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Do You know Your Risk?

As we begin a new year, we often reminisce on the previous year; acknowledging our successes and evaluating our failures and setbacks. We also begin aligning our plans with the goals and new year's resolutions that we have set for ourselves and for our business entity. In 2015, as you examine the failures and setbacks, you should also examine the money laundering and terrorist financing risks posed to your entity.

Risk is defined as a probability or threat of damage, injury, liability, loss or any other negative occurrence that is caused by external or internal vulnerabilities that may be avoided through preemptive action. In this regard, entities should develop policies and procedures to identify these risks and establish mechanisms to efficiently allocate the necessary resources to mitigate against these risks.

Regulated businesses/entities listed on the First Schedule of the Proceeds of Crime, Cap 4.28, are required to assess their money laundering and terrorist financing risks when entering into business relationships with a client. Paragraph 34 of the Financial Services (Implementation of Industry Standards) Regulations (FSR), 2011, states *"Prior to the establishment of a business relationship with the applicant for business and periodically thereafter, the regulated business shall assess the risk or otherwise of the applicant for business, the required financial services product and any other relevant factors. Based on this assessment, the regulated business must decide whether or not to accept the business relationship or to continue with it."*

AML/ CFT Risk Assessment

Risk Assessment is defined as a systematic process of evaluating the potential risks that may be involved in a projected activity or undertaking. As outlined above, entities should develop a risk assessment for its customers/business relationships, and by extension, its entity to identify the areas of its operations that are vulnerable to money laundering and terrorist financing risks.

Topics Discussed:

- *Definition of Risk*
- *AML/CFT Risk Assessment*
- *Factors to be considered in a Risk Assessment*
- *Conducting a Risk Assessment*
- *Advantages of Risk Assessment*
- *Legislative References*

Factors to be considered in a Risk Assessment

The following factors should be considered when assessing the AML/CFT risks of a client/business relationship:

* Geographical origin of the client;
* Nature of the business activity;
* Frequency of transactions;
* The AML/CFT regime of the jurisdiction where a corporate client is operating from;
* Any derogatory information revealed on beneficial owners, shareholders or directors of the company during the monitoring process;
* Type of customer e.g. Politically Exposed Person (PEP);
* Type and complexity of the business relationship/transaction;
* Source of Funds information;
* Whether the client/company is listed on any Sanction/Watch List;
* Reluctance of the client to provide pertinent information; and
* Income of the client/turnover of the company.

This list is not exhaustive and includes aspects that should be reviewed on an ongoing basis.

Conducting a Risk Assessment

When conducting a risk assessment, the following steps should be taken;

1. Identify the person(s) who will conduct the risk assessment;
2. Determine the best methods to be used to conduct the risk assessment. **One size does not fit all!**
3. Identify the risks to the entity based on its size and the type of clients, transactions and products provided;
4. Measure the risks associated with the entity. The entity should analyze the significance of the risks;
   a. Inherent Risks – risks that are present before management's action(s) and the implementation of effective internal controls;
   b. Residual Risks – risks that remain after management's action(s) and the implementation of effective internal controls;
5. Document the results of the risk assessment;
6. Determine the internal controls that should be established to mitigate against the risks identified; and
7. Establish an on-going monitoring system to analyze the existing risks and identify new risks. **Risk assessment is not a one-time thing!**

Advantages of Risk Assessments:

1. They create and maintain opportunities for a sound financial entity;
2. They reduce costs by allowing the entity to focus its efforts and resources on the high risk areas; and
3. They avoid negative images and maintain the financial integrity of the entity—the risk assessment would assist you in identifying high risk products/ clients which could be detrimental to your entity.

A risk assessment should not be conducted merely to meet the requirements of the FSR, but should also be utilized to recognize the areas of vulnerability in the entity's operations, identify the greatest areas of risk and reduce costs associated with these risks. This risk assessment should be incorporated into the policies and procedures of the entity and tested by an internal audit function to ensure effectiveness and efficiency.

In 2015, each regulated entity should make a commitment to assess and monitor its money laundering and terrorist financing risks to improve the efficiency of its operations and safeguard its AML/CFT framework.

Legislative References:

* *Proceeds of Crime Act, Cap 4.28*
* *Financial Services Regulatory Commission Act, No. 22 of 2009*
* *Anti-Money Laundering Regulations (AMLR), No. 46 of 2011*
* *Anti-Terrorism (Prevention of Terrorist Financing) Regulations (ATR), No. 47 of 2011*
* *Financial Services (Implementation of Industry Standards) Regulations (FSR), No. 51 of 2011*

Upstairs Karibhana, Liverpool Row, P.O. 898, Basseterre, St. Kitts
Tel: (869) 466-5048 | Fax: (869) 466-5317 | Website: www.fsrc.kn
Email: skanfsd@sisterisles.kn