk management representatives. For us these are proving beneficial as a means of taking the temperature on financial crime issues generally for that firm.

We are also undertaking themed work which this year is focusing on the provision of financial crime training by a cross section of firms drawn from every sector – this is presently ongoing and we intend to share the general findings with you next year.

I spoke last year about referrals that we can make to enforcement for investigation and 4 such referrals have been made since then arising from our supervisory work.

This is a referral for further investigation, from which any sanction proposed will depend on the outcome of that investigation.

These are cases where we have identified significant problems in the firm's financial crime controls which often relate to ineffective monitoring arrangements and inadequate risk assessments which jeopardise the firm's ability to identify and manage the risks.

The enforcement division was specifically established to relieve the supervisory divisions of problem cases requiring investigation and where remediation through the enhanced supervisory measures that the supervisory divisions have at their disposal were not viable unless we redirected our resources away from our planned programme of supervision. These referral decisions let us get on and focus on supervising.

We do not take lightly a decision to refer a firm to enforcement for further investigation. Whilst the financial crime division can make a referral directly, decisions are generally made in conjunction with senior staff from the relevant sector division and an independent senior member of the Commission executive.

These decisions are made where the financial crime risk appears to the Commission to be too high to be mitigated by remediation under enhanced supervisory measures which we could set such as requiring certain actions to be taken or commissioning third party reviews.

Before closing I do want to flag that the next Bailiwick project on the agenda for financial crime matters is the national risk assessment.

The FATF has introduced this in its revised standards as the foundation for the application of a risk based approach by a jurisdiction to help it determine where the risks lie and target its resources accordingly.

It therefore follows from that that the outcome of the assessment should feed in and influence the business risk assessments of every firm in the finance sector.

The Policy Council is leading this initiative which is due to commence next year with the aim of completing it before year-end. This involves not only the Bailiwick's AML/CFT agencies but also industry.

Whilst some of the information and data collected for Moneyval is likely to be relevant for this exercise I presently cannot indicate how much work is likely to be involved, however those countries which have been through this – including the Isle of Man - have spoken about how beneficial it has been having industry involvement and I gather too that firms have appreciated the opportunity to participate.

I think Moneyval is an example where the public and private sectors can work together. I hope that when the findings of the report are publicised you too will agree and that going forward such teamwork is replicated when Guernsey embarks on the national risk assessment. I look forward to working with you on that.

We now have some time for questions if you would like to ask John, Steve Chandler who worked extensively on consultation on using technology or myself about our activities this year.

Thank you