Financial Services Commission
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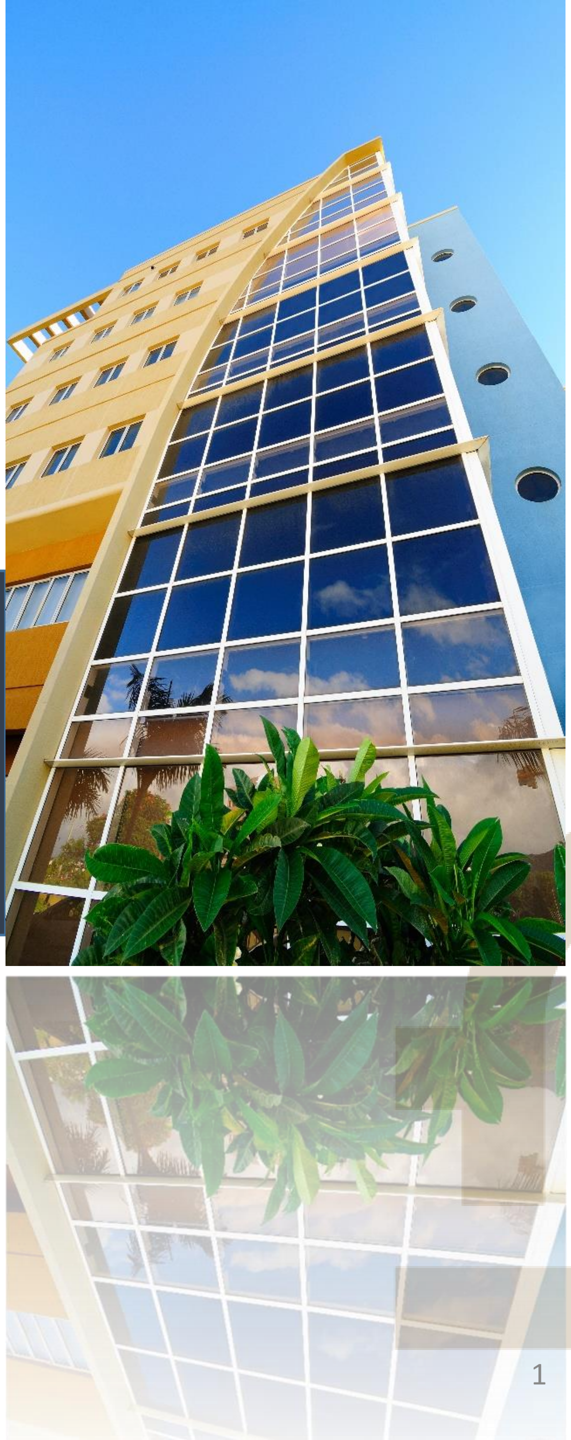

Independent Audit & Business Risk Assessment

August 2021

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Risk Based Approach– FATF's perspective

- A risk-based approach (RBA) to AML/CFT means that the measures taken to reduce ML/TF are proportionate to the risks.
- Mauritius completed its National Risk Assessment (NRA) in August 2019.
- The Money Laundering risk for the different sectors under the FSC's purview are tabled below:

Sector	ML Risk
Insurance	Medium
Securities	Medium- high
Other FIs	Medium
TCSPs	High

- According to FATF Recommendation 1, countries should require financial institutions and designated non-financial businesses and professions (DNFBPs) to identify, assess and take effective action to mitigate their money laundering, terrorist financing and proliferation financing risks.
- FATF Recommendation 18: Financial Institutions' ('FIs') programmes against money laundering and terrorist financing should include an independent audit function to test the effectiveness of their AML/CFT programme.

Legal Obligations

- **Section 17 of FIAMLA**: It is an obligation for FIs to assess and understand their Money Laundering/Terrorism Financing (ML/TF) risks.
- The independent AML/CFT audit covers a review of the Risk Assessment and AML/CFT Programme to ascertain that it meets the requirements of the FIAMLA, FIAMLR and relevant rules & regulations.
- By virtue of the FIAMLA and FIAMLR, there is a statutory obligation on every financial institution:

1. To have in place an audit function which will allow the reporting entity to evaluate its AML/CFT programme; and
2. To ascertain whether the established policies, procedures, systems and controls are adapted with the money laundering and terrorism financing risks identified.

FSC AML/CFT Risk Based Supervision (RBS) Model

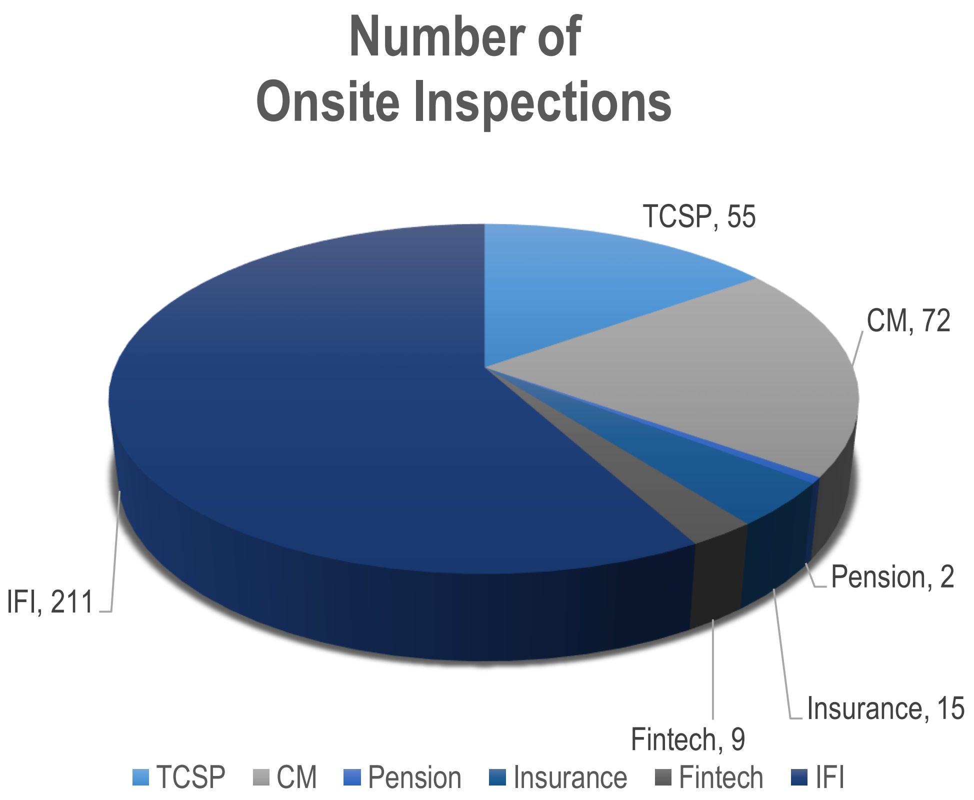
- **FSC AML/CFT RBS Framework conforms to the FATF's international standards**

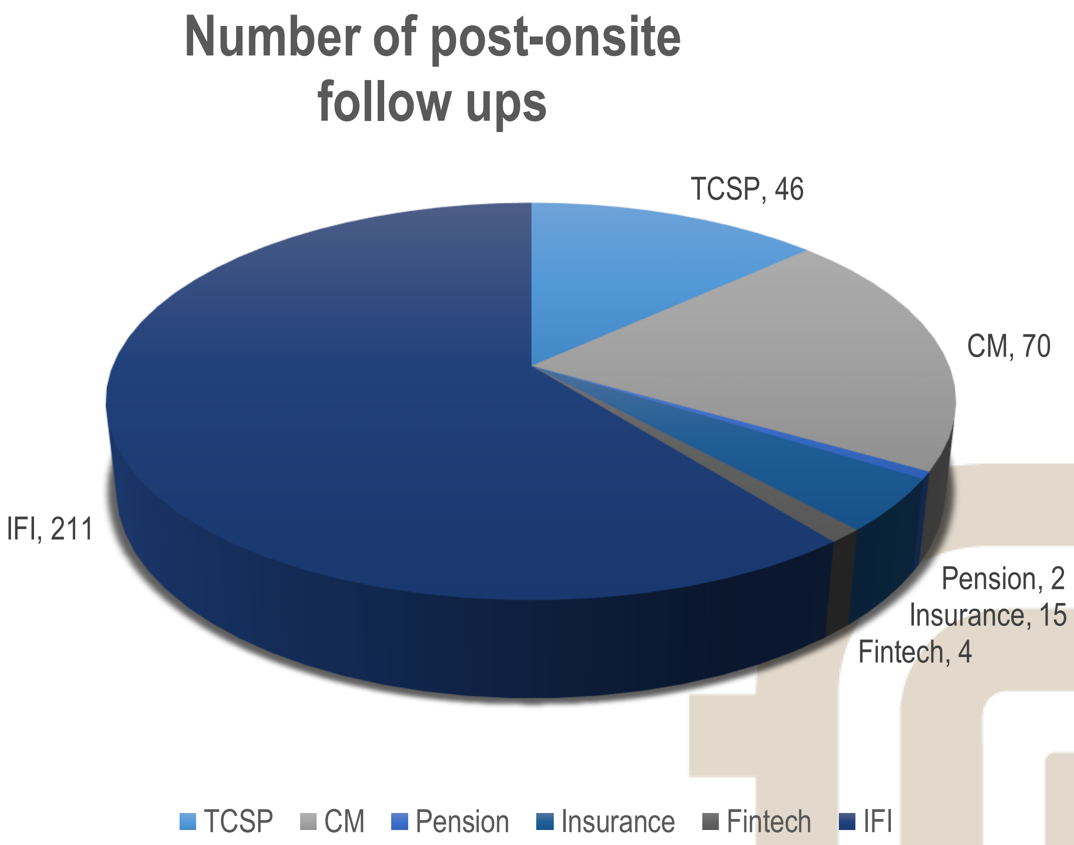
All entities subject to AML/CFT supervision by the FSC have been risk-rated at individual level.

Risk rating is based off the risk matrix, which has two major components:

5 Inherent Vulnerability Factors	7 Compliance Factors
• Entity Characteristics • Products and Services • Clientele • Geography, and • Delivery Channel	• Risk Assessment • Policies and Procedures • Customer Due Diligence • Enhanced Measures • Targeted Financial Sanctions • Suspicious Transactions, and • Internal Controls.

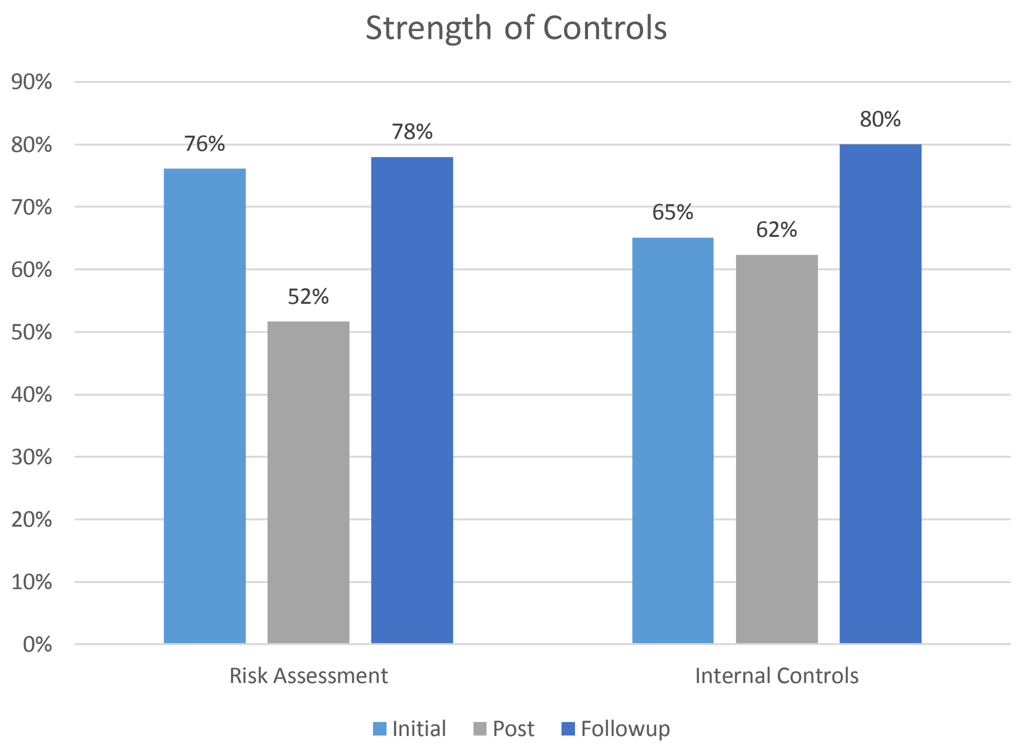
Findings of the 1st RBS Cycle 2020-21





Note:
TCSP- Trust and Company Service Provider
CM- Capital Markets
IFI- Investment Funds & Intermediaries

Findings of the 1st RBS Cycle 2020-21

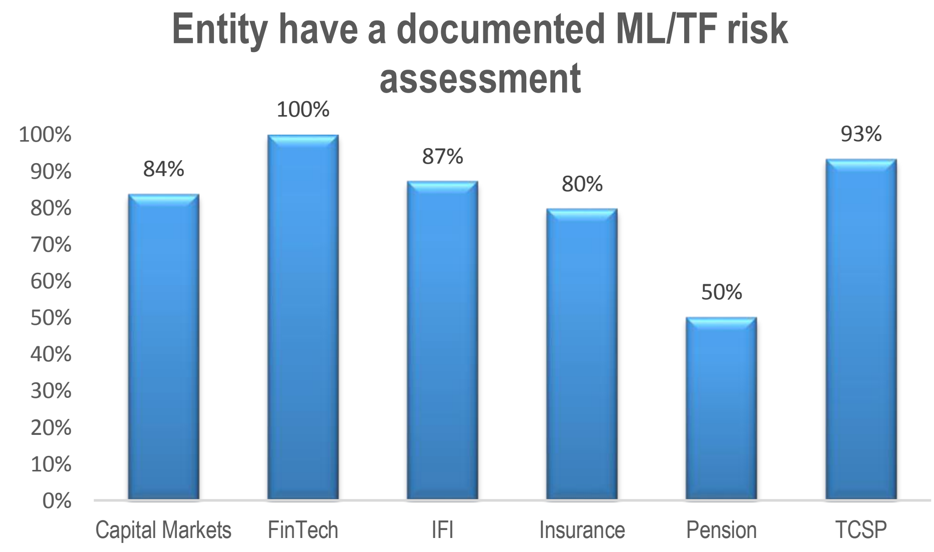


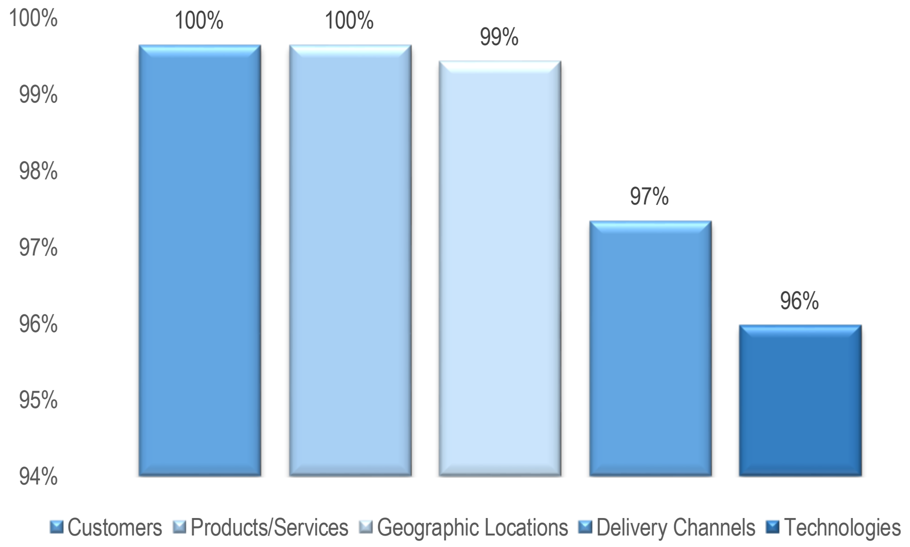
The above chart shows the change in compliance rate post on-site inspections and post follow-up to confirm the implementation of remediation actions by licensees.

- The two major deficiencies identified during the 1st cycle of onsite inspections are Risk Assessment and Internal Control compliance factors.
- Most regulated entities had not yet conducted an AML/CFT Independent Audit and properly implemented a Business Risk Assessment.
- 62% of inspected financial institutions did not have an adequate audit programme and 52% had not conducted a Business Risk Assessment.
- In fact, it was observed that during inspections many regulated entities that reported compliance with regard to BRA did not actually documented the ML/TF risks to their business.
- The post follow-up inspections showed a good progress whereby the regulated entities remedied and completed their business risk assessment.

Findings of 2nd Cycle of the Offsite Monitoring Questionnaire (OMQ)

Risk Assessment

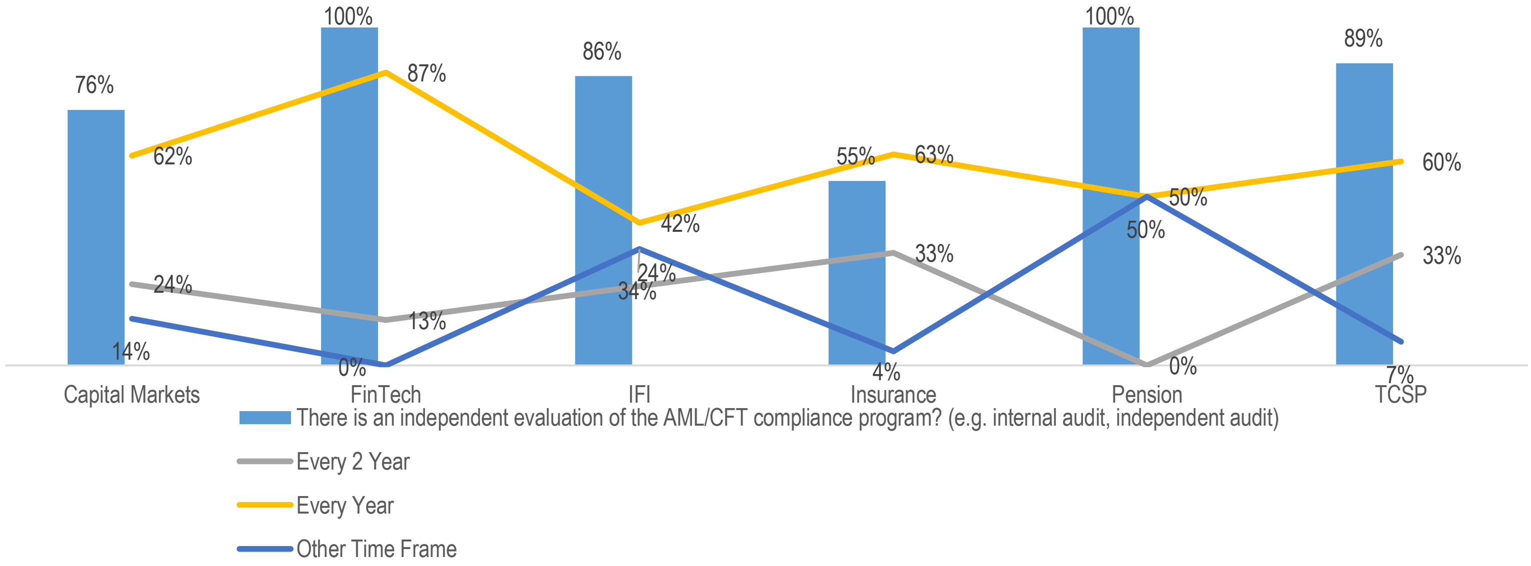


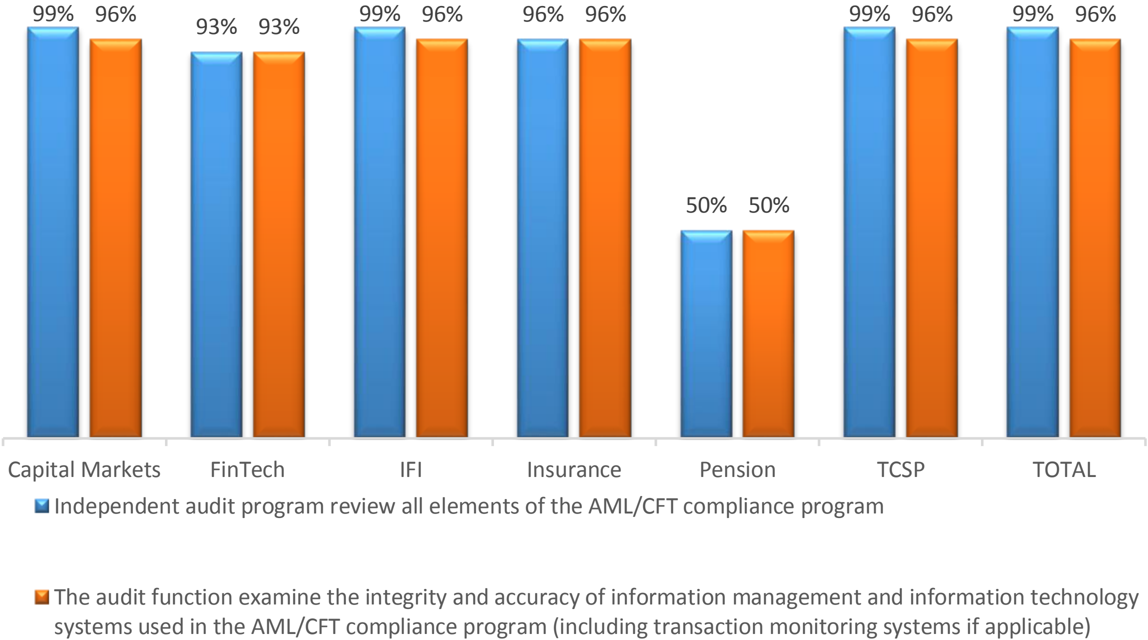


The FSC launched the 2nd cycle of OMQ in January 2021 to which around 1800 entities responded. The following observations were made:

- 87% of the targeted entities had a documented ML/TF risk assessment
- Overall, 88% of the entities which have a documented ML/TF risk assessment have considered different types of risk. 100% of them have considered risk associated with customers and products and services. It should be noted that 99% have considered risk associated with geographic factors, 97% for delivery channels and 96% for technologies.
- 98% of the entities have a documented ML/TF risk assessment, reviewed and updated on a regular basis. 71% of them review the risk assessment annually and 21% uses other time frame. The other time frames include Adhoc/Variables Timeframe, Semi Annually, Quarterly, Monthly and others.

Findings of 2nd Cycle of the OMQ Independent Audit





Observations made:

- 84% of the entities stated that they have an independent evaluation of the AML/CFT compliance program.
- 47% have an independent evaluation of the AML/CFT program every year, 25% every 2 years and 28% other time frames. The Other Time Frames include Adhoc/Variables Timeframe, discretion of Boards, as and when required and others.
- 99% of the entities which stated that they have an independent evaluation of the AML/CFT compliance program review all elements of the AML/CFT compliance program and 96% the entities' audit function examine the integrity and accuracy of information management and information technology systems used in the AML/CFT compliance program.

Expectations from and Obligations of Licensees

- Licensee should conduct BRA and the responsibility of the conduct will have to be shared with the Board, Management, Compliance and Risk Management
- The BRA should be kept up to date and is reviewed at least annually and in case of trigger events.
- Risks, risks identification and mitigation exercises should be constantly reviewed and adapt to fit the emerging risks and the licensee's reality.
- The Board should receive and review periodic reports about AML/CFT Risk.
- Licensee should consider all relevant risks while conducting the BRA.
- Licensees should conduct an AML/CFT Independent Audit and should appoint an independent auditor as specified in the AML/CFT Handbook.
- The frequency and extent of the review should be commensurate with the licensee's size, nature, context, complexity and internal risk assessment.

FSC AML/CFT Handbook Amendments

- In light of deficiencies identified in the 1st RBS cycle, the AML/CFT Handbook was amended in March 2021 in terms of :
  - Updated provisions on Business Risk Assessment – Chapter 4
    - *Section 17(1) of FIAMLA*
  - New chapter on Independent Audit – Chapter 13
    - *Reg 22(1) (d) of FIAML Reg 2018*

FSC AML/CFT Handbook – BRA

Through the business risk assessments and determination of a risk appetite, the financial institution can establish the basis for a risk-sensitive approach to managing and mitigating ML and TF risks. The following 6 key areas will have to be assessed when undertaking the business risk assessment amongst other risk factors:

- The nature, scale and complexity of its activities
- The products and services provided by the financial institution
- The persons to whom and the manner in which the products and services are provided
- The nature, scale, complexity and location of the customer's activities
- Reliance on third parties for elements of the customer due diligence process
- Technological developments

FSC AML/CFT Handbook – BRA

- A financial institution must, under Section 17(1) of the FIAMLA:

I. Identify;

II. Assess;

III. Understand; and

IV. Monitor a person money laundering and terrorism financing risks.

- A key component of a risk-based approach involves the financial institution:

I. Identify areas where its products and services could be exposed to the risks of ML and TF; and

II. Take appropriate steps to ensure that any identified risks are managed and mitigated through the establishment of appropriate and effective policies, procedures and controls.

- It is expected that this risk assessment is reviewed at least annually and in case of trigger events and this review should be documented to evidence that an appropriate review has taken place.

FSC AML/CFT Handbook – BRA

Since the risks of ML/FT vary from business to business and are not static, the financial institution need to identify the vulnerabilities and risks faced

Pursuant to Section 17(2) (b) of the FIAMLA, financial institutions shall take into account the findings of the NRA and any guidance issued in their business risk assessment.

Business Risk Assessment

Financial Institutions may rely on a third party to introduce business or to perform the CDD measures.

Financial Institutions should identify and assess ML/TF risks that may arise in relation to the development of new products and new business practices, including new delivery mechanisms, and the use of new or developing technologies for both new and pre-existing products.

FSC AML/CFT Handbook – BRA

For completeness, the assessment should consider the following posed by the use of new technologies in the context of ML/TF. Appropriate action should be taken to mitigate the risks that have been identified.

Operational Risk

- Arise from the potential loss that could be incurred due to significant deficiencies in system reliability or integrity.
- Increase in proportion to the amount of reliance placed on outside service providers.
- External experts will have implement, operate, and support portions of electronic systems.

Reputational Risk

- When systems or products do not work as expected and cause negative public reaction
- When there are large AML/CFT failures as a result of unmitigated technology risks.

Legal Risk

- Arise from violations or non-compliance with legislation such as the FIAMLA and FIAML Regulations 2018
- Financial institution may also face increased difficulty in applying traditional crime prevention and detection methods

FSC AML/CFT Handbook – Independent Audit

- Chapter 13 of the Handbook covers the following objectives:

  - the scope of the independent audit exercise;
  - the criteria to be considered when assessing the independence and choosing the audit professional;
  - the frequency to conduct an independent audit;
  - the key components of the AML/CFT programme that the independent audit report should cover; and
  - the reporting requirements of a financial institution to the Commission.

FSC AML/CFT Handbook – Independent Audit

- The core function of the assessment team is, collectively, to produce an independent report (containing analysis, findings and recommendations) concerning the financial institution's compliance with the FATF Standards, in terms of both technical compliance and effectiveness.
- A successful assessment of an AML/CFT regime requires, at a minimum, a combination of financial, legal and law enforcement expertise, particularly in relation to the assessment of effectiveness.
- The independent AML/CFT audit covers a review of your Risk Assessment and AML/CFT Programme to ascertain that it meets the requirements of the FIAMLA, FIAMLR and relevant rules & regulations.

FSC AML/CFT Handbook – Independent Audit

The scope of the independent audit exercise is mainly a verification of the AML/CFT risk faced by the financial institution.	Regulation 22 (1) (d) of the FIAML Regulations 2018 requires the audit process to be carried out independently and should separate from the operational and executive team dealing with the AML/CFT processes of the financial institution. It can either be conducted by an internal or external audit professional	The frequency and extent of the review should be commensurate with the licensee's size, nature, context, complexity and internal risk assessment.	The findings of the independent audit report, highlighting recommendations and deficiencies, should be reported to senior management and to the board of directors	All independent audit documentation, including, *inter alia*, work plan, audit scope, transaction testing, should also be properly documented and shall be made available to the FSC upon request

Overall Findings of the TCSP Sector

Strength of Controls Ratings

Based on Inspection Findings

Risk Assessment

COMPLIANCE LEVEL: HIGH

Policies, Procedures & Systems

COMPLIANCE LEVEL: HIGH

Customer Due Diligence including BO and Ongoing Monitoring

COMPLIANCE LEVEL: VERY HIGH

Enhanced Measures including PEPs

COMPLIANCE LEVEL: HIGH

Targeted Financial Sanctions

COMPLIANCE LEVEL: HIGH

Transaction Monitoring and STR reporting

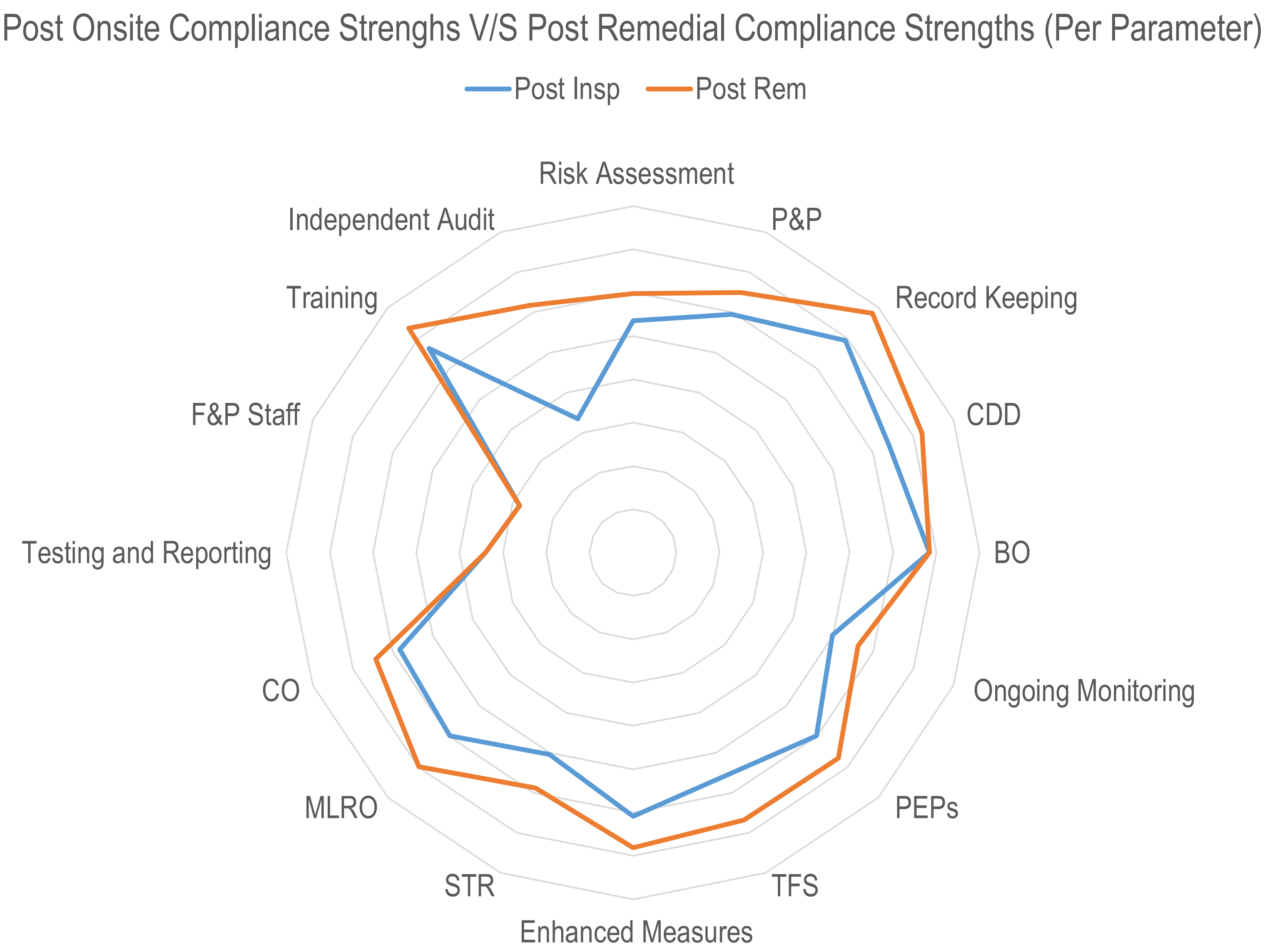
COMPLIANCE LEVEL: HIGH

Internal Controls - Compliance Officer, Training, Audit

COMPLIANCE LEVEL: HIGH

Inherent Vulnerability of Sample: HIGH; Post Inspection Strengths of Controls Sample: HIGH; Post Inspection Residual Risk of Sample: HIGH

TCSP: Inspection 2020



- Compliance to **Risk Assessment** increased from 74% Post-Onsite to 83% post remedial actions. This is mainly explained by BRAs now in place following onsite inspections and risks are primarily being adequately assessed.
- Compliance to **Independent Audit** increased from 28% Post-Onsite to 85% Post Remedial actions. This is mainly explained by independent audits have now been commissioned by the licensees;

Business Risk Assessment

Onsite Observations (74% compliance):

- Risk Assessment mainly covered CRA
- Risk not considered adequately or rationale not well documented
- Fail to align with the NRA

BRA solutions:

- Leverage on the independent audit
- Document the BRA
- Update the P&P accordingly

BRA:

- Properly documented
- Use as a basis for review of the P&P
- Comprehensive coverage

Independent Audit

Onsite Observations (28% compliance):

- Scope of independent audit did not cover AML factor
- Frequency was not established

Independent Audit solutions:

- In-house
- Third Party (Consultant)
- Group level

Type of third party auditor:

- Law Firm
- Accounting Firm
- Compliance Firm

Scope of the Independent Audit

Independent audit is the financial institution's final line of defence. It is vital to ensure that the AML/CFT independent audit is tailored to the financial institution's risks.
The scope of the independent audit exercise is mainly a verification of the AML/CFT risk faced by the financial institution.

Every independent audit should mandatorily test compliance in the following non-exhaustive areas:

- AML/CFT policies and procedures
- Internal Risk Assessment
- Risk Assessment on the use of third-party service providers (Outsourcing)
- Compliance Officer function and effectiveness
- MLRO function and effectiveness
- Implementation and Effectiveness of Mitigating Controls, including customer due diligence and enhanced measures
- AML/CFT Training
- Record Keeping Obligations
- Targeted Financial Sanctions
- Suspicious Transaction Monitoring and Reporting

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Thank You