



**ISLE OF MAN
FINANCIAL SERVICES AUTHORITY**

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Preventing Financial Crime

**Analysis of firms' data
(2017 and 2018)**

FINANCIAL ADVISORY FIRMS

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1. Introduction and Key Findings for Financial Advisory Firms

- 1.1 This report is focused on those firms whose primary business is that of being a **Financial Advisory Firm** (investment business). Reports for other sectors are also produced.
- 1.2 The typical profile for a Financial Advisory Firm is a firm with permissions to arrange deals and provide financial advice to clients. In the majority of cases, Financial Advisers do not have permission to hold client monies or client assets. Typically, financial advisers give financial advice upon packaged retail products and pensions to domestic customers with whom they have direct ongoing contact.
- 1.3 This report provides an analysis of two years of data and covers areas such as the geographical profile of customers and beneficial owners, Financial Advisory Firms' assessment of customer risk, reporting and monitoring of financial crime and sanctions, and the use of introducers and third parties.
- 1.4 **Table 1** below provides information on the population of **Financial Advisory Firms** who were required to submit the annual AML/CFT data return for December 2018 and December 2017.

Table 1: Population of financial advisory firms for the purpose of this Report

	December 2018	December 2017
Number of Financial Advisory Firms ¹	15	15

- 1.5 The analysis of returns gives a profile which is in line with the Island's National Risk Assessment: the main vulnerability for Financial Advisory Firms is the risk they could become used as part of a chain of arranging for proceeds of crime to be moved/settled into a legitimate product.
- 1.6 The analysis confirms that the sector's client base is predominantly local resident individuals, with business conducted on a face to face basis. Due to the nature of services provided, Financial Advisory Firms need detailed information about their clients' needs, and their financial circumstances. The sector uses the local banking system and no substantial reliance is placed on other parties outside the Island.
- 1.7 Very few foreign PEPs were reported by the sector, and the risk of doing business with sanctioned persons is remote.

¹ The population excludes any banks that also conduct financial advisory activity.

- 1.8 Based on the data, and the nature of services provided by Financial Advisory Firms, the level of risk for both money laundering and terrorist financing is considered to be relatively low.

2. Background to the AML/CFT data return

- 2.1 The Isle of Man Financial Services Authority's ("the Authority") regulatory objectives² include "*the reduction of financial crime*". In its **2018-2021 Strategic Plan** the Authority sets out its *long term goals* and *strategic objectives* which include:-

Long term goal	Strategic objective
<i>Continue to develop our identity and culture and to operate as a forward looking integrated regulator</i>	<i>Enhance the framework to protect consumers and deter financial crime</i>
<i>Fully implement a risk-based supervisory approach for every entity within our remit, including vulnerability to financial crime</i>	<i>Encourage innovation and continuous improvement in all that we do</i>
<i>Be an International Financial Centre which is recognised as effectively deterring financial crime</i>	

- 2.2 During 2016-2017 the Authority consulted on, and subsequently introduced, a pilot annual AML/CFT data return, designed to obtain information from regulated and registered entities to help the Authority monitor AML/CFT threats and trends in, and across, sectors. The table below shows the scope of returns to date and the planned returns for submission in 2020 and thereafter:

Responders	Annual reporting period	Basis for the information	Submission deadline
All regulated entities ³ Sample of registered entities ⁴	31 December 2016	Best endeavours ⁵	29 November 2017
All regulated and registered entities (firms)	31 December 2017	Part actual data, part best endeavours	31 December 2018
All firms	31 December 2018	Part actual data, part best endeavours	31 December 2019
All firms	31 December 2019	Part actual data, part best endeavours	30 September 2020, contingency to 31 December 2020
All firms	31 December 2020 and thereafter	Actual data (unless by exception)	30 June 2021 and 30 June thereafter

² as set out in the Financial Services Act 2008 ("FSA08")

³ Regulated under the FSA08, the Insurance Act 2008 and the Retirement Benefits Schemes Act 2000

⁴ Registered under the Designated Businesses (Registration and Oversight) Act 2015.

⁵ Refer Annex 1: Data Quality.

2.3 Based on the original pilot exercise (December 2016 data), high level results were presented to industry groups during 2018. The Authority has now also analysed the 2017 and 2018 data and developed, for the first time, a collective industry view across sectors⁶, excluding gambling, that are subject to the Island's AML/CFT framework. The Authority will use this information to help with its risk assessment of sectors, and individual firms.

3. Objectives

3.1 The gathering and analysis of data from all firms about AML/CFT helps the Authority to achieve the regulatory objective of "*the reduction of financial crime*".

3.2 The data informs the Authority's understanding of the ***inherent risks*** that firms, and sectors, may pose, and supports the Authority's AML/CFT supervisory work utilising a risk based approach. Some information provided also relates to a firm's ***control environment***. The information that must be reported is dependent on the type of activity a firm undertakes, for example a bank must report more information when compared to a financial advisory firm. Key areas of focus include:-

- The jurisdictional risk profile of the customer base and ultimate beneficial owners;
- The extent of non-face to face and introduced business undertaken by firms;
- Identification and reporting of suspicious activity for both money laundering and terrorist financing;
- Monitoring and screening processes adopted, including for sanctions;
- How firms categorise customer risk;
- The level of politically exposed persons in the system, and how these are identified;
- The compliance and internal audit mechanisms;
- Outsourcing of AML/CFT processes;
- The payment methods accepted by firms in relation to incoming and outgoing transfers; and
- The types of client or product / services provided.

3.3 The data underpins the Island's understanding of the wider financial crime environment and forms a key part of the National Risk Assessment process, alongside

⁶ The data does not include information from the small number of firms who are regulated only for bureau de change, agency payment services, or cheque cashing. These firms currently submit different AML/CFT statistical data which is analysed separately.

the specific quarterly financial flow data that the Authority receives from the Island’s banking sector.

4. Customer risk profile – Financial Advisers

A. Geographical profile - residency

- 4.1 Firms are required to report their customer relationships according to the residency of the customer, based on the ISO country code standard. This information enables the Authority to consider jurisdictional risk, and the extent to which customers are linked to higher-risk jurisdictions, when assessing sectors and firms.
- 4.2 The total number of customer relationships reported by Financial Advisory Firms as at 31 December 2018 was **24,514 (2017: 25,036)**, of which **92.1%** are resident in the Isle of Man (**2017: 90.2%**) and **6.8%** in the UK (**2017: 8.5%**).

At the end of 2018, Financial Advisory Firms reported that **97.3%** of customers were natural persons (**2017: 96.7%**). Some of these customers will be customers of more than one firm that reports data. **Table 2** below provides a more detailed breakdown.

Table 2: Total percentage of relationships based on residency of the customer

	Customer relationships: natural persons (% of total customers)		Customer relationship: Non-natural persons ⁷ (% of total customers)		Total customer relationships (% of total)	
	2018	2017	2018	2017	2018	2017
Isle of Man	89.6%	87.9%	2.5%	2.3%	92.1%	90.2%
UK	6.6%	7.6%	0.2%	0.9%	6.8%	8.5%
All other	1.1%	1.2%	0.0%	0.1%	1.1%	1.3%
TOTAL	97.3%	96.7%	2.7%	3.3%	100%	100%

The jurisdictional profile of the customer base for Financial Advisory Firms does not exhibit material higher risk features, with the majority being Isle of Man resident individuals.

⁷ For a corporate or trust customer the residency will likely be reported as the country of incorporation / establishment of that company or trust (or of the trustee).

B. Geographical profile – residency of ultimate beneficial owners

- 4.3 Financial Advisory Firms can provide services to non-natural customers (“entities”) and must understand who the beneficial owners of such entities are. The level of non-natural relationships is very limited in the sector (approximately **3%** of the total customer book by number of clients). Of the non-natural customer book, a high proportion (**85.1%**) of beneficial owners are resident in the Isle of Man (**2017: 83.5%**), followed by the UK at **8.3% (2017: 10%)**.

Table 3: Residency of the beneficial owners of non-natural customers

	Residency at 31 December 2018		Residency at 31 December 2017	
	Beneficial owners	Entities	Beneficial owners	Entities
Isle of Man	85.1%	91.7%	83.5%	69.8%
Channel Islands	0.6%	0.6%	0.3%	0.4%
UK	8.3%	6.0%	10.0%	28.2%
EU (excludes EEA and Switzerland)	2.3%	1.2%	1.5%	1.0%
Other Europe	0.5%	0%	0.6%	0.2%
Africa	2.1%	0%	3.5%	0%
Americas	0.1%	0.2%	0%	0.2%
Asia (including Middle East)	0.4%	0.3%	0%	0.2%
Oceania	0.6%	0%	0.6%	0%
TOTAL	100%	100%	100%	100%

The data supports the assessment that the geographic nature of Financial Advisory Firms’ business does not exhibit material higher risk features.

C. Politically exposed persons and other high risk customers

- 4.4 **Tables 4a and 4b** show customer relationships, as assessed by Financial Advisory Firms, deemed to pose a higher risk of money laundering, and the level of politically exposed persons (“PEPs”) among the customer base. PEPs⁸ include people with prominent public jobs who may be in a position to abuse their role for private gain.
- 4.5 At the end of 2018 Financial Advisory Firms reported **112 customers who are, or are associated with, a PEP⁹ (2017: 57)**, including only **3 related to foreign PEPs (2017: 1)**. Firms are required to identify PEPs at the start of a business relationship and, through effective monitoring, if any persons subsequently become PEPs. Firms are required by law to undertake enhanced checks and monitoring of all customers who are, or are

⁸ PEP is defined in the Anti-Money Laundering and Countering the Financing of Terrorism Code 2019.

⁹ The actual number of individual (natural) PEPs may be lower than the number of customers reported.

associated with, foreign PEPs and any domestic PEPs who the Firm assesses as posing a higher risk.

Table 4a: PEP relationships

	Number of PEP relationships (and as a % share of all relationships)	
	31 December 2018	31 December 2017
Customers who are/ are associated with PEPs	112 (0.46%)	57 (0.23%)
<i>Of which are foreign PEPs</i>	3	1
<i>Of which are domestic PEPs</i>	109	56

- 4.6 At the end of 2018, **all 15** Financial Advisory Firms confirmed that they screen for PEPs at the start of a business relationship, and screen their customer records on a periodic basis to determine if a customer has become a PEP. The frequency of ongoing screening varied but was predominantly either annually or half yearly rather than through automated daily monitoring; this takes into account the more local features of the customer book and the nature of products and services provided.

This was an improvement from 2017 when one outlier firm reported that it started screening for PEPs in late 2018, noting its customer base was mostly in the Isle of Man.

- 4.7 At the end of 2018 Financial Advisory Firms reported **159 higher risk customers (2017: 154)**; this includes customers who are categorised as being higher risk for reasons other than being a PEP. Where firms identify that customers pose a higher risk, either at the outset of a business relationship, or through an event that occurs during the business relationship, they are legally required to conduct enhanced customer due diligence.

Table 4b: High-risk customer relationships

	Number of high risk customer relationships (total and new) (and as a % share of total / new customer relationships)	
	December 2018	December 2017
Total high risk customers (<i>includes any PEPs assessed as higher risk</i>)	159 (0.65%)	154 (0.62%)
New high risk customers on-boarded in the reporting period (<i>includes any PEPs assessed as higher risk</i>)	6 (0.19%)	19 (0.16%)

- 4.8 Overall, PEPs and other high risk customers represent a **very small proportion** of the total customer base of Financial Advisory Firms (**less than 1%**). Note that the same

individual customers may appear more than once in these figures because individuals and businesses may have multiple financial relationships.

- 4.9 The number of new high risk customers on-boarded, as a proportion of all new customers, continues to be very low and steady. Proportionally, it also continues to be less than the total high risk customer population.

5. Tackling Financial Crime – Financial Advisers

A. Resourcing the fight against financial crime

- 5.1 To effectively monitor and address the risk that persons abuse the financial system for money laundering and terrorist financing requires a significant amount of firms' time and resources. As at 31 December 2018 Financial Advisory Firms reported that they collectively employ **139 staff in the Isle of Man (2017: 130)**, of which **43 (31%)** were reported as being in compliance and prevention of financial crime roles (**2017: 40 / 31%**).

It should be noted that compliance roles are not solely focused on financial crime, with conduct risk and fair customer outcomes also being a key feature of the Financial Advisory sector. Further, one firm incorrectly reported all staff (8) as being in compliance roles.

- 5.2 Relevant staff require ongoing training to ensure they have the effective knowledge to help detect and prevent their firm from being misused by criminals. In the year ended 31 December 2018, Financial Advisory Firms reported that **138 training places were filled (2017: 114)**. This effectively represented **100%** of total staff employed (including directors) (**2017: 88%**).

B. Outsourcing of processes to group entities or third parties

- 5.3 Information is obtained on the outsourcing of certain activities or functions to group entities or third parties. Where outsourcing occurs firms should have robust monitoring and control processes in place, as responsibility remains with the firm. Information is requested in respect of the following:-

- Customer on-boarding (including for risk assessments, collection of due diligence, screening, and business acceptance);
- Ongoing monitoring;
- MLRO and Compliance activity (for AML/CFT); and
- Staff screening and take-on.

5.4 Generally, the **15** Financial Advisory Firms do not outsource activity or functions, although some utilise external compliance support services.

C. Monitoring for, and reporting of, financial crime

5.5 The law requires employees of firms to report knowledge or suspicion of money laundering within their firm, to their MLRO. In the year ended 31 December 2018, **no** cases of concern, suspicion or knowledge of money laundering were either identified by staff, generated through automated processes, or identified from other intelligence sources, and reported to the firms' MLROs (**2017: 4**). In addition, **no** reports were raised which were terrorism related (**2017: zero**).

5.6 MLROs must consider these reports, and decide whether a formal submission to the **Isle of Man Financial Intelligence Unit**¹⁰ ("FIU") is justified, and must be registered with the FIU's "Themis" system to be able to make reports. At the end of 2017 and 2018, of the **15** Financial Advisory Firms, **14** reported they were registered on "Themis".

5.7 In 2018, after investigation by MLROs, **no** cases of knowledge or suspicion of money laundering were reported to the FIU (**2017: 3**). Similarly, **no** reports were made that were terrorism related (**2017: zero**). Further, Financial Advisory Firms reported **no** cases to the FIU regarding general intelligence (**2017: 1**).

5.8 In 2018 Financial Advisory Firms handled **3** requests from law enforcement and other competent authorities (**2017: 1**). Of these, **2** explicitly related to money laundering or terrorism, however it is noted that these enquiries were of a general nature for groups, rather than being specific to Financial Advisory business (**2017: zero**).

5.9 Engagement between the FIU, other law enforcement agencies and financial firms is a crucial component that supports investigations and prosecutions, not only in the Isle of Man but as part of international cooperation. The generally low levels of reporting for the Financial Advisory sector is not unexpected taking into account the nature of the services provided and the predominantly local customer base.

¹⁰ See <https://www.fiu.im/>

Table 5: Liaising with the authorities

Description	Year ended		Year ended	
	31 Dec 2018	31 Dec 2017	31 Dec 2017	31 Dec 2018
Internal Money Laundering disclosures to the MLRO	0	0	4	0
External Money Laundering disclosures to the FIU	0	0	3	0
Internal Terrorist Financing disclosures to the MLRO	0	0	0	0
External Terrorist Financing disclosures to the FIU	0	0	0	0
Section 24 disclosures to the FIU	0	0	1	0
Enquiries received from law enforcement authorities¹¹	2	2	1	1
<i>Of which were Money Laundering related</i>	<i>1</i>	<i>1</i>	<i>0</i>	<i>0</i>
<i>Of which were Terrorism related</i>	<i>1</i>	<i>1</i>	<i>0</i>	<i>0</i>
Enquiries received from other competent authorities	1	1	0	0
<i>Of which were Money Laundering related</i>	<i>0</i>	<i>0</i>	<i>0</i>	<i>0</i>
<i>Of which were Terrorism related</i>	<i>0</i>	<i>0</i>	<i>0</i>	<i>0</i>

D. Refusing and blocking services because of financial crime risk

- 5.10 Concerns relating to financial crime may lead to firms turning away a prospective customer. In the year ended 31 December 2018 Financial Advisory Firms reported that they **did not decline** any potential new relationships because of financial crime, terrorism or sanctions related concerns (**2017: zero**).
- 5.11 Firms are required to monitor ongoing business relationships and may cease to provide services because of their own financial crime risk appetite, or may terminate relationships under certain circumstances, including liaising with the FIU if a matter is subject to “consent”¹². During the year ended 31 December 2018 Financial Advisory Firms **did not terminate** any existing relationships because of financial crime, terrorism or sanctions related concerns (**2017: zero**).
- 5.12 In addition to terminating relationships, firms may be requested by law enforcement agencies to block or freeze accounts, or may themselves put additional controls around accounts if information is required from a customer. As at the end of 2018 there were **no** accounts blocked or frozen for money laundering or terrorism (**2017: zero**). This is not unexpected due to the nature of the services provided by Financial Advisory Firms.

¹¹ In 2018, this information related to generic enquiries across a group, rather than being a specific to financial advisory business.

¹² Section 154 of the Proceeds of Crime Act provides a reporting mechanism called “an authorised disclosure”, which is a means by which a defence against money laundering can be obtained by a firm. Making an authorised disclosure can be used as the vehicle to seek consent to commit a prohibited act (i.e. possessing, acquiring, moving known or suspected criminal property).

Table 6: disrupting provision of services

Description	Year ended 31 Dec 2018		Year ended 31 Dec 2017	
	Number	Asset Value £'000	Number	Asset Value £'000
Number of potential new customer relationships declined for ML/FT or sanctions purposes	0		0	
Number of customer relationships terminated for ML/FT or sanction purposes	0		0	
Blocked or frozen accounts for AML/CFT purposes – subject to consent including restraint orders etc.	0	0	0	0
Blocked or frozen accounts for any other purpose (e.g. gone away)	0	0	0	0

E. The Isle of Man banking system as gatekeeper

- 5.13 When it comes to the material flow of funds into and out of the Island, the banking sector plays an important gatekeeper role. Financial Advisory Firms reported the extent to which they use (themselves or for their clients) the Island’s banking system. In addition to using the Island’s banking sector, firms may also hold bank accounts for themselves, or their clients, outside the Island. Firms are also requested to explain the types of payment method they accept (for inward and outward remittance, where relevant) and the extent to which they are utilised.
- 5.14 **All** Financial Advisory Firms confirmed they only use the Island’s banking sector for their own banking relationships. Where a Financial Advisory Firm is permitted to hold or manage clients’ funds (which in itself is not prevalent), **only 1** reported that they sometimes use a bank outside the Island for that purpose.
- 5.15 The predominant payment methods accepted by Financial Advisory Firms were bank transfers and cheques. For 2017 and 2018 a small number reported that they accept cash by exception (two firms) or on an occasional basis (one firm).
- 5.16 The above shows that Financial Advisory Firms predominantly bank in the Isle of Man and mainly utilise very standard methods of payment, with limited cash activity.
- 5.17 The Island’s banks report the value and number of transactions by country (for money flowing in and out of the Island) on a quarterly basis. Further information is contained in the Preventing Financial Crime report for the banking sector.

6. Managing and reporting of sanctions – Financial Advisers

6.1 It is important that firms have robust controls in place to ensure they comply with local and international sanctions. In order to help achieve this firms must have appropriate monitoring and screening tools to identify whether any of their customers (existing or prospective) are sanctioned individuals or organisations, and also to make sure funds paid / received are not made to / from sanctioned individuals or organisations.

6.2 At the end of 2018, of the **15** Financial Advisory Firms, **14** confirmed that they screen for sanctions at the commencement of a business relationship, and **13** screen their customer records on a periodic basis to determine if a customer has become subject to sanctions. For the latter, the frequency of screening varied but was predominantly either annually, half yearly or ad-hoc rather than through automated daily monitoring; this takes into account the more local features of the customer book.

This was an improvement from 2017 when **3 firms** reported that they did not screen for sanctions, noting one firm reported that it had made arrangements to start screening for sanctions in late 2018. Given the predominantly local customer base the risk of sanction breaches is considered low.

6.3 There is always potential that firms hold the funds of sanctioned individuals or organisations, mainly because such individuals / organisations will not have been subject to sanctions when they were originally accepted as a customer. In such cases, firms may be required to block or freeze assets for financial sanctions purposes. As at the end of 2018 there were **no** accounts blocked or frozen for financial sanctions purposes (**2017: zero**), with an aggregate value of **£0 million (2017: £zero)**. This is not unexpected due to the nature of the services provided by Financial Advisory Firms.

6.4 The law requires firms to identify and report any suspected breach of sanctions¹³ to the **Financial Intelligence Unit**. In practice, these reports will be made by a firm's MLRO or Deputy MLRO using Themis (with processes in place internally for employees to report to the MLRO / Deputy MLRO). In the year ended 31 December 2018, **no disclosures** were made for suspected breaches of sanctions (**2017: zero**).

¹³ With reference to the "Sanctions List", which means the list of persons who are currently subject to international sanctions which apply in the Isle of Man: this list is maintained by the Customs and Excise Division of the Treasury of the Isle of Man.

Table 7: managing and reporting sanctions

Description	Year ended 31 Dec 2018		Year ended 31 Dec 2017	
	Number	Asset Value £'000	Number	Asset Value £'000
Number of disclosures made for suspected breach of sanctions	0		0	
Accounts blocked or frozen in the year for financial sanctions purposes	0	0	0	0
Blocked or frozen accounts for financial sanctions purposes released in the year	0	0	0	0
Number and value of blocked or frozen accounts for financial sanctions purposes as at the year end	0	0	0	0

7. Delivery of services: face to face, use of introducers and third parties – Financial Advisers

- 7.1 How a firm delivers its products and services to customers can range from direct relationships with face to face interaction before a business relationship is established, or an occasional transaction conducted, to situations where relationships are established remotely directly by the customer, or through introducers / third parties (and sometimes through more than one layer of introducer / third party).
- 7.2 Due to the type of business conducted by Financial Advisory Firms, and the regulatory requirements associated with providing financial advice, it is expected that a high proportion of relationships are established on a face to face basis.
- 7.3 In 2018, Financial Advisory Firms reported **3,161** new customer relationships, of which a material portion related to one firm. Of the remaining firms, **over 99% of customer relationships were reported as being established face to face.**

In 2017, Financial Advisory Firms reported **12,128** new customer relationships, of which a very material portion related to one firm, including its acquisition of an on Island book of business. This firm also reported that the majority of its financial advisory business is established face to face, with the exception being certain general insurance business. Again, of the remaining firms, **over 99% of customer relationships were reported as being established face to face.**

- 7.4 There was very little reliance placed on introducers and third parties to hold or provide evidence of customers' identity, with CDD being collected directly from customers.

The exception was the use of permitted insurance concessions for any general insurance business undertaken by Financial Advisory Firms.

Annex 1 – Data Quality

The following matters should be noted in relation to the data provided in this report:-

- Parts of some firms' data is provided on a "best endeavours basis" and therefore cannot be considered as 100% accurate.
- The figures for customer numbers, including PEPs, is based on a simple sum of individual firms' data. A customer of one firm may also have relationships with another and be counted twice in this data.
- One firm reported that its customer numbers may be double counted in parts, due to them being both financial advisory and insurance intermediary customers.