AUTORITÉ MONÉGASQUE DE SÉCURITÉ FINANCIÈRE

Sectoral risk assessment 2023
TCSP SECTOR

Executive summary

1. In 2020-2021, Monaco conducted its second detailed National Risk Assessment of money laundering and terrorist financing risks ("NRA 2"). NRA 2 was analysed by MONEYVAL in the course of the 2022 Mutual Evaluation of Monaco. While the increase in quality was generally commended by MONEYVAL, it was recommended to further strengthen the analysis in relation to certain risks, including those relating to the sector of trust and company service providers (TCSPs) and to trusts/trustees.

2. To implement MONEYVAL's recommendation, AMSF as competent AML/CFT supervisor of TCSPs coordinated the **2023 Sectoral Risk Assessment for the TCSP Sector** ("2023 TCSP SRA"). The purpose of the 2023 TCSP SRA is to complement the NRA 2, to deepen and broaden Monaco's understanding of the level of risk in relation to the TCSP sector.

3. The 2023 TCSP SRA takes into account the specific factors that characterize the potential ML/TF risks of Monaco's TCSP sector by examining the level of threat to the sector and the inherent risks relating to customers, services, products, transactions and delivery channels in the sector, and by assessing the overall AML/CFT control environment as well as specific areas of controls such as application of customer due diligence to manage and mitigate risks.

4. The 2023 TCSP SRA analyses risks and controls in relation to **three different subsectors** present in Monaco. The first and main subsector is formed by **TCSP companies**. They are mostly focused on company services such as creating and managing companies and often combine this with providing trust services, to a more limited extent. Following a specific MONEYVAL finding, special attention was paid in the SRA to risks relating to the interaction between TCSP companies and the banking sector. The second subsector is formed by **Business centers** providing domiciliation services, which were brought in scope of Monaco's AML/CFT regime in December 2022 following MONEYVAL recommendations. The third subsector is formed by **Trustees** under Article 3 of Law No. 214 catering to a niche of residents in Monaco with nationality of common law jurisdictions who wish to settle a foreign-law trust in Monaco.

5. Monaco's status as an international financial place and the myriad connections of Monaco's TCSP sector to offshore destinations, including higher-risk jurisdictions, are the main perspectives under which this assessment is conducted. At the same time, it should be kept in mind that Monaco's TCSP sector has been steadily decreasing in materiality and activities in the past years, and is relatively small compared to the TCSP sectors of other comparable jurisdictions. As of 2022, the number of TCSP companies has further decreased to 35 entities, whereas it was 42 at the time of NRA 1 and 38 at the time of NRA 2. Their annual turn-over has decreased from an average of around €60 million in the years prior to NRA 2 to around €40

million in 2022. Their client base is only a fraction of the client base of Monaco's banking sector (around 4800 clients versus 124 500 clients). The subsector of business centers, which have recently been brought into scope of Monaco's AML/CFT regime, consists of 16 entities providing only limited relevant services (domiciliation). The subsector of trustees under Article 3 of Law No. 214 consists of around 20 entities who together administer around 30 active testamentary trusts.

6. The 2023 TCSP SRA is based mainly on: data on STRs and criminal cases provided by the FIU and law enforcement authorities; data on inherent risks and controls provided by the sector to AMSF supervisors through the dedicated software tool "STRIX AML" (for the reporting period January – December 2022); the findings of AMSF inspections conducted over the past five years; data on trusts from the Register of Trusts provided by the Department of Economic Development (DDE), and data on trustees registered with the Court of Appeals.

7. Taking stock of the analyses of the SRA, overall results per sub-sector can be summarized as follows:

	TCSP companies	**Business centres**	**Trustees**
Inherent risks relating to customers	High	Medium-High	Low
Inherent risks relating to products, services & transactions	Medium-High	Medium-Low	Low
Inherent risks relating to delivery channels	Low	Medium-Low	Medium-Low
Overall Inherent risk	Medium-High	Medium-Low	Low
Controls	Moderate	Weak	Substantial
Residual sub-sectorial risk	**Medium-High**	**Medium-Low**	**Low**

8. **Compared to the situation at the time of NRA 2**, the following main developments can be noted:

- Careful indications of a decrease in the threat level to the TCSP sector as no new criminal investigations involving the sector have been opened since NRA 2 (see paragraph 9 below);
- Further decrease in materiality of the TCSP sector as described in paragraph 5 above;
- Business centres have been brought into scope of Monaco's AML/CFT regime;
- Improvements in supervisory risk assessment of the TCSP sub-sector and business center sub-sector, with AMSF having completed new risk assessments through the use of a sophisticated software tool for risk assessment, "STRIX AML";

- The national-level topical risk assessment on Terrorist Financing (TF) concluded that TCSPs, together with banking and real estate sectors, have medium-high residual risks in relation to the TF scenario of customers or BOs being terrorism financiers;
- The national-level topical risk assessment on Tax-related risks concluded that Monaco's private sector is exposed to medium-low residual risks for the risk scenario of customers entering into a business relationship with Monegasque FIs or DNFBPs with the intention to use the relationship for tax-related money laundering. The banking and real estate sectors contribute more heavily to this risk than the TCSP sector;
- The national-level topical risk assessment on Virtual Assets concluded that TCSPs do not have exposure to risks relating to VAs.

9. In relation to **threats,** up-to-date information from intelligence and law enforcement shows that the threat level for the TCSP sector can still be assessed as moderately high, with careful indications that it may be declining. STRs filed by the sector increased in 2022: whereas the average annual number of STRs was around 30 for the years prior to NRA 2, in 2022 it stood at 47. However, whereas the sector featured in 9 investigations and 4 prosecutions in the years leading up to NRA 2, for the years 2021-2023 no new ML/TF investigations or prosecutions involving financial flows through the sector have been reported. This development may be explained by the ever-decreasing materiality and activity of the sector and the fact that some of the "bad players" have been heavily sanctioned or removed from the market in previous years. However, it is too early to conclude that the sectorial threat level assigned by NRA 2 (moderately high and stable) should be adjusted. A comprehensive national-level threat assessment for Monaco is currently being conducted and may lead to further insights on the threats to the sector.

10. It can be concluded that the residual sub-sectorial risk rating for the **sub-sector of TCSP companies** should remain at **medium-high level,** comparable to how it was assessed at the time of NRA 2, mostly on account of the very high customer risks to which the sub-sector is exposed. Notably, the sector is heavily focused on offshore business and has nearly 8% of clients and 6% of BOs with links to higher-risk jurisdictions, including jurisdictions that present a higher risk of terrorism. Products and services offered by TCSPs are generally vulnerable for criminal exploitation as described in global and regional reports reviewed for the SRA, as criminals are known to frequently use cross-jurisdictional chains of companies or legal arrangements as vehicles to retain control over criminally derived assets while frustrating abilities of law enforcement to trace their origin or ownership and may seek to use TCSP services to create or manage such structures.

11. At the same time, risks related to TCSP companies in Monaco are moderated to some extent due to the limited and ever decreasing amount of cash flowing through this sector. Also, TCSP companies rarely

rely on delivery channels which would raise ML/TF risks (introducers and non-face-to-face onboarding). Based on extensive AMSF supervision of the sector in recent years, it can further be concluded that the sector's level of implementation of AML/CFT controls stands, on average, at moderate levels, which is better than generally found for TCSP sectors in FATF/FSRB evaluations under the current round. It is deemed highly important however that the sector further enhances controls to better manage their exposure to very high customer risks.

12. Following a specific MONEYVAL finding, special attention was paid in the SRA to assessing risks relating to **the interaction between TCSP and banking sectors**. Four different interactions were analysed: 1) TCSPs as customers of Monegasque banks; 2) TCSPs as introducers of clients of banks / Banks relying on KYC/CDD conducted by TCSPs; 3) The roles of TCSPs in relation to bank accounts of object structures; 4) Customers/object structures of TCSPs with foreign bank accounts.

13. It was established that banks should make further efforts to distinguish in their risk assessments whether customers are TCSPs as only half of them currently make the distinction. In relation to TCSPs acting as possible gatekeepers for banking business, it was established that even where banks rely on TCSPs to introduce clients (which is becoming in itself a rare practice), they very rarely rely on TCSPs to conduct CDD. For their part, TCSPs do not rely on third parties; hence potential risks in relation to extended "information chains" between banks, TCSPs and potential other intermediaries passing on incomplete or false CDD information to each other, are not assessed to be pertinent for Monaco.

14. It is further noted that TCSPs in Monaco are prohibited from holding nominee bank accounts for their clients. This is an important mitigant in the interaction between banks and TCSPs as it is therefore not possible for clients or BOs to conduct banking activity "hidden" behind a TCSP. TCSPs do often have a role in managing the bank accounts of the structures that they administer for their customers. If a TCSP administers a structure for a customer whereby the beneficial owner or a third party has sole signatory over the bank account, this raises ML/TF risks, since the TCSP will have limited visibility or influence on transactions and/or has knowledge of transactions only once they are executed.

15. In case of customers or structures of TCSPs which do not have a Monegasque bank account, there is no "double layer" of CDD carried out by Monegasque regulated entities (the TCSP as well as the bank). This is reportedly the case for around 21% of the client base and around 24% of structures administered by TCSPs. With some exceptions, all TCSPs involved in managing structures without Monegasque bank accounts confirm that they know all of the foreign bank account locations. 25 bank accounts for such structures were identified in higher-risk jurisdictions. Where locations of the address of the customer/structure and address of their bank are unconnected and no valid explanation can be given for the disparate addresses, this is a red flag that should raise the TCSP's suspicions.

16. Follow-up actions are outlined in the SRA to take relevant findings of the dedicated analysis on interactions between TCSP and banking sectors into account in supervisory risk assessment, inspections and guidance.

17. Turning to the next sub-sector analysed in the SRA, it is emphasised that **business centers** were not previously subject to national-level risk assessment as they were brought into scope of Monaco's AML/CFT regime only recently (December 2022). Taking stock of findings of the current SRA, it is concluded that their sub-sectorial residual risk rating should be assessed as **medium-low**.

18. The sub-sector has quite a limited number of customers (approx. 2300) and provides limited relevant services (domiciliation only). However, business centres are believed to be at increased risk due to addresses provided to a type of civil law partnership called "sociétés civiles immobilières" (SCIs), which can be used to hide beneficial ownership over real estate as noted in recent regional and national reports. Furthermore, cash is more common in this sub-sector than in the TCSP company sub-sector, although it is noted that it concerns mostly small fees paid by clients for the business center's services. The sector reports a limited presence of higher-risk customers, but this is believed to be in large part due to underreporting given the low levels of awareness on customer risks in the survey's reference period.

19. The fact that this sub-sector is now subject to AML/CFT obligations and AMSF supervision should lead to controls being introduced by this sector. However as could be expected given their recent entry into scope of the AML/CFT regime, most of the business centres have not yet taken the necessary steps in this direction in the reference period for this SRA. Sub-sectorial risks may be assessed as lower in the future if the sub-sector manages to build up a significant controls framework.

20. Finally, the sub-sector of **trustees under Article 3 of Law No 214** was subject to a separate assessment in this SRA following MONEYVAL recommendations. The sub-sector is found to target a niche of clients which are resident in Monaco with nationality from common law countries with trust law. Services provided are limited to settling testamentary trusts under Law No. 214 allowing for foreign-law trusts to be created in or transferred to Monaco under certain conditions. Substantial controls apply, thanks to legal obligations to use a registered domestic trustee or foreign trustee with local representative, subject to checks and approval by the Public Prosecutor and Court of Appeals. Most of the entities acting as domestic trustees or local representatives of foreign trustees are entities which also perform other AML/CFT regulated activities such as legal advisory services. There are also legal obligations to register the trust with the DDE and provide data on beneficial ownership that allows for screening and monitoring by DDE. No links of BOs to sanctioned individuals/entities and no links to higher-risk jurisdictions, and only 1 link to a PEP (without adverse information), were identified for this particular subset of trusts. Given

the combination of medium-low inherent risks and substantial controls, residual sub-sectorial risks are assessed as **low.**

21. Going forward, based on the findings of the SRA, the following **priorities for the private sector** are identified:

22. **TCSP companies** should further enhance controls relating to customer risk assessment (CRA), customer due diligence and enhanced due diligence, to better manage their exposure to very high customer risks. In particular, TCSPs should ensure that they distinguish all relevant risk factors in their CRA, such as customers' political exposure and net-worth; the complexity or opacity of their ownership and controls structures; the industry or geographic area in which they operate; their involvement in payments or instruments with a high potential for anonymity; and any links to higher-risk sectors. Furthermore, TCSPs should consider whether the risk levels applied to their customers are appropriate, as the current number of reported high-risk clients in their customer base points to possible tendencies to underestimate customer risks. TCSPs should also improve measures to investigate and record the customers' business and risk profile (e.g. business background, origin of their funds) and ensure that they carry out specific, timely and formalized enhanced checks in situations where they were called for, including for PEPs and links with higher-risk jurisdictions.

23. **Business centers** should build up and implement in a timely manner an internal AML/CFT framework to make sure that they comply with their new obligations under the AML/CFT Law. Their Boards and Senior Management should fully assume their oversight responsibilities in this respect and should approve the necessary policies and procedures, risk assessments, relationships with higher-risk clients and should allocate sufficient resources and powers to AML/CFT responsible persons. The new measures should also be applied to existing clients with whom the Business centers entered into a business relationship prior to the application of the AML/CFT regime to the sub-sector. In relation to KYC/CDD, it is of utmost importance that business centers should start to record all relevant data under the law and regulations, including the nationalities and residencies/place of incorporation of customers and BOs and that they distinguish higher-risk categories, e.g. PEPs, HNWIs, VASPs.

24. Progress on the above points will be monitored through ongoing supervision as well as through the next iteration of the sub-sectors' survey returns with data on inherent risks and controls for the 2023 period.

25. **Trustees under Article 3 of Law No 214** should ensure that they carry out adequate due diligence on all relevant parties to the trust and that they report all relevant information to the Register of Trusts in accordance with Law No 214 and Sovereign Ordonnance No 8.635. Local representatives of foreign

trustees should ensure that the respective roles and responsibilities in this respect are clear between them and that they have full information to avoid risks of getting caught up in opaque ML/TF schemes.

26. Furthermore, the following priorities are to be set for risk-based supervision in the upcoming supervisory cycle, to address findings of the SRA:

27. AMSF will target the **TCSP companies** with high residual risks for full-scope inspections, placing emphasis on areas where their inherent risks were considered particularly high or controls particularly weak. The two TCSPs which have not been subject to an inspection in recent years will be prioritized in this respect, so their controls can be assessed, which may lead to changes in their residual risk ratings. Furthermore, given the SRA's findings on the relative weakest areas of controls in the sub-sector, AMSF will consider the following themes for thematic inspections of TCSP companies: Customer risk assessment and risk-based approach to CDD; Links to higher-risk countries, PEPs and EDD; STR filing; TFS screening.

28. AMSF will carry out its first inspections of **business centres** since they have been brought in scope of the AML/CFT regime. The first inspections will focus on those entities which are considered higher risk than peers mostly due to considerations related to the volume of their activities (size of client base, share of addresses and PO boxes provided), as those are the areas where survey data provided by business centres can currently be considered most reliable.

29. AMSF will carry out risk-identifying inspections on **trustees** that are administering testamentary trusts settled in Monaco under foreign law, to further build up the understanding of the risks that they are exposed to and the controls that they apply. Those domestic trustees which are not already regulated for AML/CFT purposes due to other activities will be prioritized. Following the outcomes of these inspections, AMSF will consider whether a separate offsite reporting regime should be introduced for trustees as it applies to the other sub-sectors. Given the delivery channel risks in relation to foreign trustees, AMSF will further seek to obtain information from their foreign home supervisors to ascertain whether any serious integrity concerns or AML/CFT shortcomings were identified in relation to these trustees, and will follow up with the local representatives of such trustees if needed.

30. In the upcoming period, AMSF will also publish a range of **guidance papers** which will help TCSPs further enhance controls, and which will help business centres build up effective control frameworks. Notably, AMSF plans to publish guidance on business risk assessment, treatment of PEPs, STR filing and TFS.

31. Finally, Monaco will keep an eye on global, regional and national developments, and periodically update the SRA to ensure that it continues to focus resources on those subsets of the sector where its actions add most value.