BRIEFING

REVIEW OF TRUST COMPANY BUSINESS IN JERSEY BY THE JERSEY FINANCIAL SERVICES COMMISSION

Focusing exclusively on

- Governance
- Risk
- Compliance

for the financial services industry and regulators, globally.

A recent review of Trust Company Business (TCB) in Jersey by the Jersey Financial Services Commission (JFSC), highlights some of the areas where trust company businesses may be failing.

The JFSC examined 47 TCB's in 2011. There were 6 cases that led to enforcement action which is an increased from 2010 and 2009 where there were only 4 such cases each. The JFSC noted that 'Whilst, on the face of it, this represents a disappointing trend, it is also a reflection of the Commission's reduced level of tolerance in the event that businesses are found to be materially non-compliant in key areas.' However, the JFSC were pleased to report that the percentage of businesses requiring heightened supervision or enforcement fell from 25% to 21% in the last year.

Corporate Governance issues lay at the heart of cases in 5 out of the 6 examinations, which resulted in enforcement action, which indicate that issues in this area can result in serious consequences such as business failure. The JFSC highlighted that best practice was demonstrated where 'all board members were fully aware of their duties and obligations and ensured that they were provided with sufficient information in order for them to fully discharge their duties. Directors should be fully aware of the collective responsibility of the board as a whole as well as their individual duties and responsibilities.' The most common issues when reviewing governance concerned the lack of documentation relating to the thought processes and deliberations of the board.

Another area of concern arose around conflicts of interest. For example, some businesses failed to recognize and record conflicts of interest arising where shareholders and board members of businesses were co-investing with, lending to and borrowing from both customers directly and customer entities for which they were responsible. Other findings included:

- Ineffective performance of board members undertaking multiple roles such as Compliance Officer, Money Laundering Reporting Officer and Money Laundering Compliance Officer as well as undertaking a client facing role;
- A transaction where a director was involved in the decision making where he was to directly benefit from the outcome of the decision.

The JFSC feel that these illustrate that for certain businesses they have some way to go in effectively identifying,properly considering, evaluating and mitigating risks inherent with conflicts of interest.

The JFSC's most common findings in 2011 related to Customer Due Diligence (CDD) deficiencies including:

- Lack of certification of CDD information or other additional checks where businesses were relying on such information to satisfy non face-to-face identification and verification;
- CDD documentation not being appropriately certified (eg customer's self certifying documentation);
- Illegible address verification and unrecognizable photo id
- A lack of understanding of the nature and level of CDD records required in respect of higher risk customers.

The JFSC noted a common theme emerged around group introduction certificates where they found examples where no assessment of risk had taken place, nor had there been any testing to determine whether the group company held the required CDD and could have provided copies upon request.

Similarly the Commission also found that firms did not always hold enough documentation to support their decision making process in the categorization of clients high-risk status and stressed that this should be well documented. With respect to Politically Exposed Persons(PEPs) the Commission wants firms to be able to demonstrate how they have evaluated and individual as a PEP and to document their evaluation. Some of the issues identified around PEPs included:

- A lack of consideration as to whether a a foreign Supreme Court Judge would be considered a PEP;
- No consideration of the high profile status of an ex-international sportsman with on-going media exposure
- No review of the source of wealth of the widow of a foreign ambassador.

The Commission also found a lack of documentation for the rationale of new and existing customer entities. They stated that 'Whilst businesses demonstrated a good understanding of the activity of their customer entities, examinations identified that some businesses could not adequately demonstrate that they have an understanding of why the entity had been established.' Along similar lines the Commission also noted that some firms had failed to obtain copies of the relevant tax advice in respect of customer structures established primarily for the purpose of tax efficient structuring. They stressed that given the changing legislation around tax issues it is important to hold information regarding the tax advice for the client structure.

The JFSC also wished to draw firms' attention to the wide spectrum of areas where geographic risk should be considered. They point out the

BRIEFING

customers' residence, activities and source of wealth should all be considered as well as risks around the proposed activities of the customer, the location of their assets and the source of funds. They found that a number of firms were not taking these factors into consideration in their customer risk ratings. The Commission point out that there is a wealth of information available such as country reports from the FATF, Moneyval and Transparency International.

The Commission identified many businesses that operated effective risk scoring systems which referred back to the business' own risk profile as well as considering geographic risk, activity risk, customer risk and reputational risk. The best system they found combined an objective consideration of a number of risk areas with a subjective review,usually carried out by a member of the board together with compliance, to ensure the risk rating resulting from the objective scoring was reasonable. The JFSC pointed out areas with the most common shortfalls as: rationale, customer risk and geographic risk.

The Commission did find cases where businesses had commenced activity for client entities without having obtained appropriate CDD or undertaking Enhanced Due Diligence for higher risk entities. In some cases they found that businesses had not signed off client acceptance forms for some months after the business relationship was established. In some cases firms had breached the anti-money laundering legislation by transacting for customers without holding adequate CDD.

Some firms were also criticized for failing to review their Business Risk Assessments (BRA), following trigger events. Examples of circumstances were the JFSC would expect a review to take place include: a change of status from/to a managed company, organisational restructuring, or a change in business emphasis. The JFSC also found that some BRAs also failed to consider and identify the specific risks applicable to their own business sector, rather than the generic risks applicable to the TCB sector.

Further information:
JFSC Trust Company Business On-site Examination Programme 2011 Summary Findings

Jersey: PO Box 711, 2 Mulcaster Street, St Helier, Jersey JE4 OPR, Channel Islands, GB T. +44(0)1534 871701 F. +44(0)1534 615988
London: 218 Strand, London WC2R 1AT T. +44(0)20 7125 0417
E: info@stephenplattassociatesllp.com www.stephenplattassociatesllp.com