



**The National Anti-Money Laundering Committee
and the
Bermuda Monetary Authority**

CONSULTATION PAPER

Proposed Legislative Amendments

**Anti-Money Laundering Legislation and Financial
Institutions**

February 2018

I. INTRODUCTION AND BACKGROUND

Proposed Amendments to the Anti-Money Laundering and Anti-Terrorist Financing (AML/ATF) Framework in relation to financial institutions

1. This Consultation Paper (CP), together with the appended draft Bill (see Appendix I), is submitted by the Bermuda Monetary Authority (the Authority) on behalf of the National Anti-Money Laundering Committee (NAMLC) for the attention of industry and other affected persons seeking feedback on:
 - A. Proposals to further strengthen Bermuda's AML/ATF Framework in relation to the activities of financial institutions. These activities include lending, financial leasing, and financial guarantees and commitments (Money Lending activities). The Financial Action Task Force (FATF) Recommendations require that these activities be subject to AML/ATF oversight. See Appendix II for the FATF definition of "financial institutions".
 - B. The extension of the restriction under section 19 of the Insurance Act 1978 to all persons registered as insurers to limit their business to insurance activities. This amendment will effectively limit all insurers from carrying on any other business, including Money Lending activities, except where such business is ancillary to its insurance business.
 - C. The nature and extent of the activities of financial institutions carried on in or from Bermuda, and the money laundering/terrorist financing/proliferation financing (ML/TF/PF) and prudential risks in relation to such activities, especially regarding:
 - i. Lending activities such as a) non-bank entities involved in lending and b) private lending by individuals;
 - ii. Financial leasing carried on as a business by non-regulated entities;
 - iii. Entities involved in the provision of financial guarantees and commitments and particularly the role of insurers and financial institutions.
2. Bermuda is committed to ensuring that Bermuda has a strong, robust AML/ATF framework which is compliant with the relevant international standards, namely the FATF 2012 Recommendations (the Recommendations) and the 2013 Methodology (the Methodology). These legislative proposals are part of an ongoing process for Bermuda to attain a higher level of compliance with these standards. Additionally, these legislative proposals will help ensure Bermuda remains competitive and in line with the AML/ATF regimes of similar leading jurisdictions.
3. It should be noted that Bermuda continues to prepare for the 2018 Mutual Evaluation of its AML/ATF regime. Assessors will examine Bermuda's regime against the requirements in both the Recommendations and the Methodology. The outcome of this evaluation is key to the protection of Bermuda's standing as a quality international financial centre.

4. Bermuda intends to amend the Proceeds of Crime 1997 (POCA), the Anti-Terrorism (Financial and Other Measures) Act 2004 (ATFA), the Proceeds of Crime (Anti-Money Laundering and Anti-Terrorist Financing) Regulations 2008 (POCA Regulations), the Proceeds of Crime (Anti-Money Laundering and Anti-Terrorist Financing Supervision and Enforcement) Act 2008 (SEA), and the Insurance Act 1978 (the Insurance Act). The Authority will also amend the AML/ATF Regulated Financial Institutions Guidance Notes.
5. The purpose of this CP is therefore to:
 - Advise the public of the Draft Bill (Appendix I), which proposes amendments to POCA, ATFA, POCA Regulations, SEA and the Insurance Act;
 - Solicit comments from stakeholders on these proposed amendments for areas of potential impact and concern; and
 - Solicit information from stakeholders on the nature and extent in Bermuda of certain activities of financial institutions, including Money Lending activities, and the ML/TF/ and prudential risks in relation to such activities (See Appendix III for further information on Money Lending activities).
6. Responses are to be sent to the Authority by March 26 2018: policy@bma.bm.

II. DETAILS OF THE PROPOSED LEGISLATIVE AMENDMENTS

7. Recommendation 26 of the Recommendations requires that “financial institutions” are subject to adequate regulation and supervision and are implementing the Recommendations effectively. The proposed amendments will amend the legislation to ensure that all of the activities specified in the FATF definition of “financial institutions” (see Appendix II) are subject to AML/ATF regulation and supervision under Bermuda law. Under the present regime, the activities subject to AML/ATF oversight are those carried out by any business regulated as an “AML/ATF regulated financial institution” as defined under section 42A of the POCA. (see Appendix I). In practice, most of the activities specified in the FATF definition of “financial institutions” are typically conducted by AML/ATF regulated financial institutions as defined under POCA.
8. To assess the impact of the proposed amendments, NAMLC coordinated a working group to determine the scope of the amendments. The working group reviewed the legislation of comparison jurisdictions, contacted members of local law firms, reviewed the Register of Companies managed by the Registrar of Companies, interviewed property developers, and met with representatives of the Bermuda Shipping and Maritime Authority and the Bermuda Civil Aviation Authority. The working group concluded that there are a very small number of businesses that engage in the Money Lending activities set out in Appendix III. The banking sector is primarily relied upon for lending activities and therefore the AML/ATF

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risk is low. The working group noted a recent occurrence where a new business, which was not an AML/ATF regulated financial institution, has been established to provide lending services. The working group also noted private lending is offered by individuals. However, in most cases of substantial private lending, the banking sector and other professional service providers will be involved. The working group will assess on an ongoing basis whether there are any AML/ATF risks posed by such individual lending and whether this individual lending ought to be subject to AML/ATF regulation and supervision.

9. The Authority reviewed the Money Lending activities, and potential risks, of entities licensed by the Authority. The Authority reviewed all sectors including insurers, investment providers, money service providers, trustees, corporate service providers, and fund administrators. The Authority found that such entities are not usually permitted to carry on Money Lending activities. However, in relation to the insurance sector, it is proposed that an amendment be made to the Insurance Act to address a potential weakness in the AML/ATF regime that may be identified by the Assessors in the 2018 Mutual Evaluation. The proposed amendment will restrict *all* insurers from engaging in non-insurance business except where such business is ancillary to its insurance business. Currently under Section 19 of the Insurance Act, only insurers who are licensed as commercial entities are restricted from carrying on non-insurance business except as an activity that is ancillary to its insurance business.
10. As part of this exercise it is necessary to consider exemptions where appropriate. FATF recognises that jurisdictions may provide for exemptions where appropriate, provided that the jurisdiction has considered the AML/ATF risks. A number of leading financial jurisdictions with robust AML/ATF regimes have expressly provided for exemptions where the activity relates to the administration of commercial leasing of immovable property or where the activities specified in the FATF definition of “financial institutions” occur between subsidiary, holding and affiliated companies. The working group concluded that such exemptions were also appropriate in the Bermuda context (see Appendix I).
11. It is proposed that amendments be made to section 42A(1) POCA, section 2 ATFA, section 2(1) SEA, Regulation 2(2) POCA Regulations and section 19 Insurance Act (see Appendix I for proposed amendments).
12. The key proposed amendment will amend the definition of “AML/ATF regulated financial institution” in order to widen the scope of the activities contained within this definition. The amendment will incorporate those activities included in the FATF definition of “financial institutions” that are currently not subject to AML/ATF regulation and supervision. As a result of the proposed amendments, the activities currently not subject to AML/ATF regulation and supervision will fall within the definition of “non-licensed

AML/ATF regulated financial institution” as an AML/ATF regulated financial institution which is not a licensed AML/ATF regulated financial institution. Thus, persons/entities carrying out these activities as a business, for or on behalf of a customer, would be required to register with the Authority (section 9(1) of SEA) and required to comply with the AML/ATF Regulations.¹ The Authority can cancel the registration of a non-licensed AML/ATF regulated financial institution if a person or entity is in breach of a material provision of the AML/ATF Regulations (section 12(b) of SEA)).

III. CONCLUSION & NEXT STEPS

13. As noted above, these proposed legislative amendments are consistent with Bermuda’s steadfast commitment to develop and implement a framework in place to effectively detect and prevent ML/TF. Bermuda also remains committed to compliance with the international standards to combat ML/TF, and intends to continue to build upon Bermuda’s excellent reputation as a well-regulated jurisdiction, providing a positive and secure environment within which to conduct quality business.

14. As the 2018 evaluation requires Bermuda to demonstrate effective implementation of its AML/ATF regime, it is important to proceed with this matter in a timely fashion. The Authority therefore seeks your cooperation in reviewing this Consultation Paper and providing written feedback by March 26, 2018 to policy@bma.bm.

¹ In the SEA, ““AML/ATF Regulations” means the Proceeds of Crime (Anti-Money Laundering and Anti-Terrorist Financing) Regulations 2008, and any subsequent regulations made under section 49(3) of the Proceeds of Crime Act 1997 or section 12A of the Anti-Terrorism (Financial and other Measures) Act 2004.”

APPENDIX I

DRAFT BILL Proceeds of Crime (Financial Institutions) Act 2018

PROCEEDS OF CRIME 1997

The Proceeds of Crime 1997 is amended as follows—

1) Section 42A—

a) In sub-section (1) in the definition of “AML/ATF regulated financial institution” —

- i) at the end of paragraph (g) by deleting the word “or”;
- ii) at the end of paragraph (h) by inserting the word “or” ; and
- iii) by inserting the following paragraph after paragraph (h)—

“(i) carries on, for or on behalf of a customer, the business of providing any of the activities set out in paragraph 1 of Schedule 3, other than an activity falling within paragraphs (a) to (h) of this definition.”

2) By inserting Schedule 3 -

Schedule 3

(section 42A(1))

“(1) The following activities fall within the definition of an AML/ATF regulated financial institution in section 42A(1)(i).

- a) Acceptance of deposits and other repayable funds from the public.
- b) Lending, including consumer credit; mortgage credit; factoring, with or without recourse; and finance of commercial transactions (including forfeiting).
- c) Financial leasing.
- d) Money or value transfer services.
- e) Issuing and managing means of payment (e.g. credit and debit cards, cheques, traveller's cheques, money orders and bankers' drafts, electronic money).
- f) Financial guarantees and commitments.
- g) Trading in:
 - (i) money market instruments (cheques, bills, certificates of deposit, derivatives etc.);
 - (ii) foreign exchange;
 - (iii) exchange, interest rate and index instruments;
 - (iv) transferable securities;
 - (v) commodity futures trading.

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- h) Participation in securities issues and the provision of financial services related to such issues.
- i) Individual and collective portfolio management.
- j) Safekeeping and administration of cash or liquid securities.
- k) Otherwise investing, administering or managing funds or money.
- l) Underwriting and placement of life insurance and other investment related insurance.
- m) Money and currency changing.

(2) A reference in section 42A(1)(i) to carrying on, for or on behalf of a customer, the business of providing any of the activities set out in paragraph 1 of Schedule 3 shall not include

- a) the provision of the services of collecting, administering and disbursing service or maintenance charges (however described) in connection with immovable property situated in Bermuda (including such property when it is occupied under a contractual lease or licence); or
- b) the provision of any of the activities set out in paragraph 1 of Schedule 3 when made by –
 - i) a holding company to a subsidiary company of that holding company;
 - ii) a subsidiary company of a holding company to the holding company; or
 - iii) a subsidiary company of a holding company to another subsidiary company of that holding company.

(3) For the purposes of this Schedule -

- a) a subsidiary company has the meaning given in section 86(1) of the Companies Act 1981;
- b) a holding company has the meaning given in section 86(2) of the Companies Act 1981.

PROCEEDS OF CRIME (ANTI-MONEY LAUNDERING AND ANTI-TERRORIST FINANCING SUPERVISION AND ENFORCEMENT) ACT 2008

The Proceeds of Crime (Anti-Money Laundering and Anti-Terrorist Financing Supervision and Enforcement) Act 2008 is amended as follows—

Section 2 sub-section (1) in the definition of “AML/ATF regulated financial institution” by deleting the definition of “AML/ATF regulated financial institution” and by inserting ““AML/ATF regulated financial institution” has the meaning in section 42A(1) of the Proceeds of Crime Act 1997”;

PROCEEDS OF CRIME (ANTI-MONEY LAUNDERING AND ANTI-TERRORIST FINANCING) REGULATIONS 2008

The Proceeds of Crime (Anti-Money Laundering and Anti-Terrorist Financing) Regulations 2008 are amended as follows—

In Regulation 2 in paragraph (2) in the definition of “AML/ATF regulated financial institution” by deleting the definition of “AML/ATF regulated financial institution” and by inserting ““AML/ATF regulated financial institution” has the meaning in section 42A(1) of the Proceeds of Crime Act 1997”;

ANTI-TERRORISM (FINANCIAL AND OTHER MEASURES) ACT 2004

The Anti-Terrorism (Financial And Other Measures) Act 2004 is amended as follows—

In section 2 in the definition of “AML/ATF regulated financial institution” by deleting the definition of “AML/ATF regulated financial institution” and by inserting ““AML/ATF regulated financial institution” has the meaning in section 42A(1) of the Proceeds of Crime Act 1997”;

INSURANCE ACT 1978

The Insurance Act is amended as follows –

In section 19 sub-section (1) by deleting sub-section (1) and inserting “Subject to subsection (2) no insurer shall engage in non–insurance business”.

Appendix II

FATF definition of “Financial Institutions” and Recommendation 26

The General Glossary of the FATF Recommendations 2012,² define “Financial Institutions” as set out below:

“Financial institutions” means any natural or legal person who conducts as a business one or more of the following activities or operations for or on behalf of a customer:

1. Acceptance of deposits and other repayable funds from the public.³
2. Lending.⁴
3. Financial leasing.⁵
4. Money or value transfer services.⁶
5. Issuing and managing means of payment (e.g. credit and debit cards, cheques, traveller's cheques, money orders and bankers' drafts, electronic money).
6. Financial guarantees and commitments.
7. Trading in:
 - (a) money market instruments (cheques, bills, certificates of deposit, derivatives etc.);
 - (b) foreign exchange;
 - (c) exchange, interest rate and index instruments;
 - (d) transferable securities;
 - (e) commodity futures trading.
8. Participation in securities issues and the provision of financial services related to such issues.
9. Individual and collective portfolio management.
10. Safekeeping and administration of cash or liquid securities on behalf of other persons.
11. Otherwise investing, administering or managing funds or money on behalf of other persons.
12. Underwriting and placement of life insurance and other investment related insurance.⁷
13. Money and currency changing.”

² FATF Recommendations <http://www.fatf-gafi.org/publications/fatfrecommendations/documents/fatf-recommendations.html>

³ This also captures private banking.

⁴ This includes *inter alia*: consumer credit; mortgage credit; factoring, with or without recourse; and finance of commercial transactions (including forfeiting).

⁵ This does not extend to financial leasing arrangements in relation to consumer products.

⁶ It does not apply to any natural or legal person that provides financial institutions solely with message or other support systems for transmitting funds. See the Interpretive Note to Recommendation 16.

⁷ This applies both to insurance undertakings and to insurance intermediaries (agents and brokers).

FATF Recommendation 26. Regulation and supervision of financial institutions⁸

Countries should ensure that financial institutions are subject to adequate regulation and supervision and are effectively implementing the FATF Recommendations. Competent authorities or financial supervisors should take the necessary legal or regulatory measures to prevent criminals or their associates from holding, or being the beneficial owner of, a significant or controlling interest, or holding a management function in, a financial institution. Countries should not approve the establishment, or continued operation, of shell banks.

For financial institutions subject to the Core Principles, the regulatory and supervisory measures that apply for prudential purposes, and which are also relevant to money laundering and terrorist financing, should apply in a similar manner for AML/CFT purposes. This should include applying consolidated group supervision for AML/CFT purposes.

Other financial institutions should be licensed or registered and adequately regulated, and subject to supervision or monitoring for AML/CFT purposes, having regard to the risk of money laundering or terrorist financing in that sector. At a minimum, where financial institutions provide a service of money or value transfer, or of money or currency changing, they should be licensed or registered, and subject to effective systems for monitoring and ensuring compliance with national AML/CFT requirements.

⁸ See also Interpretive Note to Recommendation 26.

Appendix III

Information on Money Lending activities

The scope of the activities that fall within lending, financial leasing, and the provision of financial guarantees and commitments (Money Lending activities) are varied and complex. The scope of the activities and risks set out below are therefore not exhaustive but provide an indication of the types of activities involved. The focus of the lending activities is on credit providers and invoice finance (factoring). The focus of financial leasing activities is on the asset finance of “big ticket” assets, e.g. aircraft. The focus of the provision of financial guarantees and commitments is in the insurance context and on trade finance activities, e.g. issuing letters of credit, standby letters of credit, or bills for collection. The information is based on the UK Joint Money Laundering Steering Group Guidance.⁹

ML/TF risks of Money Lending activities: The susceptibility of Money Lending activities at the traditional placement stage of ML is low. The main ML risks in relation to lending (e.g. consumer credit providers) and financial leasing arise through the acceleration of an agreed repayment schedule, either by means of lump sum repayments, or early termination or settlement. The main ML risks for the lending activities of invoice finance (factoring) are payments against invoices where there is no actual movement of goods or services provided, or the value of goods is overstated to facilitate the laundering of funds. In relation to the provision of financial guarantees and commitments, trade finance can be used in the layering and integration stages of ML as the enormous volume of trade flows obscure individual transactions and the complexities associated with the use of multiple foreign exchange transactions and diverse trade financing arrangements permit the commingling of legitimate and illicit funds.

i) Lending:

Lending activities include, *inter alia*, consumer credit; mortgage credit; factoring, with or without recourse; and finance of commercial transactions (including forfeiting).

a) **Consumer credit providers**

Definition and scope: Consumer credit providers include both unsecured credit providers and secured lenders. Products provided include: high interest short-term unsecured lending (payday loans), store cards and other revolving credit facilities, point of sale or other retail finance, personal loans or short-term credit, second charge lending, and secured loans provided by a pawnbroker.

Risks: Overall, the provision of consumer credit carries a low inherent ML/TF risk. The main ML risks arise owing to the acceleration of an agreed repayment schedule, either by means of lump sum repayments, or early termination or settlement. Lenders will normally only accept instalment payment from the customer named on the agreement, and in the case of an

⁹ <http://www.jmlsg.org.uk>

overpayment will only make repayment to the customer named on the agreement. However, if a consumer credit provider accepts occasional payments from third parties, for example, on settlement of the agreement, it must be alert to the unknown nature of the source of these funds, which may increase the risk of receiving the proceeds of crime.

b) Invoice finance (factoring)

Definition and scope: Invoice finance companies offer numerous products to fund the working capital requirements of their clients; these generally fall into two categories – Factoring agreements and Invoice Discounting agreements. These can be operated on a Recourse or Non-Recourse basis, and with or without disclosure of the assignment of the sales invoice to the client’s customers, the debtors. Factoring is a contract between an invoice finance company and their client where revolving finance is provided against the value of the client’s sales ledger sold to the invoice financier. Invoice Discounting is a contract between the invoice finance company and their client where revolving finance is provided against the value of the client’s sales ledger.

Risks: Both Factoring and Invoice Discounting products facilitate third party payments and therefore may be used by criminals for ML activity. The different invoice finance products available vary greatly and the degree of risk is directly related to the product offering. The level of physical cash receipts directly received within the invoice finance sector is extremely low, therefore the susceptibility of the invoice finance sector at the traditional placement stage is very low. The risk within the invoice finance industry is at the layering and integration stages of ML. The main ML risks within the invoice finance sector are payments against invoices where there is no actual movement of goods or services provided, or the value of goods is overstated to facilitate the laundering of funds. Factoring should be considered to be a lower risk than invoice discounting by virtue of the fact that direct contact is maintained with the debtor. Invoice discounting would represent an increased risk of ML due to the ‘hands off’ nature of the product.

ii) Financial Leasing:

Definition and scope: The FATF requires any natural or legal person who conducts as a business financial leasing activities or operations for or on behalf of a customer to be subject to AML/ATF regulation and supervision. It should be noted that this does not extend to financial leasing arrangements in relation to consumer products. The fundamental characteristic of a lease is that ownership of the asset never passes to the business customer. Here, the focus is on “big ticket” asset finance which broadly covers very high value transactions where the products are highly visible and high profile, such as aircraft, ships and properties.

It should be noted that types of asset finance include:

- Under a *finance lease*, the leasing company recovers the full cost of the equipment, plus charges, over the period of the lease. It can claim written down allowances, whilst the customer can claim both tax relief and VAT on rentals paid.
- *Hire Purchase* (HP) is a well-established method of financing the purchase of assets by businesses. Under a HP agreement, the customer will hire the asset(s) for a fixed period

of time. During this period the asset finance company will recover, through the instalments paid, the cost of the asset(s) together with its charges. Once the agreement is paid in full, the customer has the option to purchase the asset(s) for a nominal sum.

- A *lease purchase* is similar to HP, the main difference being in the terms and structure of repayments. Some finance companies differentiate lease purchase from HP by using lease purchase where the customer wishes to defer payment of a substantial part of the asset cost until the end of the agreement.

Risks: Leasing is low risk due to the fact that the lease agreement does not result in the lessee receiving funds. Rather, the lessee receives the usage of an asset e.g. a vehicle or a piece of machinery. In many instances, property of the asset also remains with the lessor. Hence the initial leasing transaction is unlikely to be vulnerable to ML. The main ML risk arises through the acceleration of an agreed repayment schedule, either by means of lump sum repayments, or early termination.

iii) Financial guarantees and commitments:

Definition and scope: A common theme in financial guarantees and commitments is that they are default instruments which are triggered only in the event of failure to perform under the underlying commercial contract. In the insurance context, a financial guarantee can be a non-cancellable indemnity bond that is backed by an insurer in order to guarantee investors that principal and interest payments will be made. Many insurance companies specialise in financial guarantees and similar products that are used by debt issuers as a way of attracting investors. Financial guarantees and commitments also feature in trade finance - the financial component of an international trade transaction, i.e. managing the payment for goods and/or related services being imported or exported. Such operations comprise a mix of money transmission instruments, default undertakings and provision of finance. Trade finance activities may include issuing letters of credit, standby letters of credit, bills for collection or guarantees.

Risks: Given the nature of the business, there is little likelihood that trade finance will be used by money launderers in the placement stage. However, trade finance can be used in the layering and integration stages of ML since the enormous volume of trade flows obscure individual transactions and the complexities associated with the use of multiple foreign exchange transactions and diverse trade financing arrangements permit the commingling of legitimate and illicit funds. In practice, this can be achieved through the misrepresentation of the price, quantity or quality of imports or exports. Furthermore, the complex and fragmented nature of existing global finance activity where multiple parties (in many cases with limited knowledge of one another) become involved in the handling of trade finance could potentially be taken advantage of to breach sanctions and/or for the proliferation of weapons of mass destruction (WMD).