

Results of the 2015 Cayman  
Islands National Risk  
Assessment Relating to Money  
Laundering, Terrorism  
Financing and Proliferation  
Financing

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## Foreword by the Honourable Attorney General, Chairman of the Anti- Money Laundering Steering Group (AMLSG)

As a founding member of the Caribbean Financial Action Task Force (CFATF) in 1990, the Cayman Islands has demonstrated its longstanding commitment to international standards in the fight against money laundering, the financing of terrorism and the proliferation of weapons of mass destruction. The jurisdiction has undergone three mutual evaluations by the CFATF in 1995, 2002 and 2007, and is scheduled to undergo a 4<sup>th</sup> Round CFATF mutual evaluation in December 2017, based on the revised Financial Action Task Force (FATF) 40 Recommendations of February 2012 and the Methodology for Assessing Technical Compliance with the FATF Recommendations and the Effectiveness of AML/CFT Systems of February 2013 (“the Methodology”).

The Methodology marked a significant shift in the way jurisdictions are assessed. While technical compliance based on the FATF Recommendations continues to be assessed, there is now a separate assessment of effectiveness based on 11 Immediate Outcomes with a greater emphasis on national AML/CFT risks and actions to mitigate them.

On behalf of the Government I am pleased to present the summary results of the Cayman Islands’ first Money Laundering/Terrorist Financing (ML/TF) National Risk Assessment (NRA). The NRA was conducted in 2014 and 2015, with technical assistance by the World Bank. A collaborative approach to the NRA was taken as eight working groups assessed national threats and national vulnerabilities, as well as the vulnerabilities within the various financial and non-financial sectors. Sectoral working groups had the benefit of industry participation in assessing ML/TF risks. A working group was also established to review the jurisdiction’s adherence to the FATF 40 Recommendations. It is anticipated that the NRA will be updated at four-year intervals. The Cayman Islands Government thanks all those individuals, both within the private sector and public sector, who contributed to the NRA process.

Summary results of the ML/TF NRA are presented in this report. It is important to note that work has already commenced toward ensuring a more robust and risk-sensitive AML/CFT regime. This work revolves around five key themes: 1) enhancing the jurisdiction’s AML/CFT regulatory framework; 2) implementing a comprehensive risk-based approach to supervision; 3) the strengthening of sanctions, intelligence and enforcement; 4) enhancing domestic co-operation and co-ordination; and 5) ensuring an efficient and effective system for international cooperation. Actions in these areas will lead to a more robust AML/CFT framework, meet international obligations, and further enhance the reputation of the Cayman Islands.

The Cayman Islands is committed to upholding the highest international standards for AML/CFT. It is in our interest to ensure that the jurisdiction remains one of the best places in the world to conduct financial business.

## Executive Summary

The Cayman Islands' NRA involved a process through which money laundering and terrorist financing risks to the Cayman Islands were determined. It closely examined money laundering and terrorist financing threats to the Cayman Islands along with vulnerabilities existing within the jurisdiction's legal and institutional framework which could potentially be exploited.

Through the commissioning of eight subgroups, the NRA took stock of threats at the national level and investigated vulnerabilities at the national and sectoral levels. At the sectoral level, financial and certain non-financial sectors were examined with vulnerability measured on a scale of low, medium low, medium, medium high and high. The findings are summarised below:

### Key findings:

The NRA determined that the Cayman Islands faces internal and external money laundering and terrorist financing threats, including:

- Theft, corruption, and drug trafficking being the main threats emanating from domestic origins
- Fraud, the evasion by foreigners of taxes overseas, and drug trafficking in other jurisdictions

Vulnerabilities at the national level were found to include:

- Less than fulsome implementation of the risk-based approach to AML/CFT regulation
- Shortcomings in domestic cooperation among government agencies at the operational level, notwithstanding strong inter-agency cooperation at the policy level
- Lack of supervision of relevant non-financial businesses and professions
- A sanctions regime which required enhancement to meet the "effective, proportionate and dissuasive" standard required by the FATF

### Financial sector

- Securities and banking sectors, assessed at medium high, had the highest degree of ML/TF vulnerability when compared to the insurance sectors
- The securities sector includes Excluded Persons under the Securities and Investment Business Law (SIBL), which have a higher degree of vulnerability.
- Regulatory and supervisory framework within the banking sector is robust; however most banks operating in the Cayman Islands do not have a physical presence within the jurisdiction and are managed by head offices, mostly in Schedule 3 countries (which are countries assessed to have equivalent AML requirements as the Cayman Islands).
- Insurance sector assessed as having a medium level of vulnerability
- ML/TF risk is primarily in the international insurance sector, but exposure is mitigated by the insurance management requirement
- International insurers operating as commercial insurance companies, especially companies engaged in long-term insurance business, may present a higher ML risk compared to other insurers

### 'Other Financial Institutions'<sup>1</sup>

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<sup>1</sup> Consisting of remittance service providers, leasing and factoring businesses, pawnbrokers and money lenders

## Executive Summary

- Remittance service providers judged most vulnerable, largely due to the cash-intensive nature of the industry, the transient nature of customer relations and the rapid cross-border transfer of funds

### **Designated Non-Financial Businesses and Professions**

- Trust and Corporate Service Providers presented the greatest degree of vulnerability among DNFBPs due to the complexity of their international financial transactions
- Real estate agents assessed to be less vulnerable, but high value properties sold to international buyers were deemed to be the most at risk segment of that market
- Dealers of precious metals and stones represent a very small sector of the Cayman Islands economy and were assessed as having a medium level of vulnerability
- Accountants and lawyers assessed to be least vulnerable amongst non-financial businesses and professions

### **Addressing these issues:**

Decisive action taken around five key themes:

1. Enhancing the regulatory framework;
2. Ensuring a comprehensive risk-based supervisory framework;
3. Strengthening sanctions, intelligence and enforcement;
4. Enhancing domestic co-operation and co-ordination; and,
5. Ensuring an efficient and effective system for international co-operation.

Work on these areas involves several amendments to the *Proceeds of Crime Law*, the *Terrorism Law*, the *Proliferation Financing (Prohibition) Law*, and the *Police Law* among other pieces of legislation.

Work is also being done on the *Money Laundering Regulations* to ensure there is compliance with international standards and that the industry continues to observe and adhere to best practice. There has also been the hiring of staff in key roles required to ensure the effectiveness of the institutional framework.

## Introduction

ML and TF undermine the integrity and stability of financial markets and institutions. They encompass a wide range of activities and often involve transactions and activities crossing national borders. Their wide-ranging effects have motivated international bodies such as the FATF to issue global measures to fight them. In February 2012, the FATF issued a revised set of international standards on combatting ML, TF and proliferation financing (PF) – The FATF 40 Recommendations. These strongly emphasise assessment of ML/TF risk at both the country and sectoral levels, and the adoption of a risk-based approach to mitigating and combatting ML, TF and PF.

Under these new international standards countries are, for the first time, obliged to comprehensively assess their ML and TF risks, and to share the results of that assessment with financial institutions and designated non-financial businesses and professions (DNFBPs). The Cayman Islands Government, through the Attorney General’s Chambers, collaborating with the Ministry for Financial Services, Commerce & Environment and the Cayman Islands Monetary Authority (CIMA), engaged the World Bank to provide technical assistance in conducting the territory’s first ML/TF NRA. The NRA was completed in December 2015.

The primary purposes of the NRA are: 1) to inform competent authorities, financial institutions and DNFBPs of the existing ML/TF risks, thereby facilitating the design and implementation of adequate measures for risk mitigation and prevention; and, 2) to provide information assisting efficient allocation of resources for the combatting of ML/TF. This document provides the financial industry and DNFBPs with the key results of the NRA which, it is envisioned, will facilitate their design and implementation of efficient and effective risk-sensitive measures for the prevention and mitigation of ML/TF.

### **The Cayman Islands’ ML/TF Legal and Institutional Framework**

The Cayman Islands has had a long-standing commitment to fighting financial crime and has, over time, enacted legislation combatting ML and TF including:

- *The Misuse of Drugs Law (2014 Revision);*
- *The Anti-Corruption Law (2016 Revision);*
- *The Proceeds of Crime Law (2016 Revision);*
- *The Terrorism Law (2015 Revision);*
- *The Proliferation Financing (Prohibition) Law (2014 Revision); and*
- *The Money Laundering Regulations (2015 Revision).*

The *Guidance Notes on the Prevention and Detection of Money Laundering and Terrorist Financing in the Cayman Islands, March 2010 (“the Guidance Notes”)*, issued by CIMA provide guidance to be adopted by those involved in the provision of financial services. The Government of the United Kingdom has also passed a number of Overseas Territories Orders for sanctions or restrictive measures against countries, regimes or individuals deemed to be in violation of

international law. These Orders have the force of law in the Cayman Islands once passed by the UK parliament, and are usually based on similar United Nations or European Union sanctions.

Further, supervisory and law enforcement agencies in the Cayman Islands are empowered to share information with counterparts overseas through its *Criminal Justice (International Cooperation) Law (2015 Revision)* and the *Mutual Legal Assistance Treaty* with the United States. Additionally, the *Proceeds of Crime Law* enables the Director of Public Prosecutions (“the DPP”) to apply to the Grand Court of the Cayman Islands on behalf of a foreign territory for the civil recovery of property that is, or represents, property obtained through unlawful conduct. And the European Convention on Extradition has been applicable to the Cayman Islands since 1996 and applies in cases of offences that carry punishment of more than one year either in the Cayman Islands, or in the requesting country.

In relation to tax matters, the Cayman Islands currently has 36 bilateral arrangements with various countries for the provision of tax information. It also signed the Foreign Account Tax Compliance Act intergovernmental agreements with the United States of America and the UK, is an early adopter of the new global standards on the automatic exchange of information for tax purposes, and will implement the OECD Common Reporting Standard (CRS) in 2017.

The Cayman Islands also has in place, an institutional framework, underpinned by law, working to combat ML/TF. This institutional framework is made up of:

- The Anti-Money Laundering Steering Group (“the AMLSG”), charged with oversight of the AML/CFT policy of the Government and chaired by the Attorney General;
- CIMA, which is the anti-money laundering and counter terrorism financing supervisor for financial services in the Cayman Islands;
- The Financial Reporting Authority (“the FRA”), the financial intelligence unit charged with responsibility for receiving Suspicious Activity Reports (SARs), conducting analysis to substantiate suspicion, making onward disclosures to the police for ML/TF investigations, and onward disclosures to counterpart FIUs in other jurisdictions;
- The Financial Crimes Unit (“the FCU”) of the Royal Cayman Islands Police Service (“the RCIPS”), has responsibility for investigating financial crimes within the Cayman Islands, and for obtaining restraint and confiscation orders with respect to crime proceeds;
- The Joint Intelligence Unit, which consists of officers from the RCIPS, Customs and Immigration. Its primary function is to gather and disseminate intelligence to domestic and international law enforcement agencies to facilitate criminal investigations;
- The Anti-Corruption Commission, empowered to investigate reports of corruption, to liaise with overseas anti-corruption authorities, and to obtain court orders freezing the assets of corruption offences suspects;

## Introduction

- The Cayman Islands Customs Department
- The Office of the Director of Public Prosecutions (“the ODPP”), responsible for all criminal proceedings brought within the Cayman Islands; and
- The Cayman Islands Department for International Tax Cooperation, the competent authority for international cooperation for the exchange of tax information.



# Key Findings of the ML/TF National Risk Assessment (NRA)

## National Threats<sup>2</sup>

The primary threats of domestic origin within the Cayman Islands include theft, corruption and drug trafficking. Of the fifteen cases of money laundering offences prosecuted between 2012 and 2014 which saw approximately US\$3.5 million being laundered, the majority related to theft and mainly involved breach of trust situations. There were also offences of robbery and obtaining property by deception.

As it relates to corruption, the period from January 2012 to December 2014 saw 67 offences with potential proceeds of crime implications being reported to the Anti-Corruption Commission. There were within the period, however, a relatively small number of cases in which sufficient evidence was obtained for a prosecution to be instituted. Of the four cases which were prosecuted, convictions were obtained in three cases. In relation to drug trafficking, there were also relatively few charges laid for possession with intent to supply drugs throughout the period 2012 – 2014. Despite the number of cases prosecuted and convictions obtained, corruption and drug trafficking present ongoing threats which the Cayman Islands continues to factor in its design and development of AML/CFT measures.

As an international financial centre the main ML/TF threats originate from criminal activities committed in foreign jurisdictions, which may involve the misuse of Cayman Islands' financial instruments and institutions for the purpose of money laundering. Major ML/TF external threats to the Cayman Islands include fraud, the evasion of taxes in foreign jurisdictions, and drug trafficking overseas.

### ***Fraud***

Evidence from the *Mutual Legal Assistance Treaty (MLAT)* with the United States and international cooperation with other countries under the *Criminal Justice (International Cooperation) Law* reveal that fraud committed overseas poses a threat to the Cayman Islands in that those who have engaged in such activities abroad have sought to launder proceeds by way of its financial system. Since the MLAT's introduction, the Cayman Islands has cooperated with the United States on a number of fraud cases, and several millions of dollars have been returned to the United States for the restitution of victims. Of six MLAT requests for assistance related to ML between 2012 and 2014, three requests related to fraud.

Of the twenty-four requests for assistance from other countries under the *Criminal Justice (International Cooperation) Law* during 2012 to 2014, the majority was related to fraud. Twelve of the 24 cases related to allegations of ML and were received from 7 countries. These requests

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<sup>2</sup> A threat for the purposes of the NRA is a person or group of people, object or activity with the potential to harm, among other things, the state, society, or the economy. This includes criminals, terrorist groups and their facilitators, their funds, as well as past, present and future ML or TF activities. Typically, identifying threats serves as an essential starting point in developing an understanding of ML/TF risk.

## Key findings of the ML/TF National Risk Assessment (NRA)

involved different types of fraud such as wire fraud, securities fraud, investor fraud and mail fraud.

### ***Evasion of Taxes Overseas***

The possibility of foreign nationals evading taxes in their home jurisdictions and using the Cayman Islands' financial system to launder the proceeds is another potential threat to the jurisdiction. However, due to the significant number of multilateral and bilateral arrangements relating to the exchange of tax information operating within the Cayman Islands, this threat is significantly reduced. Notwithstanding the current existence of these avenues for information exchange, the Cayman Islands has been working to strengthen its AML/CFT framework by incorporating the widest array of cooperation mechanisms regarding all overseas tax crimes through explicit provisions in law.

### ***Drug Trafficking by Foreign Nationals***

One case of MLAT assistance provided to the US during 2012-2014 related to drug trafficking, and there was one instance of cooperation with another jurisdiction during that period. There were also 13 cases of importation of marijuana and 2 cases of importation of cocaine during the same period. As the Cayman Islands is a major financial centre within the Western Hemisphere the inherent risk that drug traffickers will seek to utilise the Cayman Islands' financial system to launder the proceeds of crime is recognised. This continues to be a major consideration in the design and implementation of measures aimed at strengthening the AML/CFT framework.

## **National Vulnerabilities<sup>3</sup>**

The areas in which vulnerabilities have been identified are briefly indicated below. The Cayman Islands has addressed or continues to address these vulnerabilities to ensure that its AML/CFT systems accord with international standards and are adequate to prevent the abuse of its financial system by those wishing to profit from nefarious activities.

### ***The Risk-Based Approach to AML/CFT Prevention and Mitigation***

As with many jurisdictions, the risk-based approach to AML/CFT is not yet fully embedded in the Cayman Islands' supervisory regime or within the operations of FIs and DNFBPs. Currently, the *Guidance Notes* incorporate a number of risk-based AML/CFT measures. The *Guidance Notes* are not relied upon regarding points of law; however, since a court takes the *Guidance Notes* into consideration when determining whether there is any failure to comply with the *Money Laundering Regulations* which governs the industry, the *Guidance Notes* are an integral part of the legal and regulatory framework for financial services activity within the Cayman Islands.

Based on the national ML/TF risks identified in the Cayman Islands' first ML/TF NRA, significant work has begun to ensure that the risk-based approach to addressing ML/TF is fully implemented via legislation, at both the national and sectoral levels. Among other things, FIs and DNFBPs will be required to take steps to identify, assess and understand their ML/TF risks. They

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<sup>3</sup> The term "vulnerabilities" refers to those things that can be exploited by a threat or that may support or facilitate its activities. Within the ML/TF context, assessing vulnerabilities means examining factors representing weaknesses in the AML/CFT systems or controls within a jurisdiction. They may also include the features of a particular sector, a financial product or type of service that make them attractive for ML or TF purposes.

will also be required to conduct their own assessment of the ML/TF risks relating to customers, countries or geographic areas, and for products, services, transactions or delivery channels.

### ***Domestic Co-operation and Coordination***

Inter-agency cooperation and coordination at the policy level has effectively taken place in the Cayman Islands for a number of years through the AMLSG. The AMLSG, as indicated earlier, is chaired by the Attorney-General and is otherwise comprised of the Chief Officer responsible for Financial Services, the Commissioner of Police, the Collector of Customs, the Managing Director of CIMA, the Solicitor General, the DPP, and the Chief Officer or Director of the department of Government charged with responsibility for monitoring compliance with AML/CFT measures relating to DNFBPs. Among other things, the AMLSG's responsibilities include general oversight of the AML policy of the Government, promoting effective collaboration between regulators and law enforcement agencies, and monitoring interaction and co-operation with overseas financial intelligence units. The FRA served as the secretariat for the AMLSG until March of 2014, when that function was transferred to the newly-established Anti-Money Unit (AMLU).

The Cayman Islands authorities recognised that at the operational level, measures could be taken to enhance inter-agency cooperation and coordination, particularly among supervisory and enforcement authorities. Accordingly, the *Proceeds of Crime Law* was amended to establish an inter-agency committee responsible for implementing AMLSG policies facilitating coordination and cooperation between each entity tasked with regulating AML/CFT, and assessing risks to the jurisdiction relating to ML/TF. This committee, is chaired by the Head of the AMLU, and is comprised of representatives from relevant competent authorities, namely, the FRA, the FCU, the Customs Department, the ODPP, and each statutory authority, department of Government or agency tasked with regulation for anti-money laundering, counter terrorism financing and anti-proliferation financing purposes.

### ***Supervision***

With the exception of Trust and Corporate Service Providers, DNFBPs operating within the Cayman Islands are not subject to AML/CFT supervision.

Within AML/CFT frameworks, supervisors are largely responsible for assessing and understanding risks pertinent to the sector which they supervise. To ensure that risks relevant to DNFBPs are adequately understood and addressed, the *Proceeds of Crime Law* was therefore amended to establish and empower a supervisor for DNFBPs. In accordance with section 4(9) of the *Proceeds of Crime Law (2016 Revision)*, Cabinet has assigned responsibility for monitoring dealers in precious metals and stones, and real estate agents for compliance with the *Money Laundering Regulations* to the Department of Commerce and Investment (DCI).

The NRA also identified a lack of supervision of non-profit organisations (NPOs) as an existing vulnerability. Therefore the Non-Profit Bill was developed to establish a registration system which will deal with the regulation and monitoring of non-profit organisations to ensure that NPOs are taking measures to address the ML/TF risks within the sector.

### ***Sanctions and Enforcement***

The NRA also identified areas in which sanctions for breaches of AML/CFT laws and the enforcement of such sanctions could be enhanced. According to the *FATF 40 Recommendations*, sanctions for non-compliance should be “effective, proportionate and dissuasive”. Steps have thus been taken to ensure that the applicable sanctions comply with these requirements. Further, it is recognised that administrative fines must be considered a part of supervisors’ range of sanctions as they apply preventive measures in a timely manner to combat ML/TF. In this regard, the *Monetary Authority Law* has been amended to establish a system by which CIMA can administer an administrative fines regime for breaches of regulatory laws, regulations, CIMA rules and the *Money Laundering Regulations (2015 Revision)*. Consideration is also being given to an administrative fines regime for DCI as the regulator for dealers in precious metals and stones, and real estate agents for compliance with the Money Laundering Regulations.

Vulnerabilities within the criminal sanctions regime were also identified by the NRA and the jurisdiction has quickly moved to address them. For instance, under sub-section 5(3) of the *MLRs*, a person who contravenes Regulation 5 (Systems and Training to Prevent Money Laundering) is currently criminally liable on summary conviction to a fine of \$5,000, or on conviction on indictment, to a fine and to imprisonment for two years. It has been recognised that the sum of \$5,000 is unlikely to be “effective, proportionate and dissuasive” as is required by the *FATF 40 Recommendations*. The *Proceeds of Crime Law* has thus recently been amended to allow for administrative penalties and criminal sanctions of up to \$250,000 and \$500,000, respectively, for breaches of the *MLRs*.

As it relates to enforcement, the current staffing level at the FCU stands at 13 which compares with a staffing level of 17 during the 2007 CFATF Mutual Evaluation of the Cayman Islands. Cutbacks in staffing levels, together with the departure of key personnel such as the Forensic Accountant, have presented challenges to the FCU in the processing of increasing numbers of complex investigations.

The FCU has therefore engaged in a recruitment drive to ensure that its responsibilities continue to be executed efficiently and effectively. Given the sophisticated nature of financial services in the jurisdiction, the FCU recognises that it is vital that recruitment and training focus on the requisite accounting, finance, and business intelligence skills. It is also recognised that it is important for staffing levels at the FCU to be restored at least to the 2007 level, and for there to be a team within the FCU focused particularly on complex international ML cases.

As it relates to what are referred to as “targeted financial sanctions” (meant to address terrorism financing and proliferation financing), the Methodology requires countries to implement such sanctions without delay in order to comply with relevant United Nations Security Council Resolutions. The Cayman Islands has created the post of Sanctions Coordinator responsible for the implementation and enforcement of targeted financial sanctions dealing with terrorism financing and proliferation financing.

## Financial Sector Vulnerabilities

Table 1 below illustrates the level of vulnerability of each sector within the financial industry. The different sectors were graded on a scale of a low, medium low, medium, medium high and high level of vulnerability. The factors considered in conducting the evaluation of the sectors include the level of enforcement of AML obligations, the sector’s commitment to good corporate governance, level of penalties existing within the sector, identification infrastructure existing within the sector and quality of AML supervision.

*Table 1: Financial Sector Vulnerabilities*

Thematic Area	Vulnerability Score (0.00 to 1.00) (Low to High)	Vulnerability Level
<b>Insurance</b>	0.54	Medium
<b>Banking</b>	0.61	Medium High
<b>Other Financial Institutions</b>	0.57	Medium
<b>Securities</b>	0.73	Medium High

### *The Securities Sector*

With a vulnerability score of 0.73, the securities sector was assessed to be the most vulnerable when compared to the other sectors within the financial industry.

Licensed institutions within the securities sector as at June 2015 include 39 securities and investment businesses (securities managers, advisers and broker/dealers) and 109 mutual fund administrators. The securities sector is also comprised of 2,275 *Securities Investment Business Law* (“the SIBL”) Excluded Persons registered with CIMA that are exempted from the requirement to obtain a licence to conduct securities investment business. These SIBL Excluded Persons, particularly those providing services to high net worth individuals, are vulnerable to money laundering due to limited supervision. While all SIBL Excluded Persons are subject to the MLRs and are required to have a local registered office, only three categories are required to provide an annual declaration to CIMA setting out information, including the name of the Money Laundering Reporting Officer. Further, there are no direct onsite inspections of SIBL Excluded Persons to verify that proper due diligence and account monitoring are taking place. In this regard, the Government is currently considering proposals to amend the *Securities Investment Business Law* and the *Monetary Authority Law* to enhance the regulatory and supervisory framework applicable to Excluded Persons.

The Cayman Islands is also the premier domicile for mutual funds with 11,061 total funds regulated pursuant to the *Mutual Funds Law* (“the MFL”) as at 30 June 2015. These included 103 licensed funds, 390 administered funds and 10,568 registered funds.

## Key findings of the ML/TF National Risk Assessment (NRA)

The main vulnerability for funds, especially for registered funds, is that the main activity of the fund does not occur within the jurisdiction, neither are the mind and management of the funds local in most cases. In some cases the identity and locations of the ultimate beneficial owners are not necessarily known. The high use of intermediaries, some of which may be unregulated, as well as the fact that service initiation involves little or no face-to-face interactions presents another ML risk. These risks are somewhat mitigated by the fact that the majority of the Investment Managers are from Schedule 3 countries such as the United States, which are regulated.

Additionally, the funds themselves are subject to AML/CFT supervision as they are regulated entities; and, through service providers such as the Registered Office and Administrator, the regulator, in its onsite inspection of these entities, will review the customer due diligence and onboarding procedures for the funds. Further, the Cayman Islands has passed the *Directors Registration and Licensing Law (DRLL)*, requiring the licensing or registration of the directors of regulated funds and Excluded Persons. This will allow for “fit and proper” assessments of directors to be done through due diligence checks and is specifically aimed at enhancing governance and regulatory supervision of directors.

### ***The Banking Sector***

Banking Sector vulnerability was assessed at 0.61, thereby showing a medium high level of vulnerability when compared with other sectors. The banking sector of the Cayman Islands is the sixth largest in the world, with a cross-border asset position at US\$1.365 trillion and fifth by cross-border liabilities of US\$1.347 trillion in the second quarter of 2014.<sup>4</sup> Given the size of the sector relative to other jurisdictions, its interconnectedness to the global economy, and the vital role banks play in cross-border transfer of funds, the banking sector primarily faces the threat of inward transfer of ill-gotten funds.

As a developed and sophisticated international financial centre, a high level of AML awareness and a strong compliance culture exists within the Cayman Islands. Additionally, the overall supervisory framework for banks is strong, with more robust entry requirements introduced in 2014. Further, the existing regulatory, legislative and compliance infrastructure coupled with highly qualified participants with sound industry knowledge set high standards and expectations for compliance with best practices, resulting in a strong AML/CFT framework.

However, a major source of vulnerability is the fact that approximately 144 (i.e. 73.5%) of the 196 banks do not have a physical presence in the Cayman Islands. These banks are mainly managed from their head offices outside of the Cayman Islands, mostly in Schedule 3 countries. As a mitigating measure, onsite examinations have been conducted for 96 of the 144 banks. CIMA’s onsite inspection programme includes overseas visits to head offices by teams from

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<sup>4</sup> Bank for International Settlements (BIS): <http://www.bis.org/statistics/bankstats.htm>. Report titled 2A External positions of banks in all currencies vis-à-vis all sectors; and Bank for International Settlements (BIS): <http://www.bis.org/statistics/bankstats.htm>. Report titled 2A External positions of banks in all currencies vis-à-vis all sectors, which excludes US\$34 billion in own issues of debt securities which are reported without counterparty country breakdown and is not considered to be cross-border as per recent changes to the reporting methodology by BIS.

## Key findings of the ML/TF National Risk Assessment (NRA)

CIMA; with all aspects of the planning, including document and data collection, conducted in advance. CIMA also conducts desk reviews and conference calls with the licensees before the visit, so that time onsite is primarily for high level meetings with senior management and verification of any exceptions noted during the desk reviews.

### *The Insurance Sector*

Insurance Sector vulnerability was assessed at 0.54, also showing a medium level of vulnerability when compared with other sectors. The Cayman Islands insurance sector has two distinct parts – domestic insurance and international insurance. The ML/TF risk is primarily in the international insurance sector even though this exposure is mitigated by the requirement to engage a licensed insurance manager. Insurance management companies are those incorporated and based in the Cayman Islands, providing management services to international insurers not having a physical presence.

International Insurers offer a variety of products. Captive insurance companies offer mostly commercial products such as liability insurance, automobile insurance, property insurance and accident and health insurance coverage to their shareholders or business affiliates. Commercial insurers offer products such as life and annuity insurance, and commercial reinsurers insure other direct general and long-term insurers mostly domiciled outside the Cayman Islands. International Insurers operating as commercial insurance companies, especially companies engaged in long-term insurance business may present a higher ML risk compared to other insurers.

The jurisdiction has seen an increased interest by hedge funds and private equity funds to set up and/or sponsor (re)insurance companies. Complex structures of some of the funds and the multitude of unknown individual investors could expose such companies to ML risks, especially when such entities are not subject to oversight in their home country.

On the other hand, the domestic insurance sector's main risk is small scale crime and use of cash for payments. In the domestic insurance sector, insurance companies offering products such as single premium endowment with high cash values upon surrender and investment-linked products may present a higher ML risk. However, general insurance products sold by domestic insurers are standard and less sophisticated in nature and are seen as low for ML risks.

As it relates to risk mitigation, the *Guidance Notes* provides practical assistance to insurance companies and insurance intermediaries in complying with the MLRs. They also provide practical assistance to all insurers to adopt sound risk management and internal controls for its operations.

Based on survey results and onsite inspections carried out, CIMA noted that most domestic insurers and international insurers have implemented AML/CFT controls to manage any potential ML/TF risk that may occur in a particular product or service that they offer and provide necessary AML/CFT training to their staff. However, effectiveness of their customer due diligence checks could be further strengthened if the companies use appropriate information systems to support their AML/CFT policies and procedures.

***Other Financial Institutions***

The vulnerability of “Other Financial Institutions” (OFIs) (consisting of remittance service providers, leasing and factoring businesses, pawnbrokers and money lenders) was assessed at 0.57, thus showing a medium level of vulnerability. Money remitters were seen as most vulnerable amongst the different types of entities and was assessed at 0.73 or medium high, when compared with the other subcategories. This rating is largely due to the cash-intensive nature of the industry, the transient nature of customer relations and the rapid cross-border transfer of funds. However, some of the associated risks are mitigated as all money remitters are licensed by CIMA and are subject to onsite inspections and off-site surveillance.

**Designated Non-Financial Business and Professions (DNFBPs) Sector Vulnerabilities**

***Trust & Corporate Service Providers***

Given the lack of AML/CFT supervision for most DNFBPs, assessing the vulnerability of DNFBPs has been a challenge. Within that sector, however, and as is shown in *Table 2*, Trust & Corporate Service Providers were assessed to be the most vulnerable to ML, with a score of 0.57. While this sector is supervised for AML/CFT purposes by CIMA, its vulnerability arises due to the complexity of its international financial transactions. Trust and Corporate Service Providers are typically engaged in international investments and structured finance activities, and the high value funds and asset transfers (both locally and abroad) add to the vulnerability.

*Table 2: DNFBP Sector Vulnerabilities*

Thematic Area	Vulnerability Score	Vulnerability Level
<b>Lawyers</b>	0.27	Medium Low
<b>Accountants</b>	0.28	Medium Low
<b>Real Estate</b>	0.41	Medium
<b>Dealers of Precious Metals and Precious Stones</b>	0.41	Medium
<b>Trust and Corporate Service Providers</b>	0.57	Medium

***Real Estate Agents and Dealers of Precious Metals and Stones***

The vulnerability of Real Estate Agents and Dealers of Precious Metals and Precious Stones were each assessed at 0.41. In relation to real estate, over 75% of the transactions in the market are handled by real estate companies that are members of the Cayman Islands Real Estate Brokers Association (CIREBA), with the remaining 25% being sold by non-CIREBA members. Although real estate agents are subject to the MLRs, the main vulnerability at the time of the NRA was that there was no designated AML/CFT supervisor for the sector. However, this vulnerability is somewhat mitigated as CIREBA provides AML/CFT support to its members.



## Key findings of the ML/TF National Risk Assessment (NRA)

Dealers of precious metals and stones, represents a relatively small sector within the Cayman Islands economy. The NRA found no cases of ML or TF within this sector, however, at the time of the NRA there was no AML/CFT supervisory body

### *Accountants*

The vulnerability of accountants was assessed at 0.28 or medium low when compared to the other categories within the sector. This assessment is due to the fact that accounting services in the Cayman Islands are primarily related to audit, accounting and related consultative work carried out by the top international accounting firms. The probability that these services could be exploited by those seeking to launder criminal proceeds is very small. Further, the accounting entities do not handle customer funds and the typical client profile of these firms is one of entities which are already regulated by CIMA.

### *Lawyers*

As it relates to lawyers, their vulnerability was assessed at 0.27 or medium low. This rating is primarily due to four factors. First, the existence of the currently established AML/CFT regime which obliges legal practitioners to comply with “know your customer” requirements when conducting relevant financial business and to report suspicious activity to the FRA with the exception of information subject to legal privilege. Second, the low incidence of cash transactions as the use by clients of cash to pay for services is virtually non-existent outside of smaller residential conveyancing. Third, the established compliance procedures and the natural conservative approach usually taken by the international offshore law firms so as to protect their reputations. And, finally, the majority of the clients of these law firms are corporate entities incorporated in the Cayman Islands or in jurisdictions which regulate these entities in respect of AML/CFT.

## Actions by the Cayman Islands Government

In March of 2016, the Cabinet was apprised of the preliminary results of the NRA and subsequently approved the allocation of \$1.776 million in additional funding for the 2016/2017<sup>5</sup> budget cycle to enhance the effectiveness of the jurisdiction's AML/CFT regime. These funds were earmarked as outlined below along with the activities the Cayman Islands Government undertook to protect the jurisdiction from being used for ML and TF purposes. Allocation of Resources

Firstly, a significant portion of the funds was allocated for the recruitment of additional detective constables for the FCU. The NRA pointed out the need for a dedicated team within the FCU that would focus on the major external AML/CFT threats to the Cayman Islands. As at February 2017, five qualified and experienced financial crime investigators have been appointed to the FCU's proactive ML / TF Investigations unit. All other staff within FCU have received enhanced ML/TF training within an AG funded Multi-Agency training exercise conducted by UK National Terrorist Financial investigation Unit trainers and five existing FCU staff have attended Accredited Financial Investigator Training. In addition, FCU has signed an MOU to cooperate with Cayman Island Anti-Corruption Commission (ACC) and enhance island wide capability.

Secondly, funds were allocated to the FRA for two additional staff members. A Sanctions Co-ordinator has been recruited and has been assigned responsibility for monitoring the implementation of targeted financial sanctions related to the financing of terrorism and proliferation. The FRA also has plans to recruit an additional Senior Financial Analyst to keep pace with the increasing volume of SARs.

Finally, DCI was allocated funding to recruit two additional analysts as they gear up to take on their role as supervisor for dealers of precious metals and stones and real estate agents.

### ***Enhancing the Regulatory Framework***

A number of steps have also been taken by the Cayman Islands Government to strengthen the country's regulatory framework for AML/CFT. The *Proceeds of Crime (Amendment) Law, 2016* has been enacted and included significant changes such as 1) giving the FRA responsibilities for monitoring compliance regarding combating the financing of terrorism and proliferation; 2) designating the Chief Officer for Financial Services as deputy chair for the AMLSG, and widening membership in the policy-making body to include the DPP; 3) providing for the appointment of an inter-agency group for domestic co-operation and co-ordination at the operational level; 4) increasing criminal penalties, including fines up to \$500,000, and new administrative fines for breaches of the MLRs of up to \$250,000; and 5) establishing a supervisor for DNFBPs.

Amendments to the *Terrorism Law* were enacted which, among other things, allow for the Governor to propose to the UN Security Council that a person be designated as a terrorist and to require that persons freeze, without delay, legitimate and illegitimate funds and resources of such

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<sup>5</sup> The 2016/2017 budget cycle for the Cayman Islands Government runs from 1<sup>st</sup> July 2016 to December 2017 as the Government reverts to calendar year budget cycle thereafter.

a person. The Terrorism Law was also amended to provide for an offence to possess or acquire terrorist property with intent or knowledge that it will be used for financing terrorism, terrorists or terrorist organisations as well as that “terrorist property” is property that is used in the financing of acts of terrorism, terrorists and terrorist organisations.

The *Proliferation Financing (Prohibition) (Amendment) Law 2016* was also recently passed. The amendments require the FRA to publish lists of persons who the FATF or such other international organisation has advised may be involved in unauthorised proliferation activities and also allow for the creation of regulations which may provide penalties for breaches.

Further, amendments were made to the *Police Law (2014 Revision)* and the *Penal Code (2013 Revision)*. The *Police Law* has been amended to allow for the making of regulations to further enhance the sharing of information by the Royal Cayman Islands Police Service with other law enforcement and regulatory agencies for the purpose of conducting, or providing assistance with, a criminal investigation. The *Penal Code* has been amended to allow for a graduated scale of increased maximum terms of imprisonment in relation to default of payment of costs, compensation or fines ordered by courts in criminal matters. This will allow for sanctions which are effective, proportionate and dissuasive as required under FATF Recommendations.

Amendments are now underway to the *Money Laundering Regulations* seek to among other things bring them in line with FATF Recommendations and include the introduction of the risk-based approach to supervision and conducting business, enhanced measures for addressing high risk scenarios such as those involving politically exposed persons, and introducing an administrative and criminal sanctions regime for the breach of the regulations.

### ***Next Steps***

Much work is left to be done, including a self-assessment of the effectiveness of the jurisdiction’s AML/CFT regime. In addition to ensuring that the jurisdiction’s laws allow for efficient and effective domestic and international cooperation, the Government of the Cayman Islands will continue to review and update laws to ensure that its regulatory framework continuously adopts best practices while complying with international obligations. It will also continue to strengthen its institutional framework by ensuring supervisors, law enforcement and policy makers are fully aware of developments within the industry and adequately resourced to execute their functions.

It is recognised that the effective implementation of enhanced AML/CFT policies and strategies will depend on partnerships among Government, the private sector and civil society. It is expected that this collaboration among stakeholders and their continued involvement in the process will further raise awareness of AML/CFT issues and highlight the vested interest of each stakeholder in ensuring that the jurisdiction is unfavourable to those who seek to engage in ML/TF activities.

## List of Acronyms

ACC	Anti-Corruption Commission
AML	Anti-Money Laundering
AMLU	Anti-Money Laundering Unit
AMLSG	Anti-Money Laundering Steering Group
CFATF	Caribbean Financial Action Task Force
CFT	Combating the Financing of Terrorism
CIMA	Cayman Islands Monetary Authority
CIREBA	Cayman Islands Real Estate Brokers Association
CRS	OECD common Reporting Standards
DCI	Department of Commerce and Investments
DNFBPs	Designated Non-Financial Business and Professions
DRLL	Directors Registration and Licensing Law
FATCA	Foreign Account Tax Compliance Act
FATF	Financial Action Task Force
FCU	Financial Crimes Unit
FRA	Financial Reporting Authority
NRA	National Risk Assessment
MAL	Monetary Authority Law
MFL	Mutual Funds Law
MLAT	Mutual Legal Assistance Treaty
MLRs	Money Laundering Regulations
MOU	Memorandum of Understanding
MSB	Money Service Business
MSL	Money Services Law
NPOs	Non-Profit Organizations
ODPP	Office of the Director of Public Prosecutions
OECD	Organisation for Economic Co-operation and Development
PF	Proliferation Financing
POCL	Proceeds of Crime Law (2016 Revision)
RCIPS	Royal Cayman Islands Police Service
SARs	Suspicious Activity Reports
SIBL	Securities Investment Business Law
TL	Terrorism Law