

The Central Bank of The Bahamas BANK SUPERVISION DEPARTMENT
Quarterly Letter to All Senior Officials 04/13
Email: Email Address Licensee: Name

Dear Senior Official,

At the onset of 2014, we would like to convey New Year's greetings to you, and our commitment to continue to pursue activities that strengthen our domestic regulatory landscape.

We are optimistic as we continue on track with our various strategic regulatory initiatives, at a time when the global banking sector is showing sign of a slow but steady emergence from the effect of the economic slump, triggered by the financial crisis. The various segments of our banking sector appear to reflect these global markers. Commercial Banking, notwithstanding protracted challenges in certain niche areas, has experienced some improvement in asset quality and delinquencies, but with increased demands for operational efficiencies and calls for enhanced capital adequacy, both here and in their home jurisdictions. The offshore banking sector, driven largely by regulatory initiatives elsewhere, has been experiencing increased volume of deposits and liquidity, and the concomitant challenges of placing these funds profitably in the low-interest environment and volatile capital markets.

The immediate and urgent regulatory response to the crisis is nearly over, and the international standard setters' work on capital adequacy, systemically important banks (global and domestic), liquidity, and leverage is nearly complete. For the regulators themselves, the challenge over the next few years is to ensure that these changes are rolled out globally, in a manner that is commensurate with the economic realities of individual jurisdictions, and to sustain these changes against the backdrop of rising operational/compliance costs.

Turning to a few domestic developments, licensees and registrants will have noticed that invoices for annual licence and registration fees for the year 2014 have not yet been issued by the Central Bank. You will already be aware of the changes made to these fees via the Banks and Trust Companies (Amendment) Regulations, 2013 (Statutory Instrument No. 66 of 2013), which amends the Third Schedule of the Banks and Trust Companies Regulation Act and came into force on 1st July, 2013. While these amending

Regulations set out the new fees payable by licensees as of 1st July, 2013, the Ministry of Finance advised that queries raised by the industry concerning the increases were under review. Central Bank has now been advised that the fees for pure Public Trust companies, reflected in the 2013 Regulations as \$52,500.00, will be reduced to \$42,500.00, and that new amending legislation to this effect is forthcoming. Based on this latest information, invoices are being processed and licensees should expect to start receiving these by end-January, 2014. Please note that both the Registry and Public Treasury have been made aware of the circumstances surrounding delays in distributing invoices and effecting payments.

On policy matters, there has been minimal activity in terms of the release of new and amended guidelines in the last quarter of 2013. To recap, we have revised the **Guidelines on the Prevention of Money Laundering and Countering the Financing of Terrorism**, as released on 23rd September 2013. You may recall that the amendment clarifies the date when a person ceases to be a facility holder in a manner that is consistent with the Financial Transactions Reporting Act, 2000. Specifically, bullet point (iii) was removed from paragraph 200 of the Guidelines.

On 25th November 2013, we released the **Guidelines for the Management of Operational Risk**, which provide high level principles and minimum policies and procedures that licensees should maintain in relation to their overall operational risk management. They also now incorporate the *Principles for the Sound Management of Operational Risk* issued by the Basel Committee on Banking Supervision in 2011. While the Guidelines delineate the sound practices around operational risk management, licensees are expected to have a risk management regime appropriate to size and complexity of their operations.

We wish to highlight a significant operational change impacting the non-licensee Registered Representatives, due to the repeal of Regulation 9 of the Banks and Trust Companies (Private Trust Companies) Regulations, 2007, by the **Banks and Trust Companies (Private Trust Companies) (Amendment) Regulations, 2012**. In contrast to Regulation 9 which called for the annual renewal of Registered Representative Certificates on the 1st day of January in each year, each existing non-licensee Registered Representative will each now receive a perpetual registration certificate, commencing January 2014. Likewise, all new non-licensee Registered Representatives will receive perpetual registration certificates upon registration by the Central Bank.

On the onsite examination front, we wish to draw your attention to several thematic areas identified from our review of the management of reputation risk at various licensees, and our expectations for how observed gaps should be addressed.

- **Confirmation of Source of Wealth for High Risk Clients.** For relationships/accounts that have been assessed as high risk by the licensees, there is an obligation to ensure that information on the files adequately documents the source of wealth for the account holders—as required under Section A paragraph 51 of the KYC/AML Guidelines. Confirmation may include independent evidence that supports the source of a person’s wealth; e.g., financial statements, wills, trust documentation, bill of sale, sales agreement, etc. It is not sufficient to merely record on an account opening form that the individual inherited a specific amount of money, or to include an article from an Internet search engine, such as Google, on file. Evidence that corroborates and/or supports that statement is needed. It should be noted that this approach is not unique to the Central Bank of The Bahamas, but is consistent with practices in other regulatory agencies.
- **Periodic Reviews for High Risk Clients.** These reviews should be performed on high-risk clients, at least, annually. Paragraph 35 of the AML Guidelines envisages a systematic process whereby periodic reviews are performed of all client relationships. For commercial banks, which have a large client base, the Central Bank expects that a process is in place to ensure that high risk clients are reviewed, at least annually, in a comprehensive manner. This process should include, but not be limited to, reviewing transactions to determine if they align with the account opening documents, amendments of current profile to reflect the current parameters, updating the identification and verification documents, downgrading/upgrading of risk assessed, etc.
- **Independence of the Compliance Function.** The independence of the Compliance function must reflect the requirements of the Corporate Governance Guideline. We wish to underscore that persons who function in a *compliance* role, but are not specifically positioned in the Compliance Department, should have a functional reporting line (“dotted line reporting” if appropriate) to the Head of Compliance, in the context of their compliance role. Additionally, the Head of Compliance should provide input into the performance appraisals of persons performing compliance functions, which is to ensure that the compliance role maintains independence and that quality of the work performed by those individuals is appropriately assessed and monitored.
- **Training of Persons with Compliance Responsibilities.** We wish to emphasize that licensees should ensure that persons who carry out the compliance function are sufficiently trained and are able to effectively

demonstrate their knowledge of compliance matters. In the case of the commercial banks, such training should also be extended to compliance personnel at the branch level.

In terms of new strategic initiatives, we were pleased to officially roll-out our formal **Basel II and III Implementation Program**, at an Industry Briefing we hosted on Tuesday, 29th October, 2013. The briefing was attended by representatives from nearly seventy (70) invited banks and other industry stakeholders impacted by the Basel Program. The implementation of the Basel road map is segmented into three (3) phases, that commenced in Q3 of 2013 and is expected to be completed in Q4 of 2015, with the planned 'go live' date for Q1 of 2016. We would encourage you to review the road map which has been published on the Central Bank's website.

As part of the Basel implementation program, the Central Bank is scheduled to release a Basel Readiness Survey within the coming weeks, for completion by the affected public licensees. The survey responses will not only allow us to assess licensees' readiness for implementation of the Basel II and III approaches, but will also provide useful input into the development and fine-tuning of the Basel framework for The Bahamas.


Another important strategic initiative slated for 2014 is our planned assumption of the supervisory mandate for financial co-operative credit unions. Upon passage of the new governing legislation, the Central Bank will have regulatory and supervisory oversight for these entities, which currently number seven (7) and have total footings estimated at \$310.9 million as at 31st March 2013. In anticipation of this additional responsibility in the domestic space, and to accurately reflect the expanded mandate, the name of the Commercial Banking Unit ('the Unit') has been changed to "**Domestic Financial Institutions Unit**", effective 31st December, 2013.

Again, let me thank all of you for your cooperation on supervisory matters this past year, and we look forward to a very productive engagement in the year ahead.

Any questions regarding this letter should be directed to:

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Sincerely,

A handwritten signature in black ink, appearing to read 'Abhilash D. Bhachech', with a horizontal line underneath the name.

Abhilash D. Bhachech
Inspector of Banks & Trust Companies

14th January, 2014