CAYMAN ISLANDS

Financial Reporting Authority (CAYFIN) Annual Report 2006/2007



FINANCIAL REPORTING AUTHORITY
(CAYFIN)

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30 June 2007

The Honourable Samuel Bulgin, QC, JP
Attorney General
Chairman, Anti-Money Laundering Steering Group
Government Administration Building
George Town, Grand Cayman
Cayman Islands

Dear Honourable Attorney General,

Pursuant to section 30 (b) and in accordance with section 23 (2) (f) of the Proceeds of Criminal Conduct Law (PCCL) (2005 Revision), I hereby respectfully submit the third Annual Report and Statistics of the Financial Reporting Authority for the period ended 30 June 2007. This report outlines our activities in, and our contributions to the fight against money laundering and terrorism financing.

Lindsey Cacho
Director
Financial Reporting Authority

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Message from the Director



I am pleased to submit the Financial Reporting Authority's (FRA's) report for the year ending 2006/2007.

The FRA forms part of the Cayman Islands commitment to the global fight against financial crime, in partnership with the private sector and law enforcement agencies. Our mission is to ensure that the financial and business sectors are free of money laundering, terrorist financing and other related crimes, which is in keeping with our mandate under the Proceeds of Criminal Conduct Law. In compliance with the Financial Action Task Force (FATF) 40 recommendations and 9 special recommendations, the Cayman Islands anti-money laundering, counter-terrorist financing and financial crime detection and prevention initiatives have been robust.

We continue to participate in the Egmont Group and there were significant milestones reached at the Egmont Plenary in Bermuda in June 2007. The group has now achieved international recognition with the establishment of a permanent Secretariat headquartered in Toronto, Canada. The group has also approved a Charter document and appointed an Executive Secretary to undertake the work which had been voluntarily carried out by delegates from member countries. These are important global developments which the FRA fully endorses and welcomes.

The 2006/2007 year marks the fourth reporting period for the FRA. Significant progress has been made in all areas of operation. We were able to complete investigations on 86 per cent of the 219 cases filed with the FRA this year (the remainder requiring further analysis), with just 4 cases carried over from the previous year. Our activities further involved interaction with a cross section of Cayman's business community and more than 59 countries.

We are indeed grateful and wish to thank our partners in the reporting entities, law enforcement and regulatory agencies for their support during the year. We are also thankful to the Anti-Money Laundering Steering Group for its guidance and co-operation throughout the year. I also want to recognize the hard work, commitment and dedication of staff who have all worked tirelessly to accomplish what we have achieved this year. We look forward to another successful year.



Lindsey Cacho
Director

1. Who We Are

The FRA is the Cayman Islands' Financial Intelligence Unit (FIU) with responsibility for receiving, analysing and disseminating disclosures of financial information concerning the proceeds of criminal conduct, money laundering and the financing of terrorism pursuant to the provisions of the Proceeds of Criminal Conduct Law (2005 Revision) (PCCL)

The mission of the FRA is to serve the Cayman Islands by participating in the international effort to deter and counter money laundering and the financing of terrorism.

Our primary objective is to provide timely and high quality financial intelligence to local and overseas law enforcement agencies in keeping with the statutory requirements of the PCCL. Financial intelligence is the end product of analyzing one or several related reports that the FRA is mandated to receive from financial services providers and other reporting entities. Our ability to link seemingly unrelated transactions allows us to make unique intelligence contributions to the investigation of money laundering and terrorist financing activities.

We are under the guidance of the Anti-Money Laundering Steering Group which consists of the Attorney-General, the Financial Secretary, Commissioner of Police, Collector of Customs, Managing Director of Cayman Islands Monetary Authority (CIMA) and the Solicitor General. This group has responsibility for oversight of the anti-money laundering policy of the Government and it determines the general administration of the business of the FRA. It also reviews the annual reports submitted by the Director, promotes effective collaboration between regulators and law enforcement agencies and monitors our interaction and co-operation with overseas financial intelligence units (FIUs).

2. Making a Difference in 2006/2007

ACCOMPLISHMENTS & ACTIVITES AT A GLANCE

1. COMPLETED REVIEW OF 189 CASES OUT OF 219 RECEIVED
2. DISCLOSED 23 CASES TO LOCAL LAW ENFORCEMENT
3. DISCLOSED 33 CASES TO OVERSEAS FIU'S & LAW ENFORCEMENT
4. REPLIED TO 26 REQUESTS FOR INFORMATION FROM OVERSEAS FIU'S
5. ISSUED PAMPHLET TO DEALERS OF HIGH VALUE GOODS
6. SIGNED MEMORANDA OF UNDERSTANDING WITH Australia, Chile, Guatemala, Indonesia, Nigeria, Mauritius and Thailand
7. PARTICIPATED IN CFATF REVIEW
8. PARTICIPATED IN THE DRAFTING OF NEW PCCL BILL
9. REVISED SAR FORM

- **2006/2007 CASES**

In 2006/2007, the unit received 219 new cases. 102 were analysed and required no further immediate action. Another 61 cases were onward disclosed with 23 going to local law enforcement, 33 to overseas FIUs or law enforcement agents and 5 to the Cayman Island Monetary Authority (CIMA). A further 26 cases were replies to Request for Information from overseas FIUs. As at the end of the year there were 30 cases in progress.

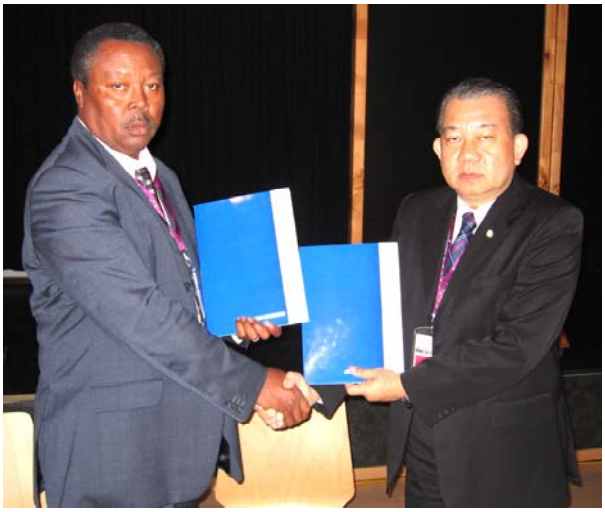
- **MEMORANDA OF UNDERSTANDING (MOUs)**

In recognition of the need to have strong working relationships with our international partners, we have concluded 7 MOUs. These have been signed and exchanged with the financial intelligence units of Australia, Chile, Guatemala, Indonesia, Nigeria, Mauritius and Thailand.



Above, Mr. Neil Jensen, Director of the Australian financial intelligence unit AUSTRAC signs the MOU with Mr. Lindsey Cacho at the Egmont Plenary in Bermuda in June 2007.

Below, Police Colonel Yuthabool Dissamarn, Secretary General for the Anti-Money Laundering Office (AMLO) of the Kingdom of Thailand exchanges the signed MOUs with Mr. Lindsey Cacho at the Egmont Legal Working Group meeting in Liechtenstein in February 2007.



- **SIGNIFICANT EVENTS**

Caribbean Financial Action Task Force

In early June 2007 the Caribbean Financial Action Task Force (CFATF), a FATF-Style regional organisation of thirty states of the Caribbean Basin, which have agreed to implement common countermeasures to combat money laundering and terrorist financing, conducted an onsite assessment of the Cayman Islands' anti-money laundering and combating terrorist financing regime, as part of the 3rd-round mutual

evaluation programme. During their visit the evaluation team met with various public and private sector entities including the FRA. The final evaluation report is expected to be submitted for approval to CFTAF plenary in November in Costa Rica.

SAR Form

During the year, the FRA became a member of the Cayman Islands Guidance Note Committee (GNC). The GNC reviews and updates the *Guidance Notes on the Prevention and Detection of Money Laundering in the Cayman Islands (GN),* which provide best practice guidance for financial services providers and other entities conducting relevant financial business on the interpretation and application of the Money Laundering Regulations (2007 Revision). The GNC is comprised of industry association representatives, government representatives and representatives from the Cayman Islands Monetary Authority. The Suspicious Activity Report Form (SAR Form), which is used by financial service providers and others to file reports with the FRA, is included in Appendix J of the GN. This year, the Form was updated and substantially revised to request information that will allow the FRA to analyse SARs more expeditiously and to produce more accurate statistics. Section 5.28 of the GN was also amended to describe the SAR Form and to provide guidance for filling in the Form. The new SAR Form is also available electronically by contacting the FRA.

Proceeds of Criminal Conduct Law

The FRA played its role in the drafting of the new Proceeds of Crime Bill, particularly in matters concerning the FRA. This Bill seeks, amongst other things, to repeal and replace the Proceeds of Criminal Conduct Law (2005) Revision and to consolidate the money laundering aspect of both the Misuse of Drugs Law and the Terrorism Law. The bill will also amend the law relating to the confiscation of the proceeds of crime and introduce civil forfeiture measures.

Pamphlet for Retailers of High Value Goods

In line with the Financial Action Task Force's Recommendations (Recommendation 12 & 16) that specifically highlight the vulnerabilities of retailers of high value goods to money laundering and terrorist financing a pamphlet was created to give this sector an overview of their responsibilities under the Proceeds of Criminal Conduct Law. The pamphlet was distributed to businesses through the Cayman Islands Chamber of Commerce to whom we extend our gratitude for undertaking this task on our behalf.

2. The Work of the FRA

- **RECEIVING INFORMATION**

The FRA receives information of a financial nature from reporting entities related to money laundering, proceeds of criminal conduct, terrorism and the financing of terrorism.

Failure to make a disclosure to the FRA is an offence where a person knows or suspects that another person is engaged in money laundering and the knowledge or

suspicion is based on information that came to his/her attention in the course of his trade, profession, business or employment. It is also an offence to assist another person to retain the benefit of criminal conduct where there is knowledge or suspicion that the other person is or has been engaged in criminal conduct unless a disclosure of the suspicion or belief is made to this unit. Similarly, it is an offence to acquire, possess or use property where there is knowledge that it represents another person's proceeds of criminal conduct unless a disclosure is made to us.

It is important to note that criminal conduct in the PCCL means conduct that constitutes an indictable offence or conduct that would constitute such an offence if it had occurred in the Islands.

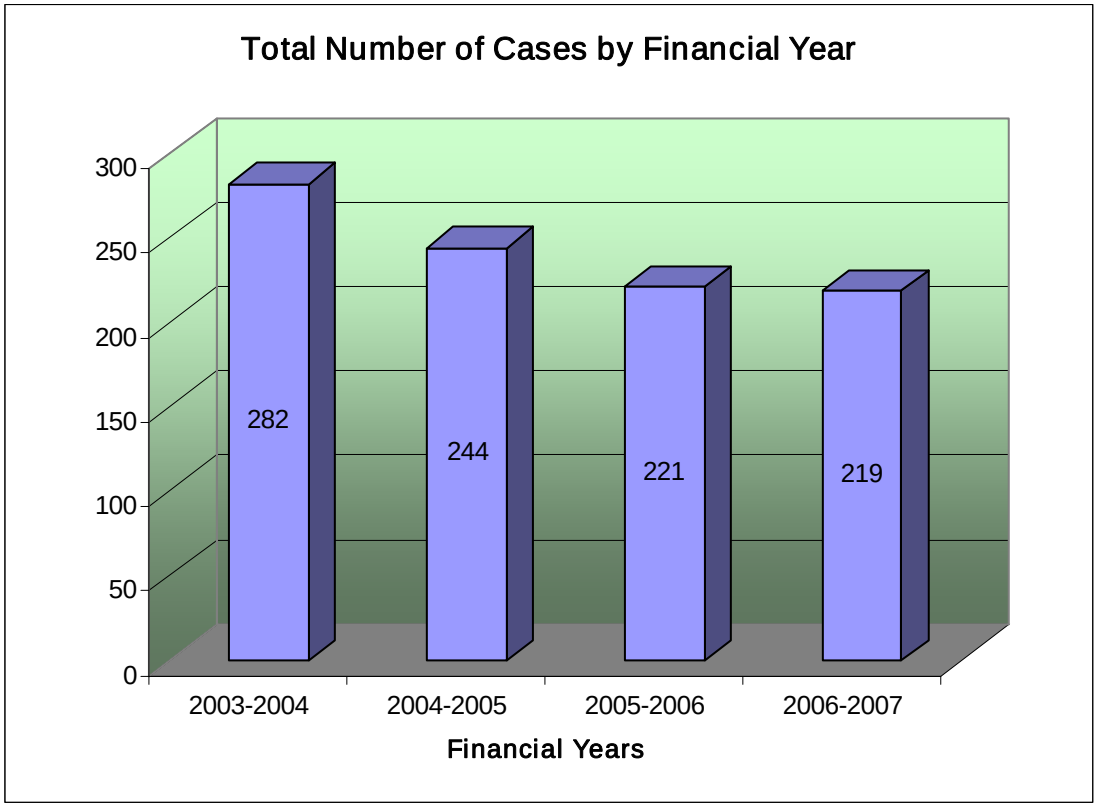
Anyone who initiates a disclosure has a defense to any potential, related money laundering offences. In addition, disclosures made under the law do not breach the Confidential Relationships Preservation Law nor do they give rise to any civil liability.

- **REPORTING ACTIVITY REVIEW**

The table below shows the total number of cases by Financial Year since 2003/2004. As noted above, in 2006/2007 the unit received 219 new cases which is two cases less than in 2005/2006.

The trend over the last three years shows a small decline in cases below the three year average of 228.

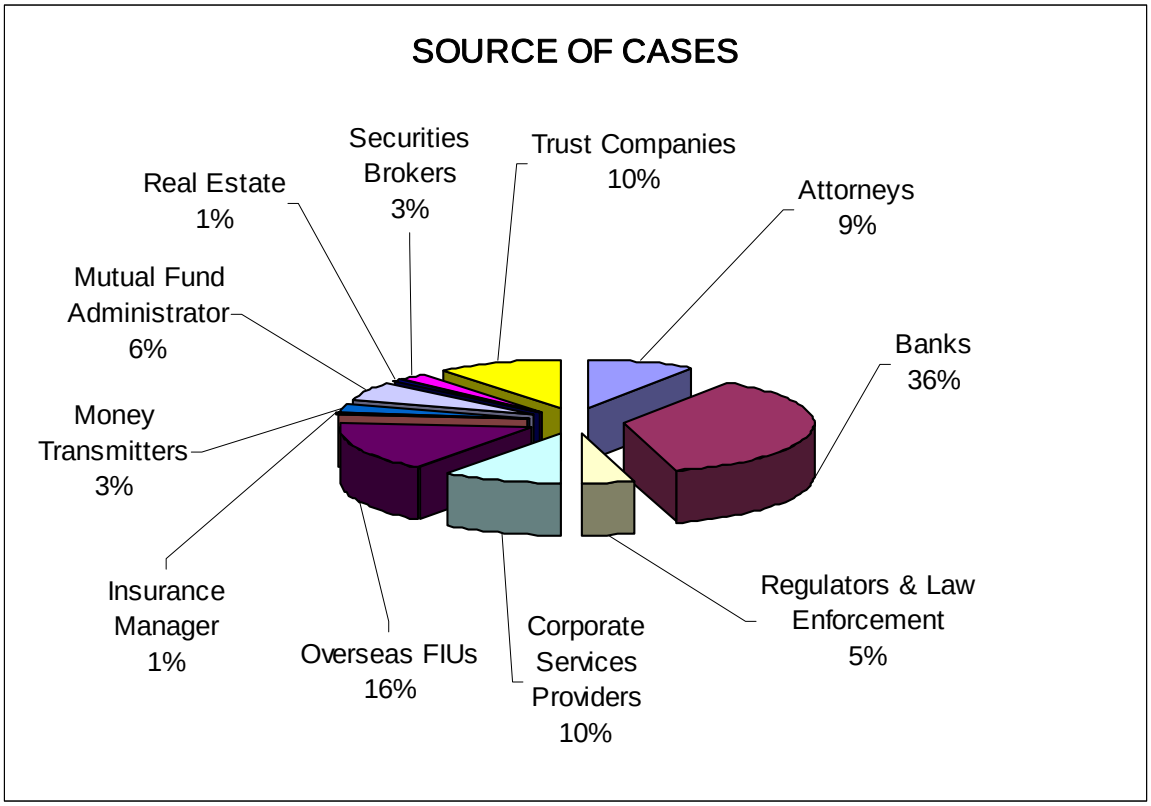
The 219 new cases involved 146 legal entities and 347 persons for a total of 493 subjects.



Source of Cases

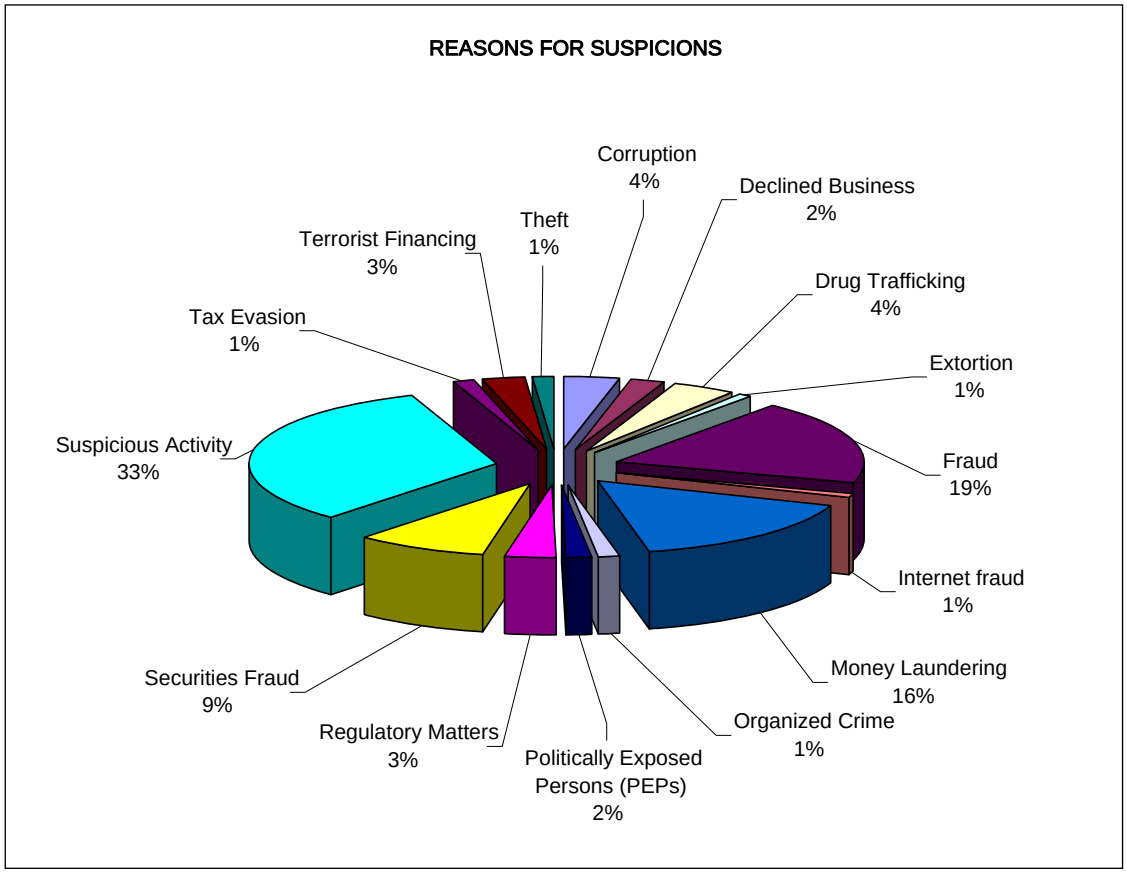
The chart below shows a detailed breakdown of the source of cases. Of the 219 cases received during 2006/2007, the four largest contributors were Banks at 36%, Overseas Financial Intelligence Units at 16%, Company Managers/Corporate Services Providers at 10%, and Trust Companies at 10% for a total of 72% of the cases received. The remaining 28% were from a wide variety of sources which included attorneys, money transmitters, mutual fund administrators, regulators, law enforcement, real estate firms, securities brokers, professional advisers and insurance managers.

Banks continue to represent the largest source of cases which have grown from 28% last year to 36% this year.



Reasons for Suspicions

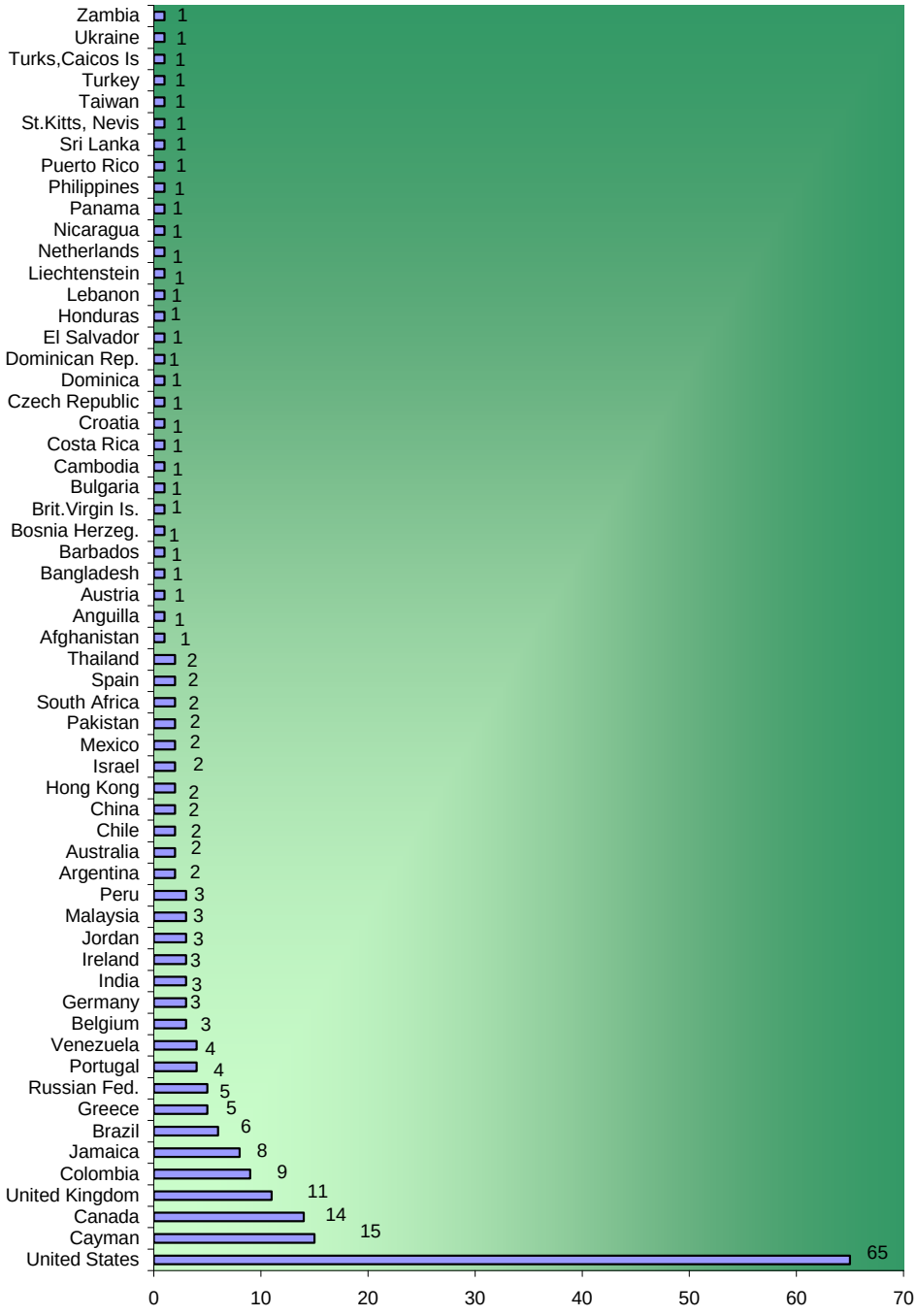
The most common reason for filing reports is suspicious financial activity at 33%, followed by fraud at 19% and money laundering at 16%. The pie chart below provides the detailed breakdown of the reasons for suspicion.



Countries of Subjects Reported

The international scope of the Cayman Islands financial services industry is reflected in the wide range of subjects' countries reported in cases. The "Countries of Subjects" bar graph lists 59 different countries for the primary subjects of the reports. In light of the international character of the subjects reported, our membership in the Egmont Group has proven a valuable resource for information exchange, and has enhanced the analysis of information reported and the development of intelligence. As in our report last year the greatest number of primary subjects is nationals of the United States. However this is a decrease from 85 last year to 65. The largest increases were in subjects from the Cayman Islands which went from 12 to 15 and the United Kingdom which went from 7 to 11.

Countries of Subjects Reported in Cases



- ANALYSING INFORMATION

Analytical Capacity

The FRA conducts an in-depth analysis of information reported in cases to determine whether the required statutory threshold for onward disclosure to law enforcement agencies has been met.

We employ a combination of knowledge, analytical expertise and advanced technology to conduct research and analysis. An important element in the analysis stage is the ability of the unit to require information from any person for the purpose of clarifying or amplifying information disclosed in a SAR. Failure to provide information as requested is an offence.

Analysis is enhanced by our ability to request and exchange information with Egmont members. As of June 2007 there are 107 member countries in the Egmont Group and we are able to communicate and exchange information with these FIUs through the Egmont Secure Web. We continue to work with Egmont to ensure the development of our data; that our systems are compatible with other members of the group, and to maintain information systems capabilities comparable to other FIUs.

SARs Trend Analysis

Declined Business:

Consistent with other years, we continue to receive SARs due to declined business. Many of these cases relate to the individuals' unwillingness to comply with financial service providers' basic KYC requirements. In some cases, elaborate explanations as to the source of funds involving individuals and foreign governments reflect the suspicious activity that triggered the SAR. Other reasons for declined business include negative media reports of individual clients discovered during the due diligence process, or business proposals that are wholly outside clients' stated business expertise, or further still, those that do not make economic sense. The reporting of declined business is included in the Financial Action Task Force's 40 Recommendations (Recommendation 5) and is also discussed in CIMA's Guidance Notes in sections 5.34 to 5.36. Financial service providers are therefore commended for their diligence in identifying this information and reporting it to the FRA.

Securities Fraud – Insider Trading:

An increasing number of SARs include the predicate offence of insider trading – insider trading is an offence in the Cayman Islands pursuant to the Securities and Investment Business Law. Routine surveillance of trading activity has generated some reports where the trading appears to be more than excellent timing. A look into the company's activities and the stock trading activity will often clarify whether it is good timing, or whether the person had insider knowledge, or was involved in manipulating the price of the stock.

Investment Managers and Cayman Islands Mutual Funds:

Investment Managers of Cayman Islands mutual funds have been reported where there has been fraud or an investigation is being carried out by the United States' Securities and Exchange Commission. Cases reported include falsified investment returns and the issuance of fictitious account statements. In addition, there have been some reports of mutual fund subscribers whose investment activity makes little economic sense, or where subscription documents or redemption requests have been forged. Suspicions also relate to the establishment of a private equity fund as the means to launder proceeds of crime.

Account Monitoring:

Ongoing monitoring of account activities continues to generate SARs including where the financial services provider becomes aware that an existing client is being

investigated in their home country for a criminal offence, or where some type of negative news comes to light about a client. Reports are also filed where a client's account is operated in a manner that is outside the expected level of activity, or inconsistent with the stated purpose of the account. Financial service providers are also reporting instances where documentation for source of funds indicates a possible connection to criminal activities. We have also received reports where a Cayman Islands company receives funds from another jurisdiction on a regular basis, and then an aggregated transfer is made to the subject's home jurisdiction. The financial services provider suspected that the funds being received were from an illegal activity. Reports are also being received by money transmitters where a client conducts multiple transactions on behalf of a third party or where a series of transactions are inconsistent with a client's level of income.

Complex Financial Transactions:

We continue to see complex financial transactions which involve companies, trusts and mutual funds set up in multiple jurisdictions which are intended to obscure the audit trail and source of funds. A common arrangement is the establishment of a Cayman Islands company where a Cayman Islands trustee holds the share capital of the company to the benefit of the ultimate beneficial owner. Accounts or assets are then held in the name of the company. While this type of arrangement is commonly used for legitimate business activity it also allows the true beneficial owner to hide behind the trustee as the legal owner of the company.

Overseas Requests for assistance:

Requests for assistance from overseas authorities continue to represent 16% of the FRA's workload. The requests are for information on individuals and entities that are the subjects of ongoing investigations into a variety of financial crimes including fraud, money laundering and drug trafficking.

- **DISSEMINATING INTELLIGENCE TO LAW ENFORCEMENT**

Disposition of Cases

Once information is analysed, a determination is made regarding onward disclosure which can take place only after the Director has reviewed and agreed with the findings. Intelligence is disclosed to the following designated agencies where the required statutory threshold has been met:

- local law enforcement agencies where there is *prima facie* evidence of criminal conduct or where the FRA has cause to suspect criminal conduct.
- the Cayman Islands Monetary Authority where the information is in relation to criminal conduct.
- overseas financial intelligence units (including law enforcement agencies) where the information is in relation to criminal conduct.

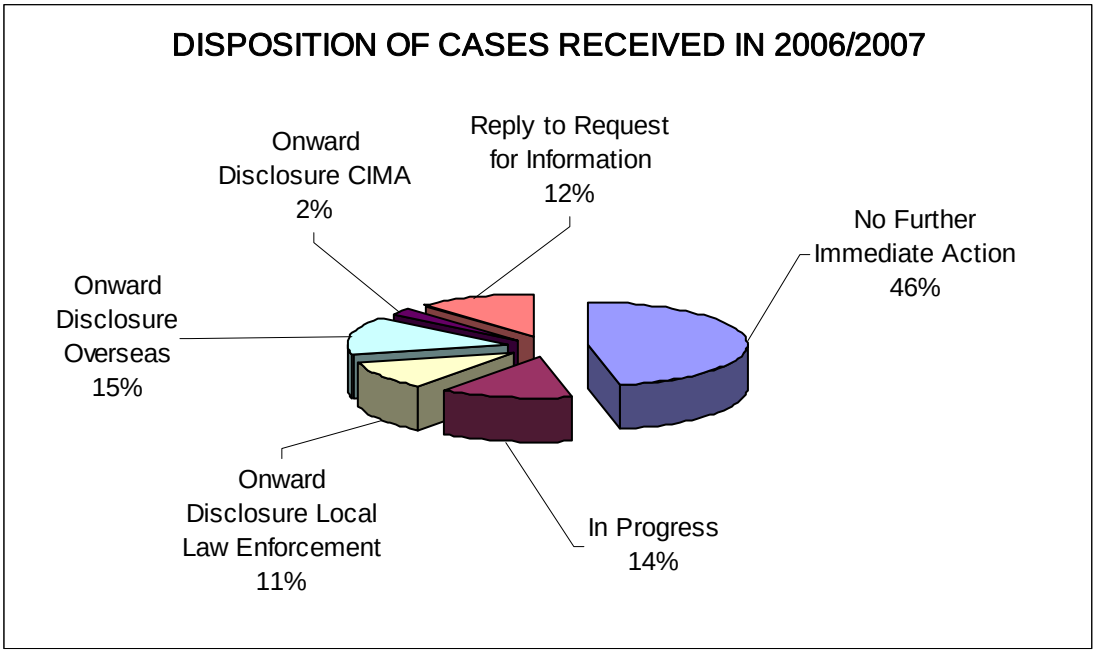
It is important to note that overseas disclosures require the consent of the Attorney-General who considers the purpose of the disclosure, third party interests, and any conditions of disclosure.

The statutory purposes of onward disclosure are to:

- report the possible commission of an offence;
- initiate a criminal investigation;
- assist with any investigation or criminal proceeding; or
- facilitate the effective regulation of the financial services industry.

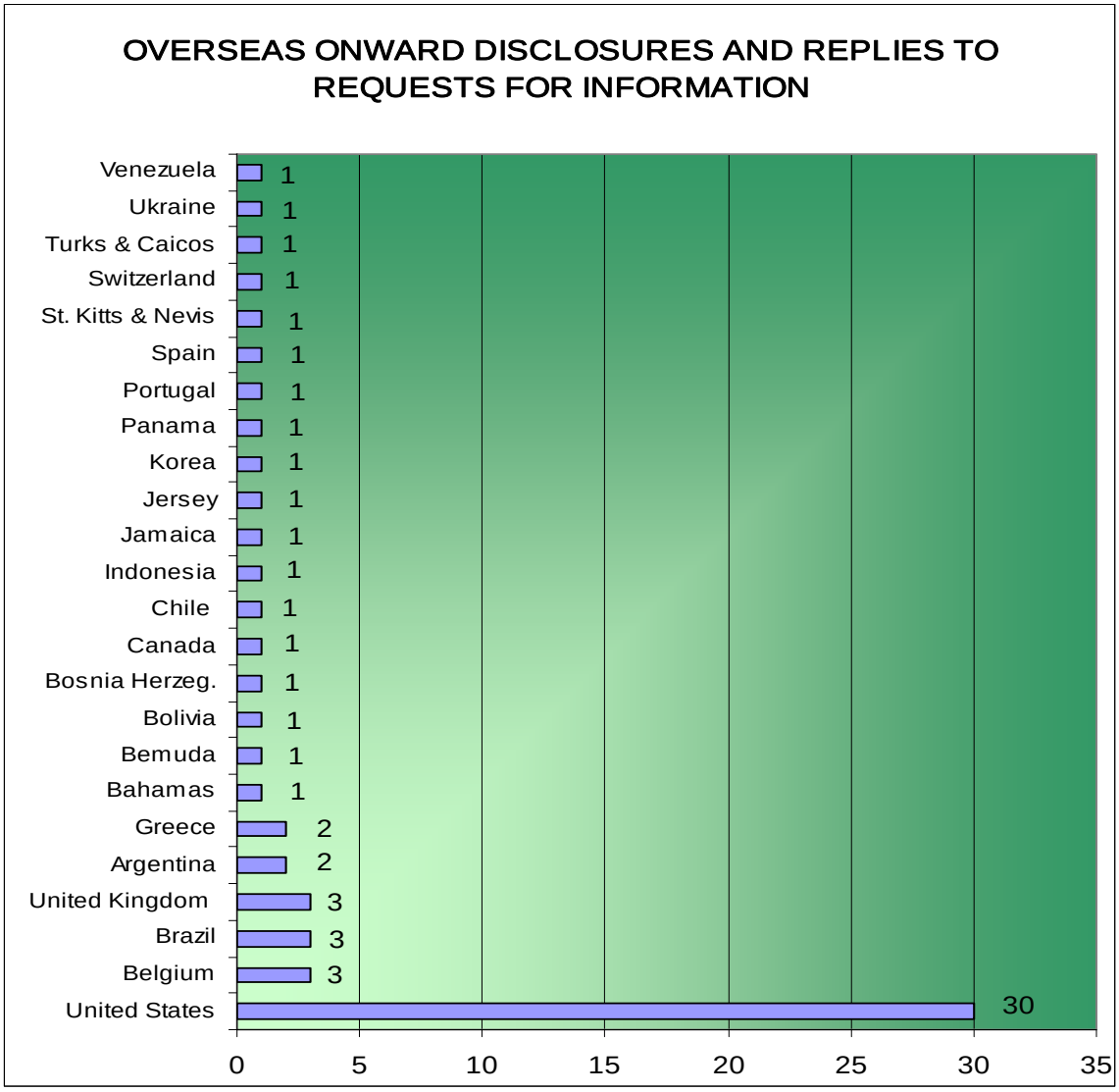
When intelligence does not meet the threshold for disclosure it is retained in our confidential database pending any future developments.

The following pie chart illustrates the disposition of cases for 2006/2007. Of the 219 cases received, 102 or 46% were analysed and required no further immediate action. Another 33 cases or 15% were onward disclosed overseas, 23 cases or 11% were onward disclosed to local law enforcement and 5 cases or 2% were disclosed to CIMA. A further 26 cases or 12% were replies to Request for Information from overseas FIUs. As at the end of the year there were 30 cases or 14% in progress.



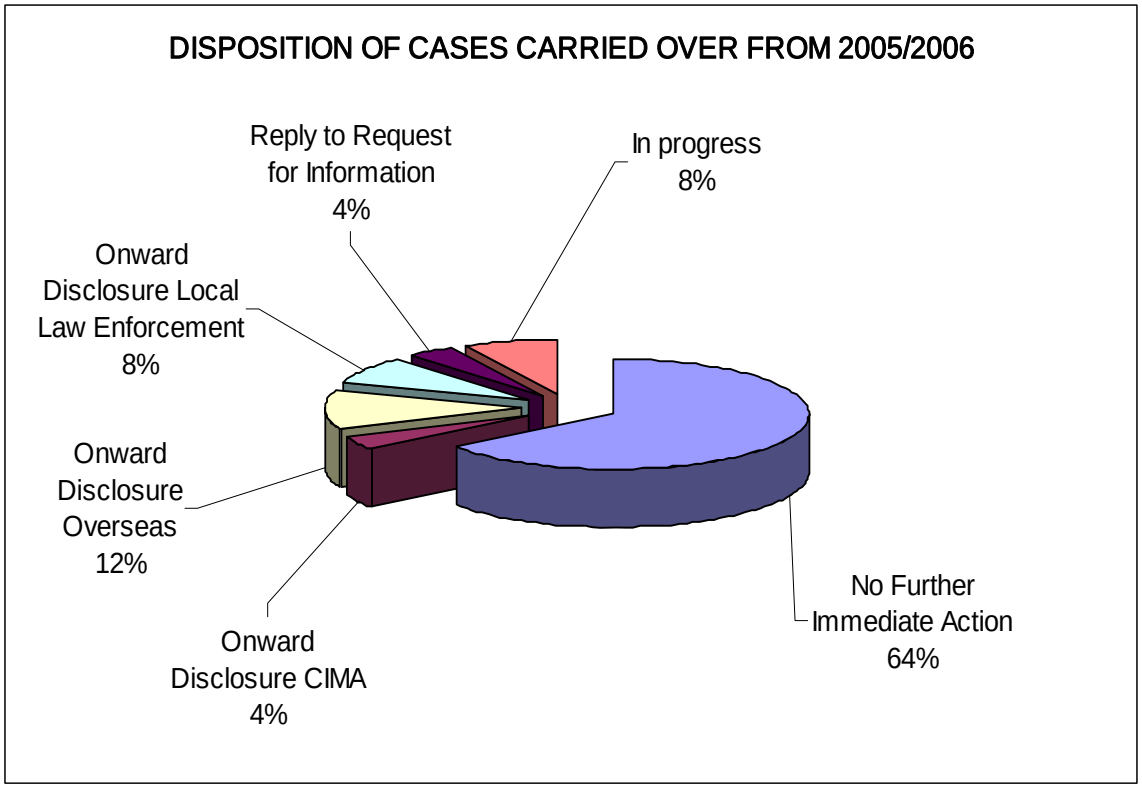
Onward Disclosures Overseas

The 59 cases that were replies to requests for information or were disclosures to overseas FIUs and other law enforcement agencies went to 24 different countries. Two of the cases were disclosed to two overseas FIUs because of the multi country activities of the subjects. By far the greatest number of disclosures was to the United States at 30 followed by the United Kingdom with 3, Brasil with 3 and Belgium with 3. The following table shows a more detailed breakdown.



- DISPOSITION OF CASES CARRIED OVER FROM 2005/2006

The following pie chart illustrates the disposition of the 51 cases carried over from 2005/2006. Of these 51 cases, 33 or 64% required no further immediate action. Another 12 cases or 24% were onward disclosed to the appropriate local or overseas agency. A further 2 cases or 4% were replies to Requests For Information from overseas FIUs. At the end of the year there were 4 cases or 8% which are still in progress a year later.



3. Our Organisation

- Building Organisational Effectiveness



The staff includes:

- Mr. Lindsey Cacho, Director;
- Mr. Kipling Douglas, Legal Adviser;
- Mr. Fred Heard, Senior Accountant;
- Ms. Sue Santedicola, Senior Analyst;
- Mr. Julian Hurlston, Analyst;
- Mr. Robert Scotland, Chief Inspector; and
- Ms. Sharon Dhamalie, Administration Manager.

Throughout 2006/2007 we improved our analytical capabilities through the staff's attendance in 54 days of training at presentations and seminars. These included a seminar at the United States Securities and Exchange Commission on Securities Enforcement & Market Oversight, a course on the analysis of financial information at the Columbian FIU, the Cayman Captive Forum, the Florida International Bankers Association conference and the Hedge Fund conference on Best Practices: Operations and Compliance.

We have also gained valuable experience from a total of 44 days representing the FIU at Egmont Group proceedings, the Caribbean Heads of FIUs meetings and the Caribbean Financial Action Task Force meetings in October 2006 and May 2007. During the year staff participated on the Egmont Group's Implementation Committee, as well as its Information Technology Working Group.

This growing expertise combined with the implementation of enhanced software tools has enabled a more advanced level of analysis.

- **PROTECTING CONFIDENTIALITY OF INFORMATION**

A layered approach to security has been adopted for the unit's premises and systems. The protection of financial information received from reporting entities is a critical function. Our computer security prevention measures include state-of-the–art firewalls to prevent unauthorised access to private data. Staff are made aware of their responsibilities to protect information and severe penalties exist under the law for the unauthorised disclosure of the unit's data.

Strategic Priorities: 2007/2008 Building on Strengths

- THE YEAR AHEAD

In 2007/2008 the FRA will continue to serve the Cayman Islands by participating in the international effort to deter and counter money laundering and terrorism financing. This unit looks forward to another year of increasing its knowledge, expertise and capacity. Our three main priorities for 2007/2008 as noted below continue to reflect and address our most significant commitments and challenges.

- ENHANCE REPORTING OF INFORMATION

Output: Maintain a cooperative interface that fosters improved quantity and quality of reporting.

The quality of our analysis hinges directly on the quality of the financial information we receive. We are committed to developing and maintaining cooperative working relationships with all reporting entities. To this end our staff will continue to offer presentations on the role and responsibilities of the unit to industry associations, groups, financial services providers and CIMA.

The scope and level of outreach activities will be expanded to support reporting entities in meeting their obligations and to improve the quality of the reports received.

- PRODUCE INSIGHTFUL AND RELEVANT INTELLIGENCE REPORTS

Output: Produce and deliver increasingly effective, technology driven financial intelligence analysis and case disclosures that are widely used and accepted by law enforcement and intelligence agencies.

Our staff will continue to receive the necessary training to remain abreast of current issues and developments affecting anti-money laundering and counter terrorist financing strategies both locally and internationally.

This unit is committed to ensuring the professional development of its staff so that they are continually able to provide the highest level of insight and add value to the intelligence product.

- APPROPRIATE DISSEMINATION OF INTELLIGENCE

Output: Ensure that disclosures to law enforcement agencies both locally and overseas are made in a timely manner and are consistent with statutory obligations. Disclosures will be relevant, add value to existing intelligence, assist with ongoing investigations and where necessary result in the initiation of investigations.

We shall strive to obtain feedback from our disclosures both locally and overseas to measure our success in contributing to the fight against money laundering and terrorism financing.

On the international scene the FRA will continue to strengthen ties with overseas FIUs and other international partners and, where possible, to share its expertise.

As an active member of the Egmont Group we will continue to support that organisation in its fight against money laundering, and more recently the financing of terrorist activity.

(This report may also be requested in electronic format by emailing sharon.dhamalie@gov.ky.)