



ISLE OF MAN
FINANCIAL SERVICES AUTHORITY

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ISLE OF MAN TRUST AND CORPORATE SERVICE PROVIDER THEMATIC REPORT

BUSINESS RISK ASSESSMENT PHASE 2 – INSPECTIONS

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Colour key used in this document:

AML/CFT Code 2019

AML/CFT Handbook

AML/CFT TCSP BRA Thematic Data

Best Practice

1 Glossary of terms

<u>TERM</u>	<u>MEANING IN THIS REPORT</u>
AML/CFT	Anti-Money Laundering/Countering the Financing of Terrorism
Authority	The Isle of Man Financial Services Authority
BRA	Business Risk Assessment
CDD	Customer Due Diligence
Code	The Anti-Money Laundering/Countering the Financing of Terrorism Code 2019
CRA	Customer Risk Assessment
FC	Financial Crime
Handbook	The Anti-Money Laundering/Countering the Financing of Terrorism Handbook
HNWI	High Net Worth Individual
Licenceholder	Licensed Entities
ML/FT	Money Laundering/Financing of Terrorism
NPO	Non-Profit Organisation
NRA	National Risk Assessment
PF	Proliferation Financing
Relevant Person	Means a person carrying on business in the regulated sector which is included in paragraphs 2(6)(a) to (t) of Schedule 4 to the Proceeds of Crime Act 2008
Registered Person	Means a person registered under section 9 of the Designated Businesses (Registration and Oversight) Act 2015
Regulated Person	Refers to firms regulated under the Financial Services Act 2008
TCSP	Trust and Corporate Service Provider
TRA	Technology Risk Assessment

2 Background

2.1 Executive Summary

The Authority has completed a thematic project involving TCSPs on the Island. The Authority initially gathered data and information on Class 4 (Corporate Services) and Class 5 (Trust Services) licenceholders, concluding a thematic project would be valuable to further connect and work with the sector. This has allowed and enabled the Authority to gather further data, assisting in risk assessing the firms and sector, as well as building knowledge and findings to be fed back into the Handbook, the sector specific guidance and the NRA.



The Authority’s regulatory objectives are:

- securing an appropriate degree of protection for policyholders, members of retirement benefits schemes and the customers of persons carrying on a regulated activity;
- the reduction of financial crime; and
- the maintenance of confidence in the Island’s financial services, insurance and pensions industries through effective regulation, thereby supporting the Island’s economy and its development as an international financial centre.

A key part in achieving these objectives is the Authority’s oversight and supervisory functions, which encompass undertaking supervisory inspections and thematic reviews.

The planning for the thematic began in 2022 and the background was

shared in a press release issued on the Authority’s website on 20 December 2022. The thematic exercise consisted of two core phases. Phase 1 consisted of data collection and analysis in regard to business risk assessments (“BRAs”), with a **BRA questionnaire** being issued to 106 TCSP licenceholders for completion. A report which outlines the results of Phase 1, as well as the Authority’s observations on the data and some subsequently identified best practice points in relation to the BRA, was published on 12 July 2023 and **can be found here**.

Phase 2, which commenced in February 2023, consisted of 70 desk-based inspections of TCSP licenceholders focusing on the BRA and their compliance with paragraph 5 of the Code. This phase of the project concluded in October 2023, with an individual inspection report issued to each firm inspected.

This overarching report outlines the

results from Phase 2 of the project, highlighting some learning points and areas of best practice.

A relevant person’s BRA is vital to evidence their understanding of the risks they face. It is also a key tool in order to establish and document a robust compliance and risk management framework to detect and prevent ML, FT, FC and PF. The BRA should serve a purpose and must be used by the business to inform its approach to AML/CFT frameworks and mitigation. It must be continuously worked upon and reviewed when circumstances change or new threats emerge. It is important for the business functions and BRA to work together in a continuous feedback loop in order to be effective. Relevant persons should also consider for each risk factor recorded within the BRA whether they should be calibrated or weighted differently, dependent on how the relevant person’s assesses each of the various factors.

We hope this report will assist firms in assessing their ML/FT risks when reviewing and/or updating their BRA, and we would like to thank the firms involved in participating in the completion of this thematic.

Phase 2 consisted of 70 desk-based inspections of TCSP licenceholders

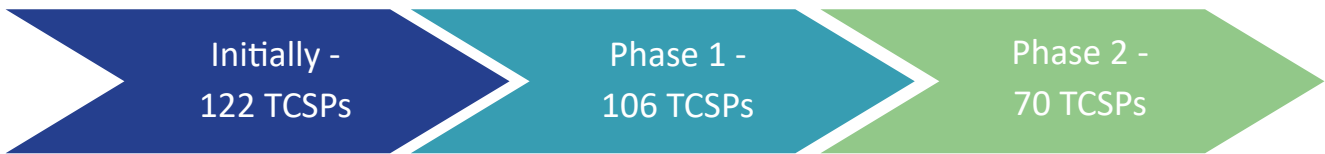
2.2 Thematic Scope

Initially, the project consisted of collating and analysing existing data from all 122 TCSPs licensed at the time, and narrowing these to form Phase 1 of the TCSP BRA thematic. In considering TCSPs to form part of Phase 1 of the thematic the Authority excluded relevant persons, at the time, for a number of various reasons, which included firms that were in liquidation or actively surrendering their licence(s). This meant, out of the 122 TCSPs, 106 firms were selected to form Phase 1 of the thematic.

After further analysis of the Phase 1 outcomes, 70 relevant persons were selected to take part in Phase 2 of the

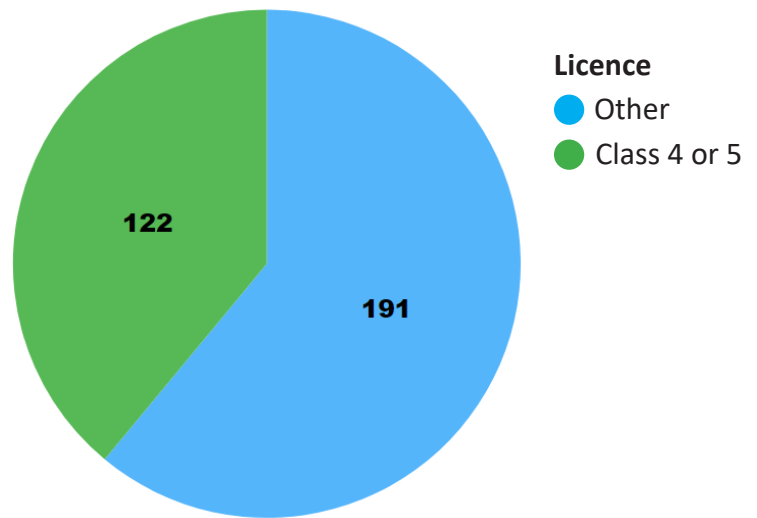
thematic project, which comprised desk-based inspections. Overall, some of the factors determining the relevant persons to take part in Phase 2 included consideration of the following:

- Phase 1 questionnaire outcomes;
- Recent supervisory inspections (e.g. thematic, desk-based or on-site); and
- Data collected by the Authority from relevant persons' AML/CFT annual statistical returns in recent years against the prescribed risk parameters.



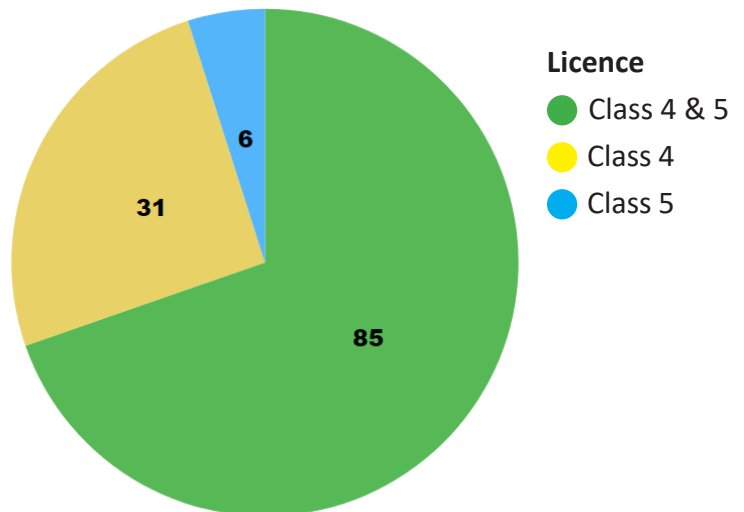
Breakdown of number of the Authority's regulated licenceholders who hold a Class 4 or a Class 5 licence;

- Total relevant persons – 313
- Class 4 or 5 licenceholders – 122
- Relevant persons who do not hold a Class 4 or 5 licence – 191



The data split from the Authority's public register of the 122 Class 4 or Class 5 licenceholders as at December 2022;

- Class 4 & 5 – 85
- Class 4 – 31
- Class 5 – 6



2.3 AML/CFT Code 2019 - BRA Obligations

5 Business risk assessment

(1) A relevant person must carry out an assessment that estimates the risk of ML/FT posed by the relevant person's business and customers.

(2) The business risk assessment must be —

(a) undertaken as soon as reasonably practicable after the relevant person commences business

(b) recorded in order to demonstrate its basis; and

(c) regularly reviewed (details of any review must be recorded) and, if appropriate, amended so as to keep the assessment up-to-date.

(3) The business risk assessment must have regard to all relevant risk factors, including —

(a) the nature, scale and complexity of the relevant person's activities;

(b) any relevant findings of the most recent National Risk Assessment relating to the Island;

(c) the products and services provided by the relevant person;

(d) the manner in which the products and services are provided, including whether the relevant person meets its customers;

(e) the involvement of any third parties for elements of the customer due diligence process, including where reliance is placed on a third party;

(f) customer risk assessments carried out under paragraph 6; and

(g) any technology risk assessment carried out under paragraph 7.

Handbook quote

2.2.8 Business risk assessment

The purpose of a BRA is to assist relevant persons to understand where, how and to what extent they are exposed to ML/FT risk and which areas of their business they should prioritise in combatting ML/FT.

The BRA should form the basis of a relevant person's risk based approach and its risk appetite making clear the types of risk and the risk level the relevant person is prepared to accept.

It is the necessary foundation for determining the nature and extent of AML/CFT resources and should be used to inform the policies, procedures and controls to mitigate ML/FT risk, including decisions on the appropriate level and type of CDD to be applied in specific situations to particular types of customers, products, services and delivery channels.

The Code sets out the minimum legal obligations for relevant persons to meet in order to try to prevent ML/FT/PF and to evidence how they do so. Paragraph 5 of the Code mandates the requirements relevant persons must adhere to in regard to their BRAs. The Authority's AML/CFT Handbook provides information and guidance to help relevant entities consider their obligations, with Section 2.2.8 offering further guidance on carrying out a BRA required under the Code.

In line with paragraph 5 of the Code, relevant persons are required to

carry out an assessment that estimates the risk of ML/FT/PF posed by the relevant person's business and customers.

It is important to note that when a relevant person is estimating the risk of FT, this should also include

the financing of proliferation, as prescribed in paragraph 3 of the Code and is to be construed in accordance with the definitions of "financing", "terrorism" and "proliferation" in section 3 of the Terrorism and Other Crime (Financial Restrictions) Act 2014.

When estimating the risk of financial terrorism, it is important to include the financing of proliferation

Good practice in relation to conducting a BRA includes ensuring the document:

- Clearly sets out the risks the firm faces in relation to customers and their activities and explains the basis of the assessment;
- Is tailored to the business and the specific risks of that particular firm;
- Is informed by other risk assessments required by the Code, including the Island's NRA;
- Provides detail on the customer base highlighting where key risks lie;
- Has input from subject or product experts from across the business;
- Is evidenced as reviewed and signed off by senior management at regular intervals;
- Is shared with staff across the organisation so they can understand the ML/FT risks faced;
- Has good version controls (and dated versions);
- Clearly articulates how much, and what level of, risk the firm is prepared to take; and
- Details what risk the firm is not prepared to take.

3 Phase 2 - BRA Inspections

3.1 Scope

The primary objective of the BRA TCSP thematic project was to review each firm's BRA documentation, and to determine if the BRA adequately and appropriately demonstrated that it met the requirements of the Code.

Paragraphs 4 (Procedures and controls) and 30 (Monitoring and testing compliance) were also considered by the Authority where appropriate.

As part of this thematic inspection process, the firms involved in Phase 2 were given three working days to supply the requested documentation to demonstrate and evidence compliance with the inspection's scope of the Code.



The objectives of the desk-based inspections included the following:

- **Objective 1:** Review the business risk assessment considering paragraph 5(1) of the Code.
- **Objective 2:** Review the business risk assessment considering paragraph 5(2) of the Code.
- **Objective 3:** Review the business risk assessment considering paragraph 5(3) of the Code.

3.2 Overall Results and Key Findings

Detailed analysis of the results and outcomes from the thematic project in relation to paragraph 5 of the Code are analysed within section 3.3 of this report.

The Authority has identified that whilst the majority of firms provided the requested information in full and in a prompt manner, a very small number of firms failed to supply the correct and/or all of the requested information in the first instance.

The Authority strongly encourages all firms to maintain an organised, well titled and labelled accessible library of policies, procedures, documents and evidence in order to best be in a position to supply these to the Authority in a timely manner in order to be able to facilitate the inspection.

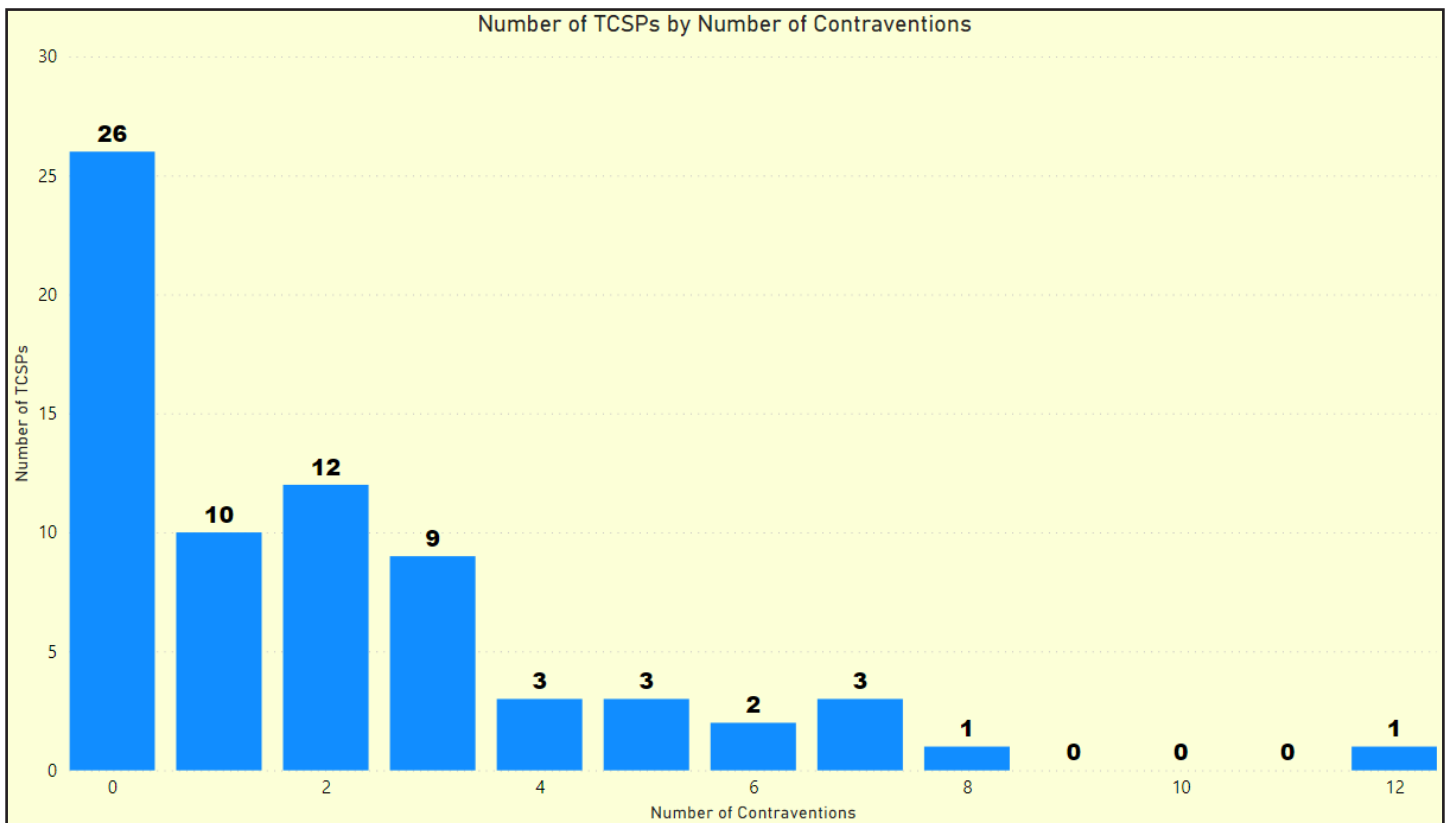
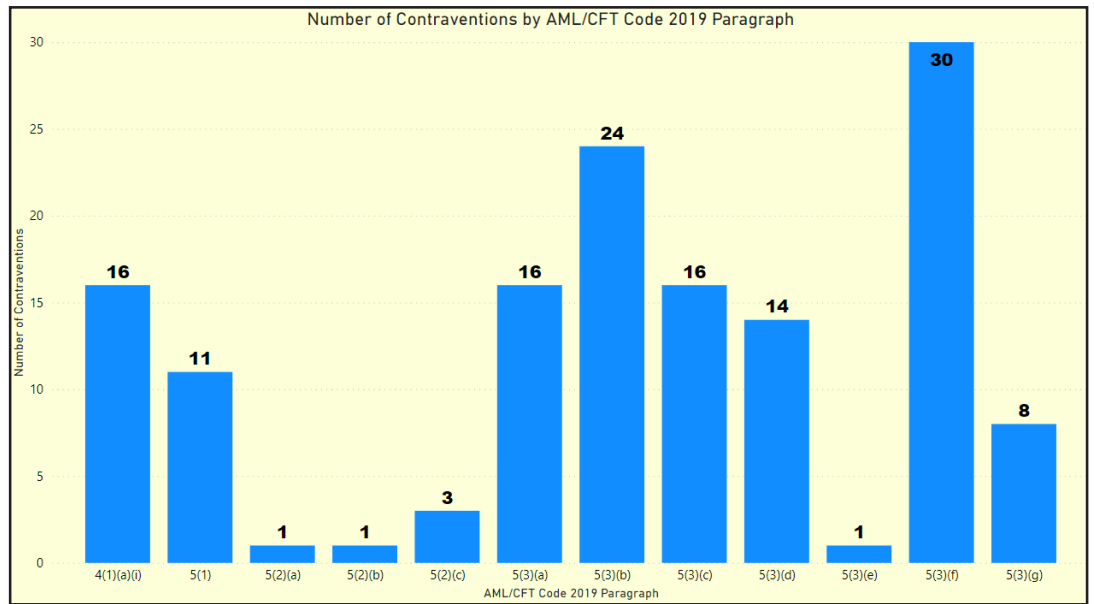
Additionally, this will also ensure the material is more accessible and used

effectively by firms' own staff.

Following analysis of the outcomes from the BRA inspection reports, and considering the type of contraventions identified, the Authority has noted that out of the total 70 inspections, the two most common contraventions identified were paragraphs 5(3)(f) and 5(3)(b) of the Code. The Authority's officers observed a

number of trends from the project, with firms varying in the level of detail or regard given to the various factors required by the Code.

Overall, the Authority has determined that out of the 70 inspections conducted, the majority of firms inspected¹ had zero or fewer than two specific Code paragraph contraventions identified.



3.3 Key Findings: Paragraph 5 of the Code

3.3.1 Paragraph 5(1) of the Code

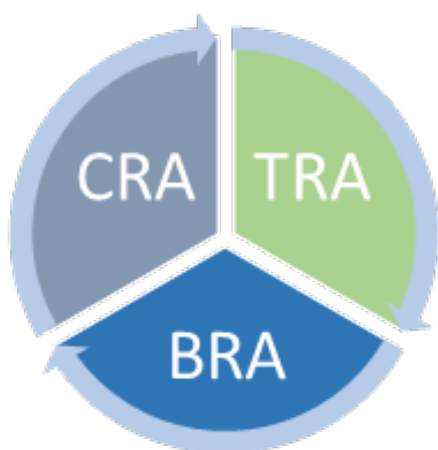
Paragraph 5(1) of the Code

5 Business risk assessment

(1) A relevant person must carry out an assessment that estimates the risk of ML/FT posed by the relevant person's business and customers.

84%

Compliance
with 5(1)
of the Code



The first objective of the inspections was to consider paragraph 5(1) of the Code. Per the Handbook, the BRA should be a firm's key risk management tool that effectively assesses and documents the firm's estimation of the ML/FT risks posed by its business and customers. The BRA can then, in turn, inform the policies, procedures, and controls that the firm implements to mitigate the ML/FT risks it has identified.

The BRA, CRA and TRA are interconnected, with each type of risk assessment informing the other.

Furthermore, they are the vital base by which to determine a relevant person's risk appetite and build a risk sensitive AML/CFT framework including mitigation procedures and controls, such as CDD procedures. Mitigation procedures and controls must flow from the results of the risk assessments, but equally, information gained when operating mitigation procedures and controls, such as for CDD and monitoring, should feedback into risk assessment considerations. Risk assessments and mitigation measures are in a continuous feedback loop.

Handbook quote

2.2.8 Business risk assessment

The purpose of a BRA is to assist relevant persons to understand where, how and to what extent they are exposed to ML/FT risk and which areas of their business they should prioritise in combatting ML/FT.

The BRA should form the basis of a relevant person's risk based approach and its risk appetite making clear the types of risk and the risk level the relevant person is prepared to accept.

It is the necessary foundation for determining the nature and extent of AML/CFT resources and should be used to inform the policies, procedures and controls to mitigate ML/FT risk, including decisions on the appropriate level and type of CDD to be applied in specific situations to particular types of customers, products, services and delivery channels.



The BRA informs the policies, procedures and controls that firms implement to mitigate ML/FT risks

Per paragraph 5(1) of the Code, relevant persons are required to carry out a BRA that estimates the risk of ML/FT, including PF, posed by the relevant person's business and customers. A relevant person must document the consideration of its ML/FT risks pertaining to its services/products, customers, jurisdictions and distribution channels, being mindful of the nature, scale and complexity of its business model.

The BRA should be appropriate and proportionate in relation to the nature of the relevant person and its activities, ensuring it is tailored and specific to the business. Where relevant persons rely on a group BRA, they should ensure the BRA is suffi-

ciently granular, clearly making reference to each and every identified risk factor for all licenceholders included within the group.

The adoption of a joint or group BRA must still demonstrate that each licenceholder has carried out an assessment that estimates the risk of ML/FT, ensuring consideration is given to all regulatory permissions and jurisdictions where applicable.

The Authority's officers observed a range of risk matrices and methodologies used to estimate risk within BRAs. Some approaches were simpler, and others were more complex with multiple layers of analysis and reasoning; this range reflects

the fact that the nature, scale, and complexity of each firm is different. Although there is no one recommended or best approach, relevant persons should clearly document and explain the method used, and ensure the outcomes are understood.

Using a wide range of scoring mechanisms will allow firms to accurately assess and separate risks, increasing their understanding of priority and urgency. Additionally, using and applying different weightings for specific risk factors or risk sections is an advanced and useful tool in risk management.

An accurate and useful BRA will also assist firms in efficient and effective resource allocation or future planning. A summary of the scoring and outcomes from the BRA within a conclusion is an identified best practice for demonstrating compliance with paragraph 5(1) of the Code.

Relevant persons should clearly document and explain the method used



Case Study 1: In the case of one BRA review, the Authority's officers saw evidence of a detailed risk methodology. The risk factor sections of the BRA were expanded further and beyond those prescribed in the Code. Each risk factor section was given total inherent and residual risk scores, from a smaller formula/calculation from within each section.

Both risk scores for all risk factor

sections were plotted onto a clear heat map to demonstrate the controls and considerations given, and the subsequent effect and mitigation.

This also allowed the firm to focus resources and time to where the firm believed their highest risks were, affecting and influencing other areas of the business and the level of controls and oversight applied.

BRA Risk Matrix - Best Practice

- Clearly documenting and using a well-designed matrix and methodology;
- Weightings of each risk factor considered;
- Both inherent and residual risk scores used and explained;
- Considers more than just the risk factors prescribed in paragraph 5(3) of the Code;
- Includes a summary or conclusion of risk factors; and
- Results in a risk rating for that particular business that assesses / determines their overall vulnerability to ML/FT.

An example of a risk matrix table can be seen below.



Risk Matrix			Likelihood / Probability				
			Very Low	Low	Medium	High	Very High
			2	4	6	8	10
Impact / Severity	Very Low	2	4	8	12	16	20
	Low	4	8	16	24	32	40
	Medium	6	12	24	36	48	60
	High	8	16	32	48	64	80
	Very High	10	20	40	60	80	100

3.3.2 Paragraph 5(2) of the Code

Paragraph 5(2) of the Code

5 Business risk assessment

(2) The business risk assessment must be —

- (a) undertaken as soon as reasonably practicable after the relevant person commences business;
- (b) recorded in order to demonstrate its basis; and
- (c) regularly reviewed (details of any review must be recorded) and, if appropriate, amended so as to keep the assessment up-to-date.

Handbook quote

2.2.8.2 Timing of the BRA

All existing relevant persons must already have undertaken a BRA. Newly licensed or registered relevant persons must undertake the BRA before entering into or carrying on a business relationship/occasional transaction.

92%

Update the BRA when a material event occurs

The second objective of the inspections was to consider paragraph 5(2) of the Code. Overall, the Authority's officers observed high levels of compliance in relation to paragraph 5(2) of the Code throughout the thematic. Per the Handbook and Code, all firms must undertake a BRA as soon as reasonably practicable after commencing business; this must be documented and recorded in order to evidence its basis and compliance.

86%

Update the BRA every year

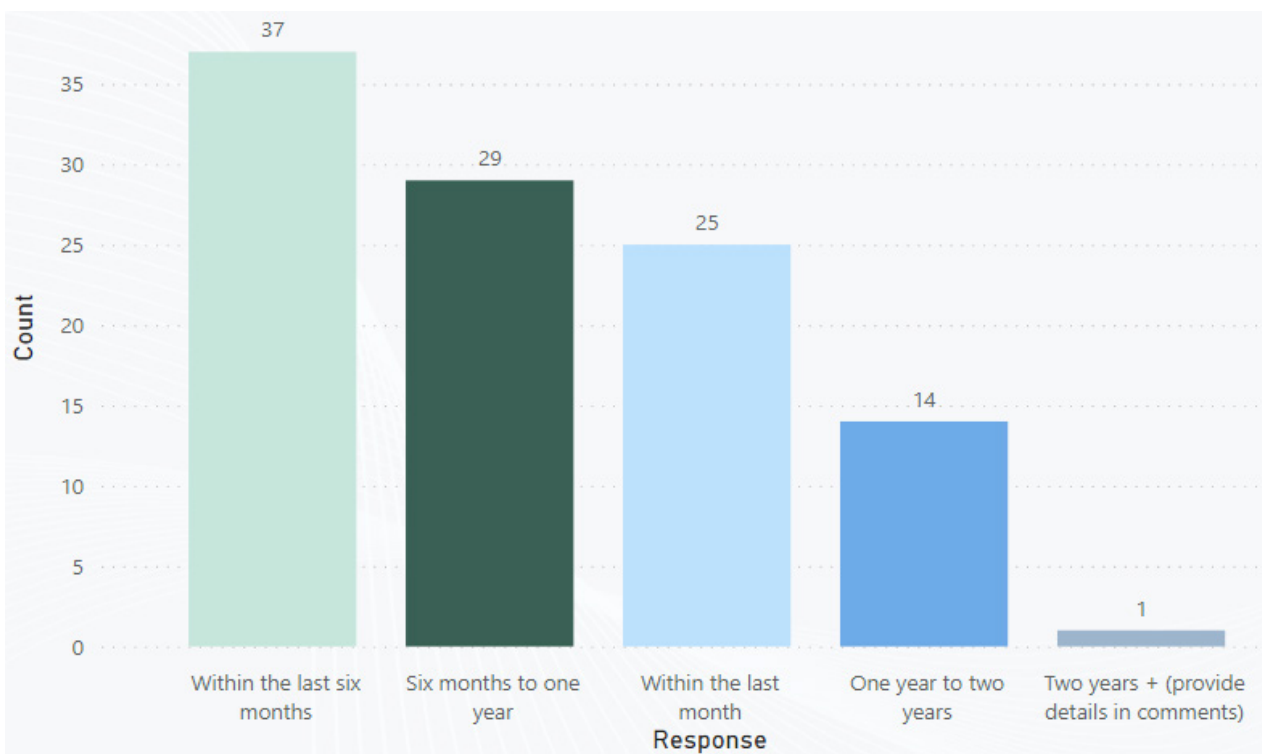
18%

Update the BRA every quarter

In the Phase 1 BRA questionnaire, 92% of firms stated that the BRA would be updated when an internal or external material event occurs, and 86% would update the BRA every year. Furthermore, 42% of firms confirmed they had reviewed/updated the BRA following a material event.

42%

Had a material event occur in the last year that changed the BRA



Graph from question 9, “When was the BRA last approved?” from the Phase 1 TCSP BRA report

In considering paragraph 5(2)(c) of the Code, the Authority’s officers also considered firms’ compliance with paragraph 4(1)(a)(i) of the Code. A common trend of what would be considered poor practice observed by the Authority’s officers was the following: firms stating in their own procedures and controls that the BRA would be reviewed and updated at least yearly/annually, and additionally when internal or external material events occur (detailed in the Phase 1 questionnaire).

The Authority’s officers then saw in some instances during the Phase 2 inspections that some firms would only document and evidence reviews or updates of the BRA within a given calendar year. However, these reviews were seen to be up to 23 months apart (e.g. January 2021 to December 2022). This extended time gap between BRA reviews is not viewed as in-keeping with those relevant persons’ documented procedures and controls defining yearly/annual reviews. As a matter of best practice, firms should better utilise and document ad-hoc, triggered or focused reviews, updates, and amendments to the BRA as the

business, customers, or risks develop and change. Particularly being flexible where there might be external events outside of the firm’s control.

The Authority’s officers also observed some cases where the firm’s definition of material events was very limited in scope; with some firms only considering this to be customer details changing or additional products and services being provided, this then resulting in a fewer material events ever happening. Relevant persons may therefore want to consider and review their BRA when material risk events occur from various local or global events that may affect the AML/CFT risks posed to the business, this including for example updates to the AML/CFT Code, FATF lists, or Sanctions. A detailed version control/history contained within the BRA document is an effective way to demonstrate compliance with paragraph 5(2)(c) of the Code. Whilst the majority of the BRAs reviewed were dated or had a version number, many

did not contain a detailed version or change history. A version history allows the relevant person to easily display and track compliance with the Code from the inception of the business or since the AML/CFT Code 2015, which came into operation on 1 April 2015. Reviews and updates of the BRA can then be further evidenced via retained copies of the BRAs and Board or senior management meeting minutes.

A point of poorer practice identified by the Authority’s officers was starting a new version control/history when there is a re-write, restructure, or a new approach to the BRA. The version history of a document, including the BRA, should never be deleted, even when a large or significant change happens; instead the change or update should be documented within the version history. Code paragraphs 33 and 34 set out the records to be kept and how long they must be retained.

A detailed version control/history is an effective way to demonstrate compliance

Version Control - Best Practice (Anonymised Example)

Version	Reviewer / Updater	Reviewer Role	Reviewer Date	Amendment	Approver	Approver Role	Approver Date
1.0	Jane Kelly	Head of Compliance	01/06/15	Annual review: updates sections 1, 8 & 16	James Kneale	Director	02/06/15
1.1	John Quayle	Compliance Officer	01/08/15	Amendment regarding customer base in sec. 9	Jane Kelly	Head of Compliance	04/08/15
2.0	Jane Kelly	Head of Compliance	01/06/16	Annual review: small amendments throughout	James Kneale	Director	03/08/16

The BRA should be considered a living, ever-changing, and ongoing document, which utilises recent data, findings and trends from the business and its customers, but also documents and describes the current controls, mitigations, risks and threats to and in the relevant person's business.

The Authority expects that the Board or senior management's sign-off and approval of the BRA is fit for purpose and current for use from the sign-off/approval date forward, so the business can include and use any new or improved aspects from that point onwards. Retrospective sign-off/ approval is not compliant with the Code.

In isolated instances seen, the BRA for the year 2022 (for use in 2022-23) was not approved by the Board until



mid-2023. Therefore, as a matter of best practice, it is recommended that firms do not backdate the sign-off/ approval of the BRA, but instead the sign-off and approval of a BRA is to be

used from the specific approval date moving forward, and ensure regular reviews and any amendments are clearly documented in minutes and version controls.

Paragraph 5(2) - Best Practice

- The BRA is clearly documented and dated with a detailed version history dating back to when the relevant person commenced business or the 2015 Code;
- Includes details of the staff members who have been involved in drafting the document;
- Is regularly reviewed in line with the relevant person's procedures and controls;
- Is reviewed and signed off by the Board or senior management on a regular basis and in line with the relevant person's procedures and controls; and
- Updates to BRA are undertaken on an ad-hoc basis, as and when risk factors occur from various local or global events that may affect AML/CFT or ML/FT risks posed to the business.

3.3.3 Paragraph 5(3) of the Code

The third objective of the inspections was to consider paragraph 5(3) of the Code. The Authority’s officers saw mixed levels of compliance in relation to paragraph 5(3) of the Code throughout the thematic project; however, generally, more positive than negative outcomes were observed.

All the risk factors prescribed in paragraph 5(3) of the Code must be fully considered, assessed, and mitigated as appropriate, with the analysis clearly documented and articulated within the BRA.

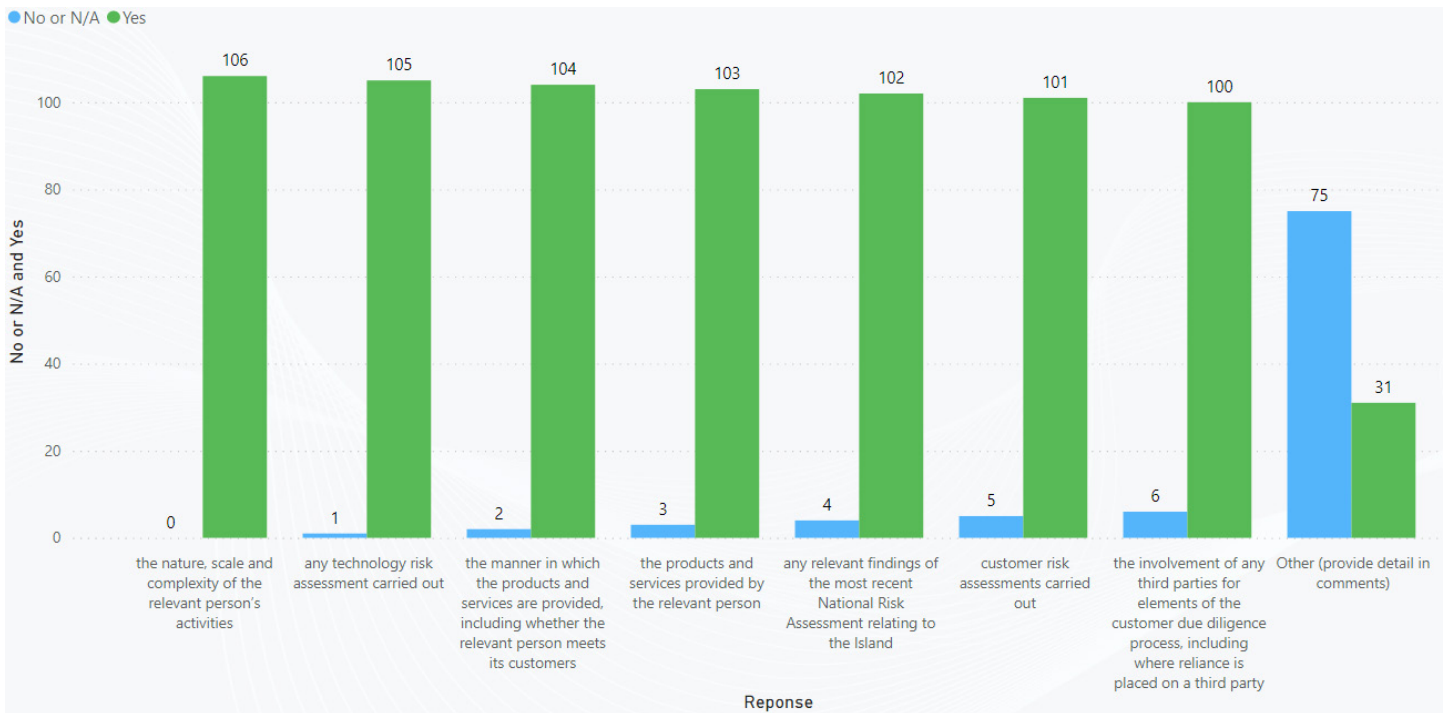
However, this list is not exhaustive and firms should consider, document and assess all relevant risk factors that expose the relevant person to ML/FT risk, even if not expressly included in paragraph 5(3).

Paragraph 5(3) of the Code

5 Business risk assessment

(3) The business risk assessment must have regard to all relevant risk factors, including —

- (a) the nature, scale and complexity of the relevant person’s activities;
- (b) any relevant findings of the most recent National Risk Assessment relating to the Island;
- (c) the products and services provided by the relevant person;
- (d) the manner in which the products and services are provided, including whether the relevant person meets its customers;
- (e) the involvement of any third parties for elements of the customer due diligence process, including where reliance is placed on a third party;
- (f) customer risk assessments carried out under paragraph 6; and
- (g) any technology risk assessment carried out under paragraph 7.



Graph from question 14, “What factors are considered when determining the business’ exposure to ML and FT risk?” from the Phase 1 TCSP BRA report.

87%

Of firms stated they considered all risk factors prescribed in paragraph 5(3) of the Code

29%

Of firms stated they consider risk factors other than those prescribed in paragraph 5(3) of the Code

There were 14 different firms that answered either “No” or “N/A” in response to whether they consider one or more of the risk factors prescribed in paragraph 5(3) of the Code (question 14 of the Phase 1 BRA questionnaire).

Only 87% of the 106 firms considered all the required risk factors of para-

graph 5(3). The Authority would like to highlight that all relevant persons must have regard to each of the risk factors prescribed in the Code and ensure they are suitably documented. Encouragingly, 31 firms confirmed that their BRA considers risk factors other than those prescribed in paragraph 5(3) of the Code. Each firm’s

BRAs should be tailored, unique and relevant to the firm’s specific business, customers and risks.

In order to have a comprehensive BRA, it is beneficial for firms to also document their regard for and consideration of risk factors other than those prescribed in paragraph 5(3) of the Code.

Paragraph 5(3)(a) of the Code

5 Business risk assessment

(3) The business risk assessment must have regard to all relevant risk factors, including —

(a) the nature, scale and complexity of the relevant person’s activities

Paragraph 5(3)(a) of the Code requires that the BRA must have regard to the nature, scale, and complexity of the relevant person’s activities. Whilst the vast majority of firms were compliant with this paragraph of the Code, the Authority’s officers observed that many firms could further enhance the detail relating to this factor to better demonstrate compliance with the Code. As a prescribed relevant risk factor of the Code with a fairly

wide scope, relevant persons should always ensure that they sufficiently and adequately detail their assessment of all aspects, identifying and documenting all potential risks posed to the business in relation to this risk factor within their BRA.

Firms should consider and document within their BRA how their business might be abused for ML/FT, and the controls and measures in place to combat and prevent criminals and

misuse. In some cases, firms only documented a high-level general overview of the business, failing to identify and document the ML/FT risks and vulnerabilities associated with their unique business, customers, products and services.

Providing a small or non-specific narrative of a firm in its business sector is not sufficient to comply with the Code and is not in-keeping with the Handbook. Other global sources, such as FATF and the World Bank, can provide helpful insight into the potential risks posed by relevant persons in the TCSP sector and the unique products and services offered.

79%

Compliance with 5(3)(a) of the Code

FATF and the World Bank can provide helpful insight into potential risks

Paragraph 5(3)(a) - Best Practice

The BRA should provide narrative on, consider and assess the risks in regard to:

- The relevant person's structural factors (this including whether the relevant person is a standalone operation or part of a group, management structures within the firm, any outsourcing factors, etc.);
- The volume and size of the relevant person's transactions;
- The scale on which products and services are provided; and
- How the services provided can be used for ML/FT.

Paragraph 5(3)(b) of the Code

5 Business risk assessment

(3) The business risk assessment must have regard to all relevant risk factors, including —

(b) any relevant findings of the most recent National Risk Assessment relating to the Island

67%

Compliance
with 5(3)(b)
of the Code

Paragraph 5(3)(b) of the Code requires for the BRA to have regard to any relevant findings of **the Island's latest NRA**. The NRA determines the overall risk of ML posed to the TCSP sector to be Medium High, taking into account the threats and vulnerabilities, balanced against the controls in place in the sector; the overall risk for FT is noted as Medium.

Some of the key facts and information from the NRA relating to the TCSP sector that could be compared with, considered and documented within a TCSP's BRA include the following:

- 30,000 client companies (approximately 60% are incorporated in the IoM and 40% elsewhere);
- 16,750 trusts;
- wide international reach, TCSPs will have customers from higher risk jurisdictions and beneficial owners with a higher risk profile;
- 5.5% of client companies or trusts are involved with PEPs, compared with an average of 2% across the whole IOM financial services industry;
- at the time of the NRA TCSPs typically had 20% of clients rated by the firm as being of higher risk; and
- the high number of suspicious activity reports ("SARs") within the sector, with TCSPs submitting 9% of SARs in 2017/18.

In order to best demonstrate compliance with paragraph 5(3)(b) of the Code, the BRA should have regard to a number of relevant identified vulnerabilities from the

NRA. Some vulnerabilities detailed in the NRA relating to the TCSP that could be considered, documented and assessed within a TCSP's BRA include:

- non face-to-face business relationships and reliance on third parties;
- corporate and trust structures which can be complex in nature; this is a legitimate activity but complexity provides the opportunity to disguise beneficial ownership, the source of funds and the activities of the entities concerned;
- vehicles could be used to carry out one or more of the components related to trade based money laundering;
- high value assets such as property, yachts and aircraft are attractive to HNWI and PEPs, some of whom may be seeking to invest the proceeds of corruption;
- misuse of vehicles to evade tax;
- the operation of, or sending money to, charities or other NPOs that are actually front organisations;
- companies which operate or run websites / social media accounts to distribute material supporting terrorism;
- companies which are used to channel funds by more sophisticated groups; and
- the exports of materials or natural resources e.g. historic artefacts, oil, diamonds, etc. to raise funds for terrorism.

Paragraph 5(3)(b) - Best Practice

- The BRA notes the ML/FT risk scoring of the relevant sector as denoted in the NRA;
- The BRA clearly considers, references and assesses the vulnerabilities detailed within the NRA;
- Consideration is given to the impact the detailed vulnerabilities have on the relevant person; and
- The BRA details the mitigation in place by the relevant person in relation to those vulnerabilities.

In a number of the BRAs reviewed, the Authority's officers noted that the detail around this risk factor could be enhanced, with further analysis and assessment provided on the vulnerabilities facing the TCSP sector, the impact those vulnerabili-

ties have on the relevant person, and the mitigation in place. Where relevant persons have contravened this paragraph of the Code, this was as a result of not having any regard to this risk factor or providing very little narrative around it.

Detail around the risk factor could be enhanced



Case Study 2: The Authority's officers observed a strong example of compliance with this paragraph of the Code whereby an NRA sub-section was included within the BRA.

This section of the BRA was structured in a tabular format with additional commentary provided. The table detailed a number of NRA observations, the position of the relevant person, and commentary on

how the firm compares to the NRA with some mitigating comments.

Each observation listed also highlighted whether the firm exhibits a lower, higher or consistent risk profile than that determined in the NRA. The firm then highlighted the TCSP ML/FT final risk ratings as detailed in the NRA, also providing a conclusion on how they compare to the NRA.

Paragraph 5(3)(c) of the Code

5 Business risk assessment

(3) The business risk assessment must have regard to all relevant risk factors, including —

(c) the products and services provided by the relevant person

77%

Compliance
with 5(3)(c)
of the Code



In line with paragraph 5(3)(c) of the Code, the BRA must document and assess the ML/FT risks associated with the relevant person's specific products, services and transactions².

The Authority's officers have identified that whilst most of the BRAs reviewed provided commentary around the products and services provided, in a small number of cases reviewed the BRA did not sufficiently split out the different products and services provided, and instead provided a high-level commentary around this without having regard to the relevant person's transactions. In some instances, the BRA did not adequately assess the ML/FT risks associated with the relevant person's products, services and transactions.

In accordance with the Handbook,

when identifying and assessing the ML/FT risks associated with a relevant person's products, services and transactions, consideration should be given to the risks related to:

- the level of transparency, or opaqueness of the products, services or transactions;
- the complexity of the products, services and transactions;
- the extent to which the products or services allow payments from third parties or accept overpayments;
- the risks associated with new or innovative products and services, in particular where this involves the use of new technologies or payment methods; and

Handbook quote

The products and services provided by the relevant person and associated transactions

Though not specifically listed in the Code, this section also covers transactions associated with products and services provided by relevant persons.

- the value or size of the products, services or transactions.

Section 2.2.8.3 of the Handbook provides further detail around the potential ML/FT risks associated with certain products, services and transactions.

Case Study 3: A strong example of compliance observed by the Authority's officers in relation to this paragraph of the Code included the BRA having a separate "Products and services provided" section, which specifically listed all the vehicles used in structures managed/provided by the relevant person.

The BRA clearly identified and listed how these products and services may be misused for illegitimate means, and provided mitigating factors on how the relevant person would manage the risks identified.



The BRA identified those relationships that may carry an increased risk, and commented on the transactional activity and how this is managed.



Paragraph 5(3)(c) - Best Practice

- Detailed narrative is provided on the different products and services provided by the relevant person;
- Regard is given to the transactions associated with the products and services provided by the relevant person;
- Consideration and analysis of the ML/FT risks associated with the relevant person's products, services and transactions.

² Regarding paragraph 5(2)(c) of the Code, the Handbook details the following - 'Though not specifically listed in the Code, this section covers transactions associated with products and services provided by relevant persons'

Paragraph 5(3)(d) of the Code

5 Business risk assessment

(3) The business risk assessment must have regard to all relevant risk factors, including —

(d) the manner in which the products and services are provided, including whether the relevant person meets its customers



Paragraph 5(3)(d) of the Code requires the BRA to have regard to the manner in which the products and services are provided to customers, including whether the relevant person meets its customers. In order to best evidence compliance with this risk factor, firms may wish to include statistical data within the BRA, of the various manners in which introductions are and ongoing business relationships are conducted by the firm. As per the Handbook, this risk factor concerns how the business relationship/occasional transac-

tion is conducted. Relevant persons should document and evidence its assessment of and regard to this risk factor, which covers aspects such as:

- the extent that the business relationship is conducted non-face-to-face;
- the risks that may arise from non-face-to-face delivery and the mitigating factors of these relationships;
- whether introducers or intermediaries are used and the nature

of use, considering the ML/FT risks of this and the outputs of any Introducer Risk Assessments³ carried out;

- whether the customer themselves may be an undisclosed intermediary for a third party;
- where products, services or payments are to be provided to or from third parties; and
- the way technology is used in delivering products and services.

Paragraph 5(3)(e) of the Code

5 Business risk assessment

(3) The business risk assessment must have regard to all relevant risk factors, including —

(e) the involvement of any third parties for elements of the customer due diligence process, including where reliance is placed on a third party



Paragraph 5(3)(e) of the Code details that the BRA must have regard to the involvement of any third parties for elements of the CDD process⁴, including where reliance is placed on a third party.

Third party involvement can occur in a number of ways, to various degrees and at various times during the business relationship. For clarity, this risk factor covers any scenario from the provision of one piece of CDD by a party who is not the customer during the on-boarding of that customer, to the continued provision of CDD through an established, known third party connection who has a relationship with the firm. Involvement of a third party in the business relationship, to any extent, should generally be considered a higher ML/FT risk factor than a strictly direct customer-firm relationship.

³ In accordance with paragraph 9 of the Code

⁴ 'Elements of the CDD process' is detailed further in section 3.4.3 of the Handbook

Outsourcing is also another area where a third party can be involved in elements of the CDD process. When identifying and assessing the ML/FT risks associated with outsourcing elements of the CDD process, consideration should include:

- the quality of control mechanisms in place, such as clarity of the division of roles and responsibilities and the quality of management information and reporting;
- whether the provider is a trusted person⁵;
- reputational issues concerning the provider;
- previous experiences with the provider;
- outsourcing of processes or functions by the provider and the potential for and impact of chains of outsourcing; and
- quality of assurance mechanisms and the results of any audits or inspections where the material generated as a result of outsourcing to the provider has been reviewed.

There are a number of factors to consider when outsourcing elements of CDD process

Paragraph 5(3)(f) of the Code

5 Business risk assessment

(3) The business risk assessment must have regard to all relevant risk factors, including —

(f) customer risk assessments carried out under paragraph 6

Paragraph 5(3)(f) of the Code requires firms to document an assessment of the CRAs carried out under paragraph 6 of the Code. The BRA should make reference to the firm's customer base, particularly highlighting higher risk relationships and the proportion of the customer base such customers represent. The statistical outcomes and findings from the CRAs carried out by the firm should be included within the BRA.

The Authority's officers saw in some instances that whilst relevant persons explained their CRA process and risk ratings utilised, the BRA did not assess or analyse the overall outcomes of the CRAs carried out. The Authority expects, in light of the guidance provided in the Handbook,

an assessment of the CRAs carried out under paragraph 6 of the Code, with the outcomes, data, trends and risks on the customers to be considered and documented.

For example, this should include considering the outcomes such as the number of introducers utilised, the various levels of involvement of third parties, geographical trends or other identified recorded and managed risk data points collected and analysed by the relevant person as part of the CRAs.

Firms may find the inclusion of graphs, charts, and tables on the statistical outcomes of CRAs will assist with the identification and analysis of risks posed to the business.

Handbook quote

The involvement of any third parties for elements of the CDD process, including where reliance is placed on a third party

The Code specifies a number of ways third parties can be involved in elements of the CDD process, namely introduced business, eligibly introduced business, persons in the regulated sector acting on behalf of a third party, certain miscellaneous concessions where the relevant person is not required to comply with paragraph 12(2)(b) and transfers of blocks of business.

57%

Compliance with 5(3)(f) of the Code

Handbook quote

Customer risk assessments carried out under paragraph 6 of the Code

CRAs must be considered as part of the BRA. The BRA and the CRAs are in a continuous feedback loop, with the BRA informing each of the CRAs and the CRAs informing the BRA. Consideration should include the proportion of the relevant person's customers that are higher risk.

⁵ As defined in the Code



Case Study 4: One BRA reviewed by the Authority’s officers, had a dedicated CRA outcomes section, where the relevant person assessed and managed relevant and up-to-date CRA outcome statistics. This section incorporated clear graphs, charts, maps and areas of growth, with a further highlight on the higher risk customers. These statistics and data points were then utilised and refer-

enced throughout the BRA, thus assisting the business in evidencing compliance, and control of the ML/FT/PF risks posed, clearly within the BRA. Including the CRA statistical outcomes also helps in affecting and influencing the relevant person’s higher-level policies, controls and procedures, as well as their resource allocation and compliance monitoring plans.

Paragraph 5(3)(f) - Best Practice

- Provides a detailed breakdown of customers – higher risk, standard risk and lower risk;
- Provides the total number in the customer base;
- Detailing the composition of the customer base – for example, the number of corporate entities and trust entities, and the services provided;
- Analysis of PEP customers – including any foreign and domestic PEPs, PEPs by association and PEPs in their own right;
- Regard to and analysis of the jurisdictions the relevant person is exposed to – including jurisdictions where customers (and beneficial owners) are based, the relevant person/group is based or have any personal links with; and
- Considers and documents the risks and vulnerabilities associated with the customer base.

Paragraph 5(3)(g) of the Code

5 Business risk assessment

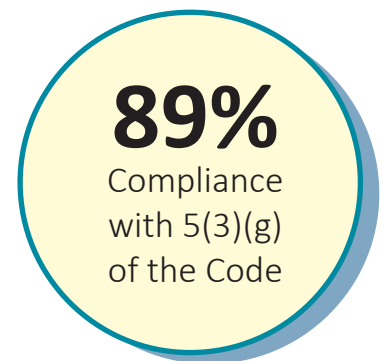
(3) The business risk assessment must have regard to all relevant risk factors, including –

(g) any technology risk assessment carried out under paragraph 7

Paragraph 5(3)(g) of the Code requires the BRA to have regard to any TRA carried out under paragraph 7 of the Code; this means making reference to the TRA as well as its outcomes and findings.

Firms should ensure that they document and evidence their narrative and assessment of identified risks and vulnerabilities, in order to

best demonstrate compliance with the Code. The Authority’s officers observed a range of different ways firms complied with this paragraph of the Code, with some firms covering the TRA and BRA within the same document, and others carrying out the TRA in a separate document and providing a summary of the outcomes and findings within the BRA.



Handbook quote

Any technology risk assessment carried out under paragraph 7 of the Code

The TRA undertaken by the relevant person must be considered as part of the BRA.

Firms should ensure they document and evidence their narrative and assessment of identified risks and vulnerabilities



Case Study 5: In one case seen by the Authority, whilst the BRA and TRA were included within the same policy document, the BRA itself made no reference to the outcomes and findings from the TRA.

Relevant persons should ensure that

the BRA and TRA are interconnected, with the BRA clearly documenting and providing narrative around the risks identified within the TRA. This will enable relevant persons to clearly demonstrate how they have reached and determined the level of risk.

3.4 Summary/Conclusion

The observations, findings, recommendations and best practices identified within this report should be considered, and where relevant, implemented by all relevant persons in their compliance with the Code. The Authority reiterates that compliance with the Code is mandatory,

and all relevant persons should use the range of resources available to assist in complying with the requirements of the Code, including; the Handbook, sector specific guidance, webinars, reports, and public statements the Authority issues and publishes.

Legislation and Guidance	Web Links
The Anti-Money Laundering and Countering The Financing of Terrorism Code 2019	Link
The Anti-Money Laundering and Countering The Financing of Terrorism Handbook December 2023	Link
Supplemental Information Document July 2021	Link
The Isle of Man Financial Services Authority AML/CFT Requirements and Guidance webpage	Link
The Isle of Man Financial Services Authority TCSP Thematic Report Phase 1	Link
The Isle of Man Financial Services Authority Webinars webpage	Link



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