



Jersey Financial Services Commission

Trust Company Business Anti-Money Laundering Themed Examination Programme 2007 Summary Findings

Introduction

The aim of the Commission in conducting a series of themed on-site examinations is to concentrate on a specific area of conduct taken across a segment of the industry. For 2007, the chosen theme was anti-money laundering (“AML”) systems and controls. This programme of examinations was undertaken on behalf of the Commission by Deloitte & Touche LLP.

Specifically, the AML themed examination programme was designed to:

- Assess the degree of compliance with the AML regulations which came into force in Jersey on 1 July 1999;
- Identify any potential weaknesses; and
- Highlight areas of best practice.

As with all on-site examinations, a business is assessed in terms of its performance against the relevant laws, orders and codes of practice. The objective in publishing summary findings from a programme of themed examinations is to share experiences as to how different firms seek to meet the requirements of the regulatory regime and to highlight the difficulties that are sometimes incurred.

Scope

The on-site examination focused on five key areas of AML risk management:

- Customer take-on procedures;
- Monitoring outstanding customer due diligence;
- Transaction monitoring;
- Suspicious activity reporting; and
- AML reporting.

Process

A self-assessment questionnaire covering a range of questions, which addressed AML procedures was circulated to a sample of fifty-eight trust company businesses. Responses to the questionnaires were analysed from which a further sample of sixteen trust company businesses was selected for an on-site examination.

Overview

It was encouraging that the majority of businesses examined did record and monitor outstanding due diligence material and that most had completed retrospective due diligence for pre-1999 customers. The majority of businesses managed both internal and external suspicious activity reports (“SARs”) effectively.

However, virtually all businesses struggled to complete prospective transaction monitoring and the Commission believes that controls in this area need to be strengthened in most trust companies.

Whilst it is acknowledged that there are difficulties in automating the transaction monitoring process, it is important that systems are reviewed in order to consider how this could best be achieved. The Commission’s expectations in this regard are that, at the outset of the customer relationship, the profile of the expected activity, both in terms of the value and volume of anticipated transactions, should be clearly defined and documented. As transactions are being processed, they should be compared to the profile so that exceptions to the pattern are highlighted and appropriate action taken, for example, further verification in relation to the transaction may be sought. The transaction profile should be updated on a regular basis. It would be acceptable for parameters to be set so that only transactions above a certain defined value, depending on the profile of the business, will be prospectively monitored.

The Commission was concerned that the review of customer take on procedures highlighted some cases where businesses appeared to have been prepared to facilitate transactions on behalf of customers prior to the full completion of due diligence. In one case, the failure to critically examine the purpose of the offshore structure and the nature of funds flowing through it, exposed the business to risk when the underlying customer was subsequently prosecuted for alleged tax fraud.

The Commission has noted a continued trend of consolidation within the trust company business sector and, in this regard, it is worth noting that acquisition activity poses money laundering risks for the acquirer. This highlights the importance of addressing the differences between AML procedures at entities subject to a merger transaction. The acquirer also needs to consider the profile of the target’s customer base and the impact this may have on its own risk profile. It is important to establish target dates for the alignment of AML policy after an acquisition transaction and for the board of directors to be fully engaged in this process. The resource and cost implications of the harmonisation of AML procedures post merger need to be fully considered. The Commission has observed that, in many cases, this resource requirement is significantly underestimated by the acquirer.

Findings

The observations detailed below have been drawn from on-site findings:

Customer take-on procedures

The customer take on procedures at 25% of the trust companies examined revealed significant deficiencies, principally in relation to the timing of customer payments

versus the completion of due diligence. In one example, the due diligence consisted of extremely poor quality passport copies, (in respect of customers who had not been met in person), no proofs of address and no examination of the source of wealth.

Customer take on forms were not always tailored to define the due diligence requirements for corporate customers or to document the reason that the customer wished to establish an offshore entity.

In one instance, the customer take-on form focused only on administrative matters, rather than comprehensively addressing the customer's background in order to facilitate an assessment of the customer's AML risk profile.

Monitoring outstanding due diligence

94% of the trust companies examined did monitor outstanding due diligence material. However, none of the reports maintained by the trust companies in respect of outstanding due diligence systematically reflected either the ageing or the risk weighting of the outstanding information.

Transaction monitoring

The majority of trust company businesses did not routinely profile customers or monitor customer transactions. In 19% of businesses, transactions were monitored retrospectively. Retrospective transaction monitoring is a useful exercise but it is unable to prevent money laundering transactions.

Transaction monitoring is not a mechanical process and does not necessarily require sophisticated electronic systems to be effective. The key elements of such a system are maintaining appropriate customer profiles to include the value and volume of expected transactions, and asking pertinent questions to elicit reasons for unusual or complex transactions, in order to determine whether there is a risk of money laundering. Inevitably, a high degree of reliance is placed on the knowledge of the individual trust officers and directors who are dealing with customer transactions. This emphasises the importance of ensuring that high quality AML training is provided to all directors and employees of trust company businesses.

Suspicious activity reporting

One trust company business recorded no SARs. All of the remaining trust company businesses that raised SARs collected and evaluated evidence effectively once a suspicion was raised and clearly documented the decision on whether to communicate the suspicion to the Joint Financial Crimes Unit. Most trust company businesses maintained an electronic register of all SARs, which reflected key dates, salient points and the current status of each SAR.

The Commission would query the standard of AML awareness in a business where no SARs are raised.

AML reporting

The boards of all of the trust company businesses examined considered AML issues on a regular basis, although the meeting minutes for some boards were very brief in their coverage of AML matters. Controls could be strengthened by the greater involvement of the board in this respect. The failure of AML procedures presents significant threats to business reputation and viability. The trust business is particularly vulnerable to AML risks and it is important that the board dedicate sufficient time to AML matters as part of an effective risk management strategy.

Examples of best practice

The best due diligence systems record comprehensive source of wealth and source of funds information, which is supported by documentary evidence, for example:

- Information printed from the internet;
- Website links;
- Copies of financial statements of the customer's business; and/or
- Copy of a customer's curriculum vitae demonstrating that he held well paid roles with international organisations throughout his career.

It is best practice to undertake a periodic review of due diligence information depending on the AML risk rating and to maintain a register that reflects outstanding due diligence, including the ageing and risk weighting of the outstanding documentation.

In one example, a trust company updated the due diligence information on an annual basis, which included seeking fresh customer identity documents where necessary, for example if the customer had changed residential address since the last review. This is considered best practice for businesses with a higher than average risk profile.

Conclusion

The Commission recognises that the vast majority of trust businesses are making significant efforts to improve and upgrade their AML systems and controls. In view of the introduction of the new AML regulations during 2008, it is vital that these efforts are maintained. The Commission would urge all trust company businesses to review their procedures with particular emphasis in the area of transaction monitoring.

Given that the lack of transaction monitoring is a repeat finding from both the 2005 and 2006 risk themed examination programme, and in view of the new AML regime being implemented during 2008, the Commission strongly recommends that specific attention is paid to this important area.

Any comments on the contents of this paper would be welcomed. We would also be happy to address any concerns or questions that the reader may have in this respect. Any such communications should be addressed to:

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