The EU AML/CFT List of High-Risk Third Jurisdictions: Implications and Options for The Bahamas

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Abstract

This Policy Brief argues that inclusion on any future adopted European Union (EU) AML/CFT list of high-risk third jurisdictions would be problematic for The Bahamas for three main reasons. First, EU 'obliged entities' will be required to conduct enhanced client due diligence (ECDD) on transactions involving Bahamian clients and Bahamian intermediaries. Secondly, while no sanctions are involved, noncompliance for an international financial center like The Bahamas might entail reputational fallout at a time when Caribbean countries are facing the loss of correspondent banking relationships (CBRs) due to the de-risking practices of large global banks, with the attendant implications for the ease of doing business, cross-border trade and financial transaction flows. Thirdly, The Bahamas will now be expected to comply with another set of rules defined by a body of which it is not a member and where it has little or no opportunity to influence the methodology by which it is being assessed.

JEL Codes: G1, E5

Keywords: anti-money laundering/countering the financing of terrorism (AML/CFT), European Union (EU), high-risk jurisdiction

I. Introduction

On February 13, 2019,[1] the Commonwealth of The Bahamas (The Bahamas), along with 22 other jurisdictions, was included on an updated list of high-risk third jurisdictions with strategic deficiencies in their anti-money laundering/countering the financing of terrorism (AML/CFT) regimes published by the European Commission (the Commission) of the European Union (EU). The list stems from an increased impetus by the EU to step up its AML/CFT monitoring in the wake of several major money laundering scandals involving European banks in recent years. On March 5, 2019, the EU Council rejected this expanded list, which included 11 jurisdictions not included on the Financial Action Task Force (FATF) list of High-Risk and Other Monitored Jurisdictions. The Commission is presently working on formulating another list to be presented to the EU Council and Parliament for approval.

This Policy Brief offers some reflection on the EU's AML/CFT list, with a specific focus on the implications for The Bahamas and available policy options. The Bahamas is currently identified by FATF as 'a jurisdiction with strategic deficiencies for which they have developed an action plan with FATF'.[2] Being on any future adopted EU AML/CFT list of high-risk third jurisdictions would have several additional implications for The Bahamas.[3] Firstly, EU obliged entities,[4] such as financial institutions and certain professionals, will be required to conduct enhanced customer due diligence (ECDD) on transactions involving Bahamian clients and those involving Bahamian intermediaries.[5] Secondly, while no sanctions are involved, noncompliance for an international financial center (IFC) like The Bahamas might entail reputational fallout at a time when Caribbean countries are already facing the loss of correspondent banking relationships (CBRs) due to the de-risking practices of large global banks, with the attendant implications for the ease of doing business, cross-border trade, and financial transaction flows. Thirdly, The Bahamas will now be expected to comply with another set of rules defined by a body of which it is not a member and has little or no opportunity to influence the methodology by which it is being assessed.

[1]The European Union (EU) had also included the Bahamas on its list of non-cooperative tax jurisdictions. However, it removed The Bahamas from its non-cooperative jurisdictions list in March 2019 after the recent passage of tax compliance laws in Parliament and its continued engagement with the EU's tax watchdog.

[2] The other jurisdictions on this list are Botswana, Cambodia, Ethiopia, Ghana, Pakistan, Serbia, Sri Lanka, Syria, Trinidad & Tobago, Tunisia and Yemen. The current list (of February 22, 2019) is available here: http://www.fatf-gafi.org/countries/a-c/bahamas/documents/fatf-compliance-february-2019.html.

[3] Three times a year, FATF releases two public statements. The first identifies the jurisdictions that have strategic AML/CFT deficiencies for which they have developed an action plan with the FATF. The Bahamas is included on this list. The second and more serious of the two identifies (i) jurisdictions subject to a FATF call on its members and other jurisdictions to apply counter-measures to protect the international financial system from ongoing and substantial money laundering and financing of terrorism (ML/FT) risks, and (ii) jurisdictions subject to a FATF call on its members and other jurisdictions to apply enhanced due diligence measures proportionate to the risks arising from the jurisdiction.

[4] These are entities defined as such under Article 2 of the Fourth EU AML Directive (Directive (EU) 2015/849) and as amended by the Fifth EU AML Directive (Directive (EU) 2018/843. These include credit institutions, financial institutions, and several categories of natural or legal persons acting in the exercise of their professional activities, such as tax advisors and estate agencies. They also now include providers engaged in exchange services between virtual and fiat currencies, custodian wallet providers, and persons trading or acting as intermediaries in the trade of works of art where the value of the transaction amounts to EUR 10,000 or more.

[5] Enhanced due diligence is already required if the jurisdiction is on the FATF list.

This brief is organized as follows: Section 2 provides background on the EU's list and discusses the EU methodology. Section 3 looks specifically at The Bahamas' inclusion on the draft EU list, which was rejected by the Council. Sections 4 and 5 discuss the implications of the possible inclusion of the Bahamas on any future adopted EU list and some possible policy options for The Bahamas to avoid such inclusion. Section 6 concludes.

II. Background

In recent years, an unprecedented slew of high-profile money laundering scandals has rocked the European banking system, resulting in fines for some banks. The lack of compliance has raised concern about shortcomings in the EU's AML/CFT regime.[6] As a result, the EU stance on AML/CFT became stricter, and the European Council, in its conclusions on the EU's Anti-Money Laundering Plan, described the fight against AML/CFT as a "high priority" for the EU.[7]

The legal basis for the EU's formulation of its most recent AML/CFT list of high-risk jurisdictions stems from two directives: Directive (EU) 2015/849 (Fourth Anti-Money Laundering Directive) and Directive (EU) 2018/843 (Fifth Anti-Money Laundering Directive).[8]

The Fourth Anti-Money Laundering Directive on the prevention of the use of the financial system for the purposes of money laundering or terrorist financing was adopted on May 20, 2015. It has the stated aim of "preventing the use of the Union's financial system for the purposes of money laundering and terrorist financing."[9] Article 9 requires the Commission to adopt delegated Acts in accordance with Article 64 of that directive to identify third-country (non-EU) jurisdictions having strategic deficiencies in their AML/CFT regimes, which pose a threat to the EU financial system and internal market. The stated objective of the identification of high-risk third jurisdictions is to protect the integrity of the EU's financial system and internal market. A delegated act under Article 9 will only enter into force once no objection has been expressed by either the European Parliament or Council within a month of their notification of said delegated act, or once both institutions have informed the Commission that they have no objections.[10]

The Fifth Anti-Money Laundering Directive originated following a proposal by the Commission in July 2016 in the aftermath of terrorist attacks and the Panama Papers Scandals, and was part of the Action Plan of the Commission of February 2016.[11] The directive came into force on July 9, 2018, and must be implemented by Member States in their national legislation by January 10,

[6] The biggest have included the Estonian subsidiary of the Copenhagen-based Danske Bank, Latvia's ABLV Bank, and Sweden's Svedbank.
[7] https://www.consilium.europa.eu/media/37283/st15164-en18.pdf
[8] The EU adopted its first AML directive, Council Directive 91/308/EEC of 10 June 1991, on the prevention of the use of the financial system for the purpose of money laundering. It focused on drug offences and placed obligations only on the financial sector. The second directive, Directive 2001/97/EC of the European Parliament and Council, widened the scope to encompass a larger number of crimes and professions. The third Directive, 2005/60/EC of the European Parliament and Council, took into account the FATF's revisions of its Recommendations.
[9] Article 1 of the Directive (EU) 2015/849.
[10] Article 64(5) of the Fourth AML Directive (2015/849).
[11] See the Statement by First Vice-President Timmermans, Vice-President Dombrovskis, and Commissioner Jourova on the adoption by the European Parliament of the Fifth Anti-Money Laundering Directive of April 19, 2018:

2020. Inter alia, it expanded the criteria to be considered by the Commission in assessing high-risk third countries under Article 9 of the Fourth Anti-Money Laundering Directive.[12]

The first list of third countries identified as having strategic deficiencies in their AML/CFT regimes was adopted on July 14, 2016, by Delegated Regulation (EU) 2016/1675.[13] This list was further amended by Delegated Regulation (EU) 2018/105,[14] Delegated Regulation (EU) 2018/212,[15] and Delegated Regulation (EU) 2018/1467. The new updated list was published in the form of another Delegated Regulation (EU) on February 13, 2019[16] and submitted to the European Parliament and Council for approval. On March 5, 2019, the EU Council rejected this new list, mainly due to EU Member States' objection to the inclusion of Saudi Arabia and the five U.S. territories of American Samoa, Guam, Puerto Rico and the U.S. Virgin Islands.[17] Therefore, the list has not been adopted and the Commission will have to formulate another.

The FATF vs the EU

The Financial Action Task Force ("FATF") is the recognized international standard-setting body regarding AML/CFT[18]. It is an inter-governmental body established in 1989 to "set standards and to promote effective implementation of legal, regulatory and operational measures for combating money laundering, terrorist financing and the financing of proliferation and other related threats to the integrity of the international financial system" (FATF, 2018).

Previously, FATF only assessed jurisdictions based on their technical compliance with its FATF recommendations. Jurisdictions are rated as either Compliant, Largely Compliant, Partially Compliant or Non-Compliant on each of the 40 recommendations. The results are published in that country's Mutual Evaluation Report (MER), and wherever necessary, in follow-up reports.

However, under its new methodology adopted in 2013, jurisdictions are now assessed not just on their technical compliance with the FATF recommendations, but also on the effectiveness of their AML/CFT regimes, that is, the extent to which they achieve their defined outcomes.[19] This High-Level Objective is: "financial systems and the broader economy are protected from the threats of money laundering and the financing of terrorism and proliferation, thereby strengthening financial sector integrity and contributing to safety and security" (FATF, 2013 p.15).

[12] It also requires public beneficial ownership registers for companies, beneficial ownership of trusts will be available to competent authorities, tackling TF risks associated with anonymous use of virtual currencies and pre-paid instruments, increased cooperation and exchange of information between AML supervisors and with the European Central Bank and broadens the criteria for assessing high risk third-country jurisdictions. See Factsheet available here: https://ec.europa.eu/cyprus/news/20180709_2_en.
[13] This list included Afghanistan, Bosnia and Herzegovina, Guyana, Iraq, Lao People's Democratic Republic, Syria, Uganda, Vanuatu, Yemen, Iran, and Korea.
[14] Ethiopia was added to the list of High-Risk Third Countries.
[15] Pakistan was added to the list of High-Risk Third Countries.
[16] http://europa.eu/rapid/press-release_IP-19-781_en.htm
[17] https://www.reuters.com/article/us-eu-saudi-moneylaundering/eu-states-block-putting-saudi-arabia-u-s-territories-on-dirty-money-list-idUSKCN1QI4RZ
[18] While the FATF is based at the headquarters of the Organisation for Economic Co-operation and Development (OECD) and the two organizations work closely together, they have separate mandates.
[19] See FATF Methodology 2013 as updated February 2019.

Effectiveness is assessed in a fundamentally different way from technical compliance. As stated in the revised FATF methodology, an assessment of effectiveness "does not involve checking whether specific requirements are met or whether all the elements of a recommendation are in place. Rather it "requires a judgement as to whether the key objectives of an AML/CFT system, in line with the FATF standards, are being effectively met in practice."[20] FATF makes its assessment of effectiveness based on 11 immediate outcomes, each of which represents one of the key goals to be achieved by an effective AML/CFT system. These are further linked to three intermediate outcomes representative of the major thematic goals of AML/CFT measures.

Under each Immediate Outcome, the effectiveness of a jurisdiction is rated as either 'High Level of effectiveness', 'Substantial Level of effectiveness', 'Moderate level of effectiveness' and 'low level of effectiveness'.

Three times yearly FATF releases two public documents in which it identifies jurisdictions with strategic AML/CFT deficiencies based on the FATF's International Co-operation Review Group (ICRG) analysis.[21] The first is the FATF Public Statement (call for action) and the second is the Improving Global AML/CFT Compliance: On-going Process (other monitored jurisdictions).[22] The Bahamas is on the latter list.

The European Commission is one of the 38 members of the FATF, while 13 EU Member States are also FATF members in their own right.[23] The Council of Europe Committee of Experts on the Evaluation of Anti-Money Laundering Measures and the Financing of Terrorism (MONEYVAL) is a FATF Associate Member.

In 2017, the European Parliament, in the report of its Committee of Inquiry into money laundering, tax avoidance, and tax evasion, "regretted that the process of FATF assessment and peer review had resulted in a list which is not useful for tackling money laundering."[24] It argued that being taken off the FATF list should not be made simply after undertaking commitments to institute reforms, but "following a thorough FATF evaluation confirming the existence of changes in practice."[25]

The Commission sees the FATF list as a baseline and has gone further to formulate its own methodology for identifying high-risk jurisdictions. The EU methodology encompasses three major phases: (i) a scoping phase, (ii) a listing phase, and (iii) an assessment phase. It considers jurisdictions identified by the FATF as having strategic deficiencies as its starting point for assessing high-risk third jurisdictions. It further relies on criteria from EU anti-money laundering

[20] See FATF Methodology 2013 as updated February 2019.
[21] The ICRG was established in 2007. It analysis high risk jurisdictions and makes recommendations on the specific actions to be taken to achieve compliance. See more here: https://www.fatf-gafi.org/publications/high-riskandnon-cooperativejurisdictions/more/moreabouttheinternationalco-operationreviewgroupicrg.html?hf=10&b=0&s=desc(fatf_releasedate)
[22] Countries have the opportunity to respond to findings from the MER and powerful countries may be able to influence some aspects of the process more than others.
[23] These are Austria, Belgium, Denmark, Finland, France, Germany, Greece, Iceland, Italy, Luxembourg, the Kingdom of the Netherlands , Spain and Sweden. See https://www.fatf-gafi.org/about/membersandobservers/
[24] http://www.europarl.europa.eu/doceo/document/A-8-2017-0357_EN.html#title1
[25] Ibid.

legislation, the Commission, other information sources such as Europol, European External Action Services, and the EU list of non-cooperative tax jurisdictions. It should be noted that this methodology applies only to third States, not EU Member States.

Based on the abovementioned methodology, the EU in its scoping phase identified 132 jurisdictions on November 15, 2018. Of these 132 jurisdictions, 54 were identified as "Priority 1" jurisdictions on the basis of (i) being on the FATF list or (ii) being exposed to a high level of threat identified by Europol/European External Action Service; being on the EU list of non-cooperative tax jurisdictions or being identified by Europol; jurisdictions de-listed by the FATF since July 2016 (but still listed on the former processes); and jurisdictions identified by Europol and the FATF during their mutual evaluation processes.[26]

The EU in its assessment phase eventually formulated a list of 23 jurisdictions which it deemed to have strategic deficiencies in their AML/CFT regimes. They were assessed based on the criteria outlined: insufficient criminal sanctions in place in the case of AML/CFT, insufficient application of customer due diligence requirements by financial institutions or non-financial intermediaries, insufficient powers of competent authorities and low levels of sanctions in case of breaches, insufficient international cooperation with Member States, lack of transparency on the real owners of companies and trusts, and insufficient implementation of targeted financial sanctions based on United Nations (UN) resolutions.[27]

The remaining jurisdictions are deemed "Priority 2" jurisdictions and will be assessed progressively by the Commission until 2025.

Jurisdictions Included on the Latest EU List – February 2019

Although the EU's first list was issued in 2016, the February 13, 2019, list is the first to be adopted utilizing the new methodology and criteria prescribed by the Commission pursuant to the Fifth Anti-Money Laundering Directive. Of the 23 jurisdictions identified, 16 were already on the EU list.[28] Moreover, 12 of the jurisdictions identified are on the FATF List of High-Risk and Other Monitored Jurisdictions, while 11 are additional jurisdictions added by the EU in accordance with its methodology.

[26] See European Commission Fact Sheet entitled "Anti-money laundering: Q&A on the EU list of high-risk third countries" of February 13, 2019, which details the process: http://europa.eu/rapid/press-release_MEMO-19-782_en.htm
[27] Ibid.
[28] The Commission de-listed five countries: Bosnia-Herzegovina, Guyana, Lao People's Democratic Republic, Uganda, and Vanuatu.

The 23 jurisdictions listed as having strategic deficiencies in their AML/CFT regimes as of February 13, 2019, are presented in the table below:

JURISDICTIONS ON EU AML/CFT LIST – FEBRUARY 13, 2019			
Jurisdictions on FATF list		**Additional jurisdictions identified by the Commission**	
NO.	**JURISDICTION**	**NO.**	**JURISDICTION**
1	The Bahamas	1	Afghanistan
2	Botswana	2	American Samoa
3	Democratic People's Republic of Korea	3	Guam
4	Ethiopia	4	Iraq
5	Ghana	5	Libya
6	Iran	6	Nigeria
7	Pakistan	7	Panama
8	Sri Lanka	8	Puerto Rico
9	Syria	9	Samoa
10	Trinidad & Tobago	10	Saudi Arabia
11	Tunisia	11	US Virgin Islands
12	Yemen		

Source: FATF List of High Risk and Other Monitored Jurisdictions (February 22, 2019) http://www.fatf-gafi.org/countries/#high-risk

Unlike the FATF, which provides detailed country-specific information through the MERs, the EU did not provide any specific reasons for the inclusion of each jurisdiction other than noting that the listed jurisdictions met at least one of the following criteria: (i) they have a systemic impact on the integrity of the EU financial system, (ii) they are reviewed by the International Monetary Fund as international offshore financial centers, and (iii) they have economic relevance and strong economic ties with the EU.[29]

III. The Bahamas

As an IFC, The Bahamas is vulnerable to both actual and perceived ML/TF risks. It is constantly obliged to allocate scarce resources to comply with ever-shifting goal posts on international standards and best practices in myriad areas, including AML/CFT. It must take steps to continually update its regulatory and legislative framework to protect the integrity of its own financial system and maintain its reputation as a well-regulated jurisdiction for business. The Bahamas is a member of the Caribbean Financial Action Task Force (CFATF), one of several FATF-style regional bodies, and is currently included on the CFATF List of High Risk and Other Monitored Jurisdictions.

[29] http://europa.eu/rapid/press-release_IP-19-781_en.htm

Fourth CFATF MER

Technical Compliance

In its Fourth CFATF MER published July 2017, The Bahamas' main strengths with regard to technical compliance were in the following areas: international cooperation, preventive measures for financial institutions (FIs) and designated non-financial business or professions (DNFBPs) and criminalization of money laundering and terrorist financing. According to the CFATF, although the legislative framework for the supervisory regime is well developed, sanctions need to be improved. The main deficiencies in technical compliance involved (i) targeted financial sanctions for terrorist financing and financing of proliferation, (ii) understanding and assessing national ML/TF risks and developing AML/CFT national strategies, and (iii) transparency and beneficial ownership of legal persons and arrangements. [30]

The Bahamas' technical compliance ratings are presented in the table below:

Description	**Recommendation**	**Rating**
AML/CFT policies and coordination	R.1	PC
	R.2	PC
Money laundering and confiscation	R.3	C
	R.4	C
Terrorist financing and financing of proliferation	R.5	LC
	R.6	NC
	R.7	PC
	R.8	PC
Preventive measures	R.9	C
	R.10	PC
	R.11	LC
	R.12	PC
	R.13	C
	R.14	C
	R.15	PC
	R.16	LC
	R.17	PC
	R.18	PC
	R.19	PC
	R.20	C
	R.21	C
	R.22	PC
	R.23	PC
	R.24	PC

[30] https://www.fatf-gafi.org/media/fatf/documents/reports/mer4/cfatf-4meval-bahamas.pdf

Transparency and beneficial ownership of legal persons and arrangements	R.25	PC
Powers and responsibilities of competent authorities and other institutional measures	R.26	PC
	R.27	PC
	R.28	PC
	R.29	C
	R.30	PC
	R.31	LC
	R.32	PC
	R.33	PC
	R.34	LC
	R.35	PC
International Cooperation	R.36	LC
	R.37	LC
	R.38	LC
	R.39	LC
	R.40	LC

Source: CFATF (2017).

Effectiveness

Under the area of effectiveness, The Bahamas was rated as effective in supervision and preventive measures due to what the CFATF termed its "robust" AML/CFT supervisory regime and the level of compliance of FIs and DNFBPs. However, the CFATF found weaknesses in the following areas: ML/TF confiscations, investigations, prosecutions and convictions, the identification of national ML/TF risks and development of appropriate AML/CFT strategies and proliferation financing financial sanctions.

The Bahamas scored less favorably in the area of effectiveness, achieving a rating of 'low' for 6 of the immediate outcomes and 'moderate' for 5. A rating of 'low' means that the "immediate outcome is not achieved or achieved to a negligible extent and fundamental improvements are needed." A rating of 'moderate' means the "immediate outcome is achieved to some extent. Major improvements are needed."[31]

Immediate Outcome (IO)	Description	Rating
IO.1	Risk, policy and coordination	Low
IO.2	International cooperation	Moderate
IO.3	Supervision	Moderate
IO.4	Preventive measures	Moderate
IO.5	Legal persons and arrangements	Moderate

[31] See FATF Methodology 2013, updated February 2019.

IO.6	Financial intelligence	Moderate
IO.7	ML investigation and prosecution	Low
IO.8	Confiscation	Low
IO.9	TF investigation and prosecution	Low
IO.10	TF preventative measures and financial sanctions	Low
IO.11	PF financial sanctions	Low

Source: CFATF (2017).

The Bahamas' 1st Enhanced Follow-up Report

As a result of its ratings in the May 2017 CFATF Fourth Round MER, the CFATF placed The Bahamas in enhanced follow-up. In its 1st Enhanced Follow-up Report (FUR) on The Bahamas' technical compliance dated December 2018, the CFATF gave The Bahamas a re-rating on Recommendations: 1, 2, 6, 10, 12, 15, 17, 18, 23, 25, 30, 32, and 35 as follows:

R1 – **Assessing risks and applying a risk-based approach** from *partially compliant* to *largely compliant*
R2 – **National cooperation and coordination** from *partially compliant* to *compliant*
R6 – **Targeted financial sanctions related to terrorism and terrorist financing** from *non-compliant to partially compliant*
R10 – **Customer due diligence** from *partially compliant* to *compliant*
R12 – **Politically exposed persons** from *partially compliant* to *compliant*
R15 – **New technologies** from *partially compliant* to *largely compliant*
R17 – **Reliance on third parties** from *partially compliant* to *compliant*
R18 – **Internal controls and foreign branches and subsidiaries from** *partially compliant* to *largely compliant*
R23 – **DNFBPs: other measures** – from *partially compliant* to *largely compliant*
R25 – **Transparency and beneficial ownership of legal arrangements** - from *partially compliant* to *largely compliant*
R30 – **Responsibilities of law enforcement and investigative authorities** from *partially compliant* to *compliant*
R32 – **Cash couriers** from partially compliant to largely compliant
R35 – **Sanctions** from partially compliant to largely compliant
Source: CFATF Follow-up Report: The Bahamas (December 2018): http://www.fatf-gafi.org/fr/publications/evaluationsmutuelles/documents/fur-bahamas-2018.html?hf=10&b=0&s=desc(fatf_releasedate)

Source: CFATF (2017).

However, while the CFATF welcomed the steps that The Bahamas had made on Recommendations 5, 7, 19, 22, 26, 27, 28, and 33, it found "insufficient progress" to justify a re-rating on those recommendations at that time. The Bahamas maintained the "largely compliant" rating for Recommendation 5, the "compliant" rating for Recommendation 21, and the "partially compliant" rating for Recommendations 7, 8, 19, 22, 26, 27, 28, and 33.[32]

[32] http://www.fatf-gafi.org/fr/publications/evaluationsmutuelles/documents/fur-bahamas-2018.html?hf=10&b=0&s=desc(fatf_releasedate)

Steps Taken by The Bahamas

In its comprehensive response to the Commission, The Bahamas outlined that the Commission failed to take into account The Bahamas' progress since its 2017 MER, including the CFATF's acknowledgement of this progress.[33] For instance, in its release in February 2019, CFATF remarked that The Bahamas had taken steps towards improving its AML/CFT regime,[34] highlighting the passage of the Register of Beneficial Ownership Act, 2018[35] and the Codes of Practice for lawyers, accountants, and the real estate sector.

The recent International Monetary Fund (IMF) Article IV 2018 Report on The Bahamas noted that the authorities are taking steps to strengthen their AML/CFT framework for domestic and offshore institutions. Legislation was amended to include general insurance companies in the AML/CFT requirements as well as the creation of an Analytics Unit at the central bank to perform better risk-focused assessments, increase requests for annual reporting, and enhance the central bank's support for more targeted examinations. The IMF staff stressed that it is critical to work closely with the CFATF and the FATF to promptly address the strategic deficiencies in the AML/CFT regime identified in the 2017 MER.

On August 29, 2018, the Central Bank of The Bahamas also released revised AML/CFT guidelines.[36] The Bahamas' Group of Financial Services Regulators (GFSR)[37] released its inaugural National AML/CFT Report in 2018. The report gave an overview of The Bahamas' AML/CFT supervisory landscape, recent legislative developments, and steps the government of The Bahamas is taking to address the concerns raised by CFATF in its last MER. These include passing legislation,[38] strengthening inter-agency cooperation, and establishing a Risk Framework Steering Committee. The GSFR report noted that in 2017, the FIU saw a 45.75 percent increase in the number of suspicious transaction reports (STRs) filed.[39]

According to data published in the GFSR report, there was a marked increase in the number of money laundering investigations, prosecutions, and convictions between 2015 and 2018. The chart below summarizes this data:

[33] Response to European Commission "High Risk Third Countries List" published by the Bahamian government, available at: https://bit.ly/2J1bKk1

[34] http://www.fatf-gafi.org/countries/a-c/bahamas/documents/fatf-compliance-february-2019.html

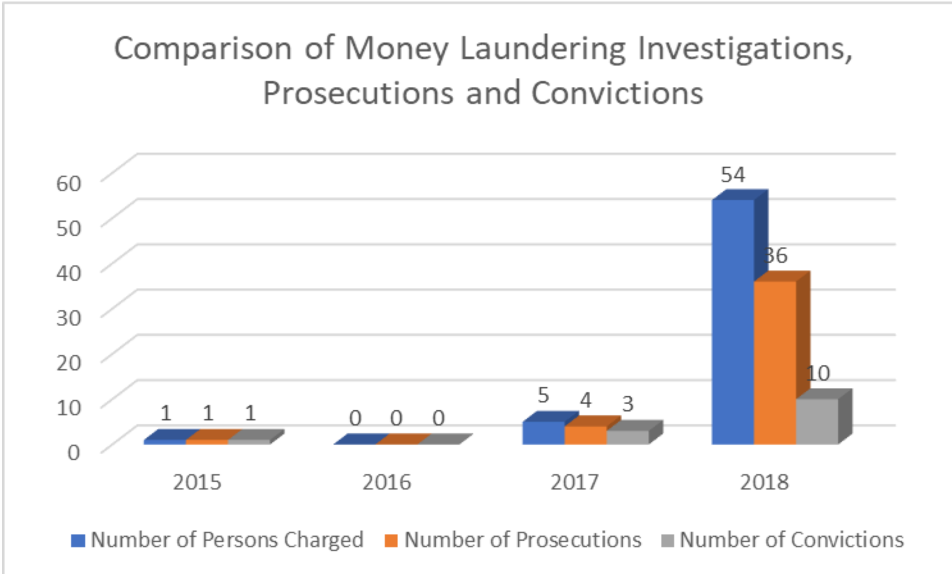
[35] This Act became law on December 31, 2018. It provides for the establishment by the Attorney-General of The Bahamas of a secure search system of databases managed by registered agents which hold beneficial ownership information of legal entities. The Act is available at: https://bfsb-bahamas.com/wp-content/uploads/2019/01/REGISTER-OF-BENEFICIAL-OWNERSHIP-ACT-31-DECEMBER-2018-GAZETTE-1.pdf

[36] See: https://www.centralbankbahamas.com/news.php/legal_guidelines.php?id=16449&cmd=view

[37] The GFSR, formed in 2002, comprises the Central Bank of the Bahamas, the Compliance Commission of the Bahamas, the Gaming Board for the Bahamas, the Insurance Commission of the Bahamas and the Securities Commission of the Bahamas. Together, these agencies have responsibility for ensuring the effective operation of The Bahamas' AML/CFT regime.

[38] See also the Financial Transaction Reporting Act (2018) which is available at: http://laws.bahamas.gov.bs/cms/images/LEGISLATION/PRINCIPAL/2018/2018-0005/FinancialTransactionsReportingAct2018_1.pdf.

[39] GSFR (2018).



Source: GFSR (2018).

The relevant bodies comprising the GFSR also increased their outreach activities through the publication of AML/CFT guidance notes, hosting an inaugural AML/CFT Risk Management Conference[40] and an AML/CFT website. It also mentioned the work of the FIU to increase AML/CFT training. The number of AML/CFT professionals trained by The Bahamas FIU per year increased from 853 in 2011 to 1196 in 2017.[41]

IV. Implications of any Future EU Listing

Perceived noncompliance with international AML/CFT best practices presents non-negligible implications for The Bahamas. Firstly, under the Fourth Anti-Money Laundering Directive, EU banks and other financial institutions will be required to apply ECDD when establishing business relationships or when dealing with transactions involving jurisdictions on the list. The Fifth Anti-Money Laundering Directive provides greater clarity about which ECDD is to be applied.[42] They include, for example, obtaining additional information on the customer and the beneficial owner, the intended nature of the business relationship, the source of funds and source of wealth of the customer and the beneficial owner, the reasons for the intended or performed transactions, requiring the approval of senior management for establishing or continuing the business relationship, and conducting enhanced monitoring of the business relationship by increasing the frequency and timing of controls applied and selecting patterns of transactions requiring further examinations.[43]

[40] This was held September 17-18, 2018: https://www.bahamasamlcft.com/.
[41] This is according to data published in the chart entitled "# of AML/CFT Professionals Trained" in Appendix IV: FIU Statistics (GFSR, 2018: 41).
[42] The Fifth Anti-Money Laundering Directive inserts a new Article 18a requiring Member States that, with respect to business relationships or transactions involving high-risk third countries identified by the Commission pursuant to Article 9(2), they are to require obliged entities to apply a wide range of ECDD measures outlined in Article 18a.
[43] Ibid.

Therefore, if The Bahamas is again included on any future EU AML/CFT list which is subsequently adopted, EU banks, other financial institutions, and certain professionals which fall under the definition of 'obliged entities' under Article 2 of the Fourth Anti-Money Laundering Directive, and as amended by the Fifth Anti-Money Laundering Directive, will be required to apply ECDD when establishing business relationships with Bahamian clients or when dealing with transactions involving Bahamian intermediaries. This enhanced scrutiny may impact The Bahamas' attractiveness as a domicile of choice for compliance-conscious investors. The recent passage of tax compliance laws in Parliament and continued engagement with the EU's tax watchdog will help keep The Bahamas off any future EU lists.

Secondly, although the EU directives do not mandate any sanctions or restrictions on trade relations or aid to be applied, the reputational fallout may lead to increased scrutiny by financial institutions in Europe and other jurisdictions. This is of particular concern at a time when The Bahamas, like other jurisdictions in the Caribbean, is facing the threat of withdrawal or restriction of correspondent banking relations as a result of the de-risking practices by large global banks. This has implications for the ease of doing business, cross-border trade, and other financial transactions which are the lifeblood of the Bahamian economy.

The IMF Article IV 2017 report suggests that The Bahamas has suffered no significant disruptions due to the loss of correspondent banking relationships (CBR). Using information from the central bank survey of CBR users, the IMF report shows that almost 26 percent of respondents, mostly concentrated in the offshore sector, have faced some restrictions or termination of CBR relations but have been able to continue activities through other existing relationships or their parent company (IMF Article IV Report). If The Bahamas is again included on an EU AML/CFT list which is subsequently adopted, EU banks will be required to observe this list as well as the FATF list. Although FATF advocates a risk-based approach, EU banks may find the risk of dealing with Bahamian banks too great to justify the provision of CBRs and may withdraw or restrict the provision of CBRs to Bahamas-based banks.

Thirdly, as the EU's methodology goes beyond the methodology of FATF, the international standard-setter for AML/CFT rules and best-practices, the EU list presents another set of rules defined by a few jurisdictions with which The Bahamas will now be expected to comply. The Bahamas is not an EU Member and will be judged based on a methodology which it has had no input in formulating. Moreover, The Bahamas also criticized the short time frame in which it was notified of the Commission's intention to include the country on its list.[44]

The EU's decision to create a separate list from the FATF list has been strongly criticized. The U.S Department of the Treasury Statement on the European List of Jurisdictions with Strategic AML/CFT Deficiencies, published on February 13, 2019, stated that "the U.S. Department of the Treasury has significant concerns about the substance of the list and the flawed process by which it was developed." The U.S. Treasury Department also categorically stated that it did not expect

[44] According to The Bahamas' response to the European Commission's High Risk Third Countries List, The Bahamas was only made aware of the possibility of being included on the list in January 21, 2019, via a memo from the EU's Jamaica-based Caribbean representative.

U.S. financial institutions to take the European Commission's list into account in their AML/CFT policies and procedures. However, unlike the United States, as a small IFC, The Bahamas cannot ignore the EU list.

V. Policy Options for The Bahamas

On March 5, 2019 the EU Council unanimously rejected the Commission's new list. The Council stated that it "cannot support the current proposal that was not established in a transparent and resilient process that actively incentivizes affected countries to take decisive action while also respecting their right to be heard."[45] The next step for the Commission will be to formulate and present a new list for the Council and Parliament's approval. This gives The Bahamas some time to again reach out to the Commission to indicate the steps it has been taking to achieve progress on AML/CFT compliance and which have been recognized by CFATF. A similar lobbying effort was successful in getting The Bahamas removed from the EU's List of non-cooperative tax jurisdictions in March 2019.

However, given that the EU's starting point for its list is a jurisdiction's inclusion on the FATF List of High Risk and Other Monitored Jurisdictions, a major factor for The Bahamas' inclusion on the EU list of February 2019 was its presence on the FATF list. The priority for The Bahamas, therefore, should be on trying to achieve compliance with the FATF requirements, particularly the areas highlighted by CFATF for further work, in order to be de-listed from the FATF list. This should reduce the likelihood that The Bahamas will be included on the revised Commission list. It should also be noted that Guyana, which had been included on the 2016 EU list, is no longer on the FATF list of High Risk and Other Monitored Jurisdictions and was not included in the European Commission's February 2019 list.

Specifically, the FATF compliance report of 2019 outlines the steps that The Bahamas should take to implement its action plan to address its strategic deficiencies. These include the following:

(1) "developing and implementing a comprehensive electronic case management system for international cooperation;
(2) demonstrating risk-based supervision of non-bank financial institutions;
(3) ensuring the timely access to adequate, accurate and current basic and beneficial ownership information;
(4) increasing the quality of the FIU's products to assist LEAs in the pursuance of ML/TF investigations, specifically complex ML/TF and stand-alone ML investigations;
(5) demonstrating that authorities are investigating and prosecuting all types of money laundering, including complex ML cases, stand-alone money laundering, and cases involving proceeds of foreign offences;
(6) demonstrating that confiscation proceedings are initiated and concluded for all types of ML cases; and

[45]See Statement by the EU Council here: https://data.consilium.europa.eu/doc/document/ST-6964-2019-REV-1/en/pdf

(7) addressing gaps in the TF and PF TFS frameworks and demonstrating implementation."[46]

In the interim, it is also important for the Bahamian authorities to continue their public awareness and outreach activities to local stakeholders, as well as to external stakeholders such as financial regulators, financial institutions, and correspondent banks in the EU and in other third jurisdictions to keep them abreast of the progress The Bahamas is making on its FATF compliance.

V. Conclusions

This Policy Brief has argued that inclusion on any future adopted EU AML/CFT list of high-risk third jurisdictions would be problematic for The Bahamas for three main reasons. Firstly, EU obliged entities will be required to conduct ECDD on transactions involving Bahamian clients and on transactions involving Bahamian intermediaries. Secondly, while no sanctions are involved, noncompliance for an IFC like The Bahamas might entail reputational fallout at a time when Caribbean countries are facing the loss of CBRs due to the de-risking practices of large global banks, with the attendant implications for the ease of doing business, cross-border trade, and financial transaction flows. Thirdly, The Bahamas will now be expected to comply with another set of rules defined by a body of which it is not a Member and where it has little or no opportunity to influence the methodology by which it is being assessed. It may be important to highlight the importance of focusing on effectiveness, which is connected with institutional strengthening of supervisory and regulatory agencies of DNFAPs

Going forward, to avoid being included on the Commission's revised list, The Bahamas should prioritize addressing the outstanding issues highlighted by CFATF in order to be de-listed from the FATF list of High-Risk and Other Monitored Jurisdictions. Bahamian authorities should also continue their public awareness and outreach activities to local stakeholders, as well as to external stakeholders, such as regulators, financial institutions, and banks in the EU and third States to ensure that they are kept aware of The Bahamas' commitment and progress toward FATF compliance.

[46] http://www.fatf-gafi.org/countries/a-c/bahamas/documents/fatf-compliance-february-2019.html

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