

Vanuatu

National Risk Assessment

Money Laundering through the Offshore Sector and Terrorist Financing

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Foreword by the NCC Chairman

The Vanuatu National Money Laundering and Terrorism Financing Risk Assessment (ML&TF NRA) has been prepared by the Vanuatu government authorities and is a significant outcome in Vanuatu's anti- money laundering and countering the financing of terrorism (AML&CTF) program.

In addition to identifying the most significant ML&TF risks for Vanuatu, it also assists Vanuatu in meeting the global AML&CTF standards established by the Financial Action Task Force on money laundering (FATF).

Money laundering and terrorist financing are global issues and Vanuatu has a responsibility to ensure that it establishes and maintains an environment hostile to these offences, and part of this responsibility is this NRA.

This NRA provides a preliminary overview of the ML&TF issues affecting Vanuatu now, and importantly what the ML&TF risks may be in the coming years, and aims to generate knowledge and understanding to inform priority setting and aid decision makers.

This assessment of ML&TF risk requires the ongoing monitoring and reviewing of all potential ML&TF risks, and the updating of the NRA at regular intervals of between 2 to 5 years. Consequently, this requires that effective communication and consultation between all stakeholders are in place that promote collaboration and intelligence sharing across agencies.

Coupled with the sharing of information among the stakeholders, Vanuatu must ensure that its risk management plans remain up to date, relevant to objectives and that they are regularly reviewed and evaluated. This in turn enables decision makers to exchange ideas, clarify any uncertainty and ultimately make better and more confident choices.

As the key stakeholder, the Vanuatu Financial Intelligence Unit will play an important part in maturing and refining the NRA process and will need to provide a forum to gather and then to disseminate information to all other stakeholders.

This risk assessment recognises that while risk can be mitigated and managed, zero risk is unobtainable. Consequently, strategies must be implemented to continually monitor the levels of the ML&TF risks and where and when appropriate, to implement procedures to manage and to reduce the severity of those risks.

The NRA represents an opportunity for government agencies and the private sector to better understand the ML&TF issues that they may encounter, and to be able to adapt their part of the Vanuatu AML&CTF program to those risks.

This NRA is both timely and necessary in the development of Vanuatu's AML&CTF program.

Johnson Naviti Marakipule
Director General
Prime Minister's Office, Government of the Republic of Vanuatu

Introduction

1. This document represents Vanuatu's National Risk Assessment (NRA) in relation to two aspects: money laundering¹ through the Offshore Financial Centre (OFC) and terrorist financing. The assessment² was undertaken over the period February-July 2017. It complements an earlier NRA, completed in January 2015, and seeks to expand on the two issues that were not fully explored in the original NRA. As a result, this current document does not seek to address the background to the concepts of money laundering and terrorist financing, and the dangers that they pose to a country's financial system, economic development and international reputation. Discussion of these issues can be found in the relevant sections of the original NRA.

2. The preparation of this NRA was overseen by the National Coordinating Committee on Anti-Money Laundering and Combating the Financing of Terrorism (NCC). The methodology employed involved (a) initial oral input from a broad range of stakeholders in the country, from both the public and private sectors³, in order to gather their perceptions of the money laundering and terrorist financing threats and vulnerabilities faced by the country; (b) the analysis of written responses to tailored questionnaires, circulated to both public and private sector stakeholders, seeking to collect core data; (c) follow-up meetings with relevant parties to further develop the information provided; and (d) meetings of the NCC and workshops involving all interested stakeholders (both public and private) to discuss and validate the findings from the assessment.

3. The basic approach adopted in preparing the NRA has been to consider the threats and vulnerabilities faced by Vanuatu in relation to money laundering (ML) through the OFC and terrorist financing (TF), in general. A *threat* is a person, group of people, object or activity with the potential to harm, for example, the state, society, the economy, the financial system, etc. *Vulnerabilities* comprise those things that can be exploited by the threats, or may support or facilitate their activities. The response to these issues will necessarily involve the adoption of a risk-based approach to addressing the challenges, in order to be able to allocate the country's limited resources to best effect.

4. Vanuatu has made important progress in recent years towards strengthening its defences in relation to anti-money laundering and combating the financing of terrorism (AML/CFT). Since early-2016, the Government of Vanuatu (in partnership with the private sector stakeholders) has been heavily engaged with the International Cooperation Review Group (ICRG) of the Financial Action Task Force⁴ (FATF) as part of the Government's efforts to bring the AML/CFT framework into line with international standards. This has resulted in a major initiative to update legislation and to improve awareness of AML/CFT issues within both the public and private sectors. A total of 31 laws have been identified as requiring amendments, of which thirteen (judged to be an

¹ Money laundering is broadly defined to mean the process by which the proceeds of criminal activity are placed and integrated into the financial system and broader economy with the intention of concealing their origin.

² Vanuatu is grateful to the Asian Development Bank for the technical assistance granted in relation to the NRA.

³ A list of the contributors to the NRA is attached at Annex 1

⁴ The ICRG is tasked with working with jurisdictions that have been identified as having serious deficiencies in the core elements of their regimes to combat ML and TF. Vanuatu was brought into the ICRG process following the mutual evaluation by the Asia Pacific Group on Money Laundering, which highlighted a substantial number of material deficiencies.

absolute priority) were enacted by parliament and brought into force on 16 June 2017. This action has addressed quite significantly the potential vulnerabilities that existed at the time when the current risk assessment was started in January 2017. It is an important step forward towards ensuring that the overall framework is not only in compliance with international standards at a technical level, but is also implemented in an effective and robust manner. The remaining amendments, which are mostly consequential to the changes brought about by the priority legislation, will be addressed in due course.

5. In undertaking the NRA, it must be recognised that there were a number of challenges towards obtaining firm evidence on which to make reasoned judgements. These included limitations on (a) the data maintained by the authorities in relation to criminal activity involving the offshore sector; (b) the data and information collected through the regulatory process; and (c) the information on the activities undertaken by non-resident institutions and entities taking advantage of the OFC. Where consolidated data has been available, the assessment has sought to consider trends and overall developments over the three-year period, 2014-2016. In practice, much of the assessment of the threats faced by Vanuatu has had to be prepared on the basis of general perceptions within the public and private sectors, rather than on empirical evidence, although information obtained from external sources (primarily the Internet) has been valuable in producing some case studies.

6. The following assessment is split into two sections. The first part deals specifically with the ML risks within the offshore sector, while the second part addresses TF risks in relation to both the domestic and offshore sectors

Key Findings

- Overall, Vanuatu's offshore sector is very small by international comparison, in terms of both the scale and scope of the activities being undertaken. Most of the sector has been in marked decline for several years.
- The number of international companies has been falling year-on-year (currently about 4,500) with a high annual turnover. It is believed that the majority of the active companies are used as investment or asset-holding vehicles. The only growth area involves business from the Peoples Republic of China.
- The international banking sector is very small, comprising six institutions with total assets of only US\$106 million. The banks are engaged primarily in private banking and in-house treasury operations. Regulation of the sector has improved significantly in recent years, but there continue to be some challenges to ensuring that the sector is not open to criminal abuse.
- The number of licensed securities dealers has increased rapidly since 2015, and the sector has not been subject to effective supervision. There is little information available on the activity within this sector. The regulator has recently been given new statutory powers as part of an attempt to improve supervision and to mitigate the potential risks.
- While the legal and regulatory frameworks in relation to money laundering and terrorist financing have previously lagged behind international standards, substantial progress has been made since 2016 to bring appropriate legislation into force. These reforms are continuing.
- Due to a shortage of data and broader evidence, it is difficult to assess the exact nature and potential scale of money laundering within the offshore sector, but there is no evidence to suggest that it takes place on a substantial scale.
- All stakeholders perceive foreign tax evasion as the most common threat posed to the offshore sector, but measures have very recently been introduced to make such activity a predicate offence for money laundering in Vanuatu. This will strengthen the authorities' hands in providing international cooperation in this area.
- Fraud, illicit transnational flows and infiltration by organised criminal groups are also recognised as potential threats.
- The law enforcement agencies have never investigated criminal activity within the offshore sector, and they have limited capacity to undertake the potentially complex financial analysis that would be required. A specialist Money Laundering Unit was established within the Police Force in early-2017, and the delivery of appropriate training to improve capacity is a priority.
- The regulatory and supervisory authorities have recently been given enhanced statutory powers, but human and financial resources are under pressure, resulting in challenges in implementing an effective regime to ensure compliance with AML/CFT measures.
- The NCC has mandated two Working Groups (Supervision and Law Enforcement) to work closely with the government agencies on the implementation stages. The Supervision Working Group has been working on an overall supervisory framework.
- No financial or other sanctions have yet been applied to institutions within the offshore sector for non-compliance with AML/CFT obligations, but recent amendments to the AML/CFT law broaden the scope of the available measures. The VFIU will give particular attention to ensuring that effective, proportionate and dissuasive sanctions are applied where necessary in the future.

- Significant steps have been taken recently to improve transparency in relation to international companies. Companies are now required to file beneficial ownership information with the VFSC, bearer shares have been abolished, and the strict secrecy provisions have been extensively changed to permit greater access to, and sharing of, information by the authorities with domestic and foreign counterparts.
- The provision of international cooperation in relation to money laundering and predicate offences has frequently been slow and restricted by legal constraints. Recent amendments to relevant legislation will open appropriate gateways to permit improved performance.
- There is no evidence that Vanuatu has been the source of, or conduit for, terrorist financing in either the domestic or offshore sectors. There is on-going work to improve the authorities' understanding and oversight of the NPO sector.
- The terrorist financing risks have been less well understood among many in both the public and private sectors, but outreach has improved to help ensure that there is greater awareness of the threats and the measures needed to counter them.
- The procedures for implementing targeted financial sanctions have not been fully developed in the past. New legislation introduced in June 2017 will allow for a more robust regime to be put in place.

Part One: Money Laundering Risks within the Offshore Financial Centre

Background to the OFC

7. Vanuatu's OFC⁵ was created in 1970/71 while Vanuatu was under the joint Franco-British Condominium. The primary attraction of using Vanuatu as an offshore base is the absence of income tax, corporation tax and capital gains tax. Also, by international standards, the costs of incorporation and local service-provider fees are very low, and the regulatory requirements have previously been quite limited. The OFC was originally based primarily on incorporation of International Companies (ICs), but has also, progressively, provided for the establishment and licensing of financial service providers (e.g. international banks, insurance companies, mutual funds, securities dealers, etc.). The number of ICs reached a peak (approximately 21,000) in the period of 2011-15, driven primarily by the requirement in the Permanent Residence Visa Program for applicants to incorporate an IC as part of the package. Subsequently, there has been a sharp contraction, and many now characterise the overall offshore sector as in terminal decline, if it remains based on its current structure.

8. This decline has resulted from a combination of circumstances, including actions taken by Vanuatu to bring regulation of the OFC into line with international standards; relatively high compliance costs for institutions in view of Vanuatu's international reputation; increased competition from other OFCs globally; difficulty for international banks to acquire correspondent banking relationships; and the relative lack of an environment (modern legal framework and provision of high quality professional services) that meets the needs of institutional and sophisticated international investors. The only growth area in recent years has been with respect to the issue of securities dealers' licences⁶. Currently, the offshore sector comprises approximately 4,500 active ICs, six international banks (with total assets of only about USD106 million), just over 400 licensed securities dealers (with unknown levels of trading), one mutual fund, and six captive and three international insurers. Only one of the insurance companies provides life or investment-related policies. Therefore, by comparison with many other OFCs, Vanuatu's offshore sector is very small in terms of both the number of licensed or registered entities (with the exception of the securities dealers) and the size of the institutions' business. The sector is serviced locally by 59 Company and Trust Service Providers (CTSPs) that hold one of five different types of licence, depending on the nature of the service being provided.

Legislation, Supervision and Law Enforcement

9. While there are a number of general laws that may be relevant to the OFC, the primary legislation that impacts the business and financial activities discussed in this assessment comprises the following (including relevant amendments through to June 2017):

⁵ There is no generally accepted definition of what constitutes an OFC, as the various models differ greatly. The definition in the OECD Glossary of Statistical Terms is a reasonable characterisation of the situation in Vanuatu: "Countries or jurisdictions with financial centres that contain financial institutions that deal primarily with non-residents and/or in foreign currency on a scale out of proportion to the size of the host economy. Non-resident-owned or -controlled institutions play a significant role within the centre. The institutions in the centre may well gain from tax benefits not available to those outside the centre."

⁶ See the discussion in the "vulnerabilities" section.

- Company and Trust Services Providers Act (2010)
- Dealers in Securities (Licensing) Act (1971)
- International Banking Act (2002)
- International Companies Act (1992)
- Insurance Act (2005)
- Proceeds of Crime Act (2002)
- Anti-Money Laundering and Counter-Terrorism Financing Act (2014)
- Counter Terrorism and Transnational Organised Crime Act (2005)
- United Nations Financial Sanctions Act (2017)

10. Administration, oversight and supervision of the various entities within the offshore sector are the responsibility of three agencies.

- The Vanuatu Financial Services Commission (VFSC) undertakes the registration of international companies, and also has legal responsibility for the prudential supervision of CTSPs and Securities Dealers.
- The Reserve Bank of Vanuatu (RBV) is the prudential supervisor and regulator for international banks and insurance companies. It acquired the responsibility for international banks from the VFSC in 2003 following the introduction of new legislation (International Banking Act) that requires such banks to maintain a physical presence in Vanuatu in line with international standards. The RBV also assumed responsibility from the VFSC for supervising insurance companies in 2009.
- The Vanuatu Financial Intelligence Unit (VFIU), besides fulfilling the traditional role of a FIU, has legal responsibility for supervising and enforcing compliance by all reporting entities subject to the Anti-Money Laundering and Counter-Terrorism Financing Act. The VFIU has entered into Memoranda of Understanding (MoUs) in relation to information-sharing and joint-supervision with both the VFSC and the RBV. In practice, the RBV has been undertaking some degree of AML/CFT compliance checks in conjunction with its prudential supervisory inspections of international banks and insurance companies, and reports its findings to the VFIU.

11. Law enforcement responsibility with respect to ML issues is vested in two agencies.

- The Money Laundering Unit (MLU) within Vanuatu Police was created in early-2017 to provide specialist investigative resources. It works in close cooperation with the Transnational Crime Unit (TCU) which can provide intelligence support and additional resources where necessary; and
- The Department of Customs and Inland Revenue (DCIR) is responsible for enforcing the Currency Declaration Act, and for investigating ML and other serious offences in relation to trade commodities and passenger movements.

12. The extent to which the legal framework and the supervision and law enforcement roles of the agencies impact the risks within the OFC is discussed below when considering the vulnerabilities of the sector to ML and TF.

Compliance with International Standards

13. Vanuatu is a member of the Asia Pacific Group on Money Laundering (APG), which is an Associate Member of the FATF, the international standard-setter in relation to AML/CFT. As a member of the APG, Vanuatu is routinely subject to a peer review for

compliance with the FATF standards (or “Recommendations”). Since 2013, these assessments have addressed not only technical compliance with the FATF Recommendations, but also the extent to which a country is effective in achieving certain defined Outcomes that are deemed to be at the core of a robust AML/CFT regime.

14. In its latest evaluation report by the APG, published in September 2015, Vanuatu was judged to have achieved a broadly satisfactory level of technical compliance with only ten of the 40 Recommendations, and was assessed as delivering a low level of effectiveness in all eleven of the defined Outcomes. As a result, Vanuatu was referred to the FATF’s ICRG process. In February 2016, the government of Vanuatu committed to an action plan, agreed with the FATF, to address the key deficiencies identified by the APG report. A number of the items in the action plan have direct relevance to the offshore sector, specifically:

- To criminalise money laundering and terrorist financing adequately;
- To ensure a fully operational and effectively functioning financial intelligence unit;
- To strengthen the preventive measures, including for wire transfers;
- To establish transparency in relation to the financial sector, and legal persons and arrangements;
- To implement an adequate AML/CFT supervisory and oversight programme for all the financial sector and CTSPs;
- To establish appropriate channels for international co-operation and domestic coordination policies and actions on identified risks, and ensuring effective implementation.

15. A key (and overarching) element of the action plan was to continue the risk assessment work undertaken in 2014/15, and to prepare a NRA specifically examining the risks in the offshore sector. The June 2017 amendments to the priority laws substantially address the technical deficiencies identified within the action plan. The issue of effective implementation of the laws is necessarily a longer-term objective to which the Government and the competent authorities are firmly committed.

Money Laundering Threats

Sources of Data

16. As indicated above, the law enforcement and regulatory authorities within Vanuatu possess only limited data on criminal activity that might have been conducted through the offshore sector. Moreover, it has not been possible to identify any recent cases (i.e. within the last ten years) where there has been a direct link between activity in the offshore sector and local criminal investigations, prosecutions and convictions⁷. There are limited cases where suspicious activity reports from the offshore sector have prompted analysis and international enquiries by the VFIU, but these have not developed into criminal investigations. Examination of criminal cases investigated overseas has provided some, but limited, substantive information in relation to links with the OFC in Vanuatu; international requests for cooperation offer some evidence of suspected crimes committed overseas; and

⁷ The only case consistently cited by the authorities is the so-called Moana Bribery Case, in which 14 members of the Vanuatu parliament were convicted for corruptly giving or receiving funds, supposedly originating from sources overseas. However, there is nothing in this case that indicates that it involved the use of an offshore structure.

analyses of regional crime trends provide some suggestions with respect to emerging threats, but these are rarely specific to Vanuatu.

Foreign Tax Crimes

17. All stakeholders, within both the public and private sectors, agree that the most likely threat faced by Vanuatu through the OFC is the commission of foreign tax crimes by persons either establishing ICs or other structures in Vanuatu, or using the services provided by offshore financial institutions. However, it has not been possible to establish any reliable indication of either the frequency with which this threat might emerge in practice, or the potential volume of funds involved. Information on cases coming before the courts overseas is entirely limited to Australia and New Zealand, which historically have been seen to be the primary sources of interest in accessing the Vanuatu OFC. This somewhat parochial focus is no longer seen to be an accurate reflection of the OFC client base, with both the VFSC and the private sector stakeholders identifying the Peoples' Republic of China, Hong Kong⁸, Malaysia, Singapore and parts of Europe as being a source of clients wishing to create offshore structures. It has not been possible, so far, to identify specific cases where the proceeds of tax evasion in these countries are being channelled through Vanuatu.

Case Study A

“Robert Agius [a Vanuatu-based accountant] has been sentenced to almost nine years’ jail by an Australian court for his part in an A\$5 million (Vt 476 million) tax evasion scheme.”

Source: Vanuatu Digest, 23 August 2012

Case Study B

“High-profile [Vanuatu] tax adviser and former Inland Revenue Department official, Brent Gilchrist, has been found guilty of six charges of helping orchestrate a fictitious invoice-writing scheme that sought to route funds through Vanuatu as part of a tax avoidance scheme.”

Source: New Zealand Herald, 26 July 2013

18. The analysis of inward requests for international cooperation, directed towards both the VFIU and the State Law Office (the latter as the Central Authority for mutual legal assistance requests), has also not produced any substantive evidence to indicate the likely scale of the tax evasion threat. Only one of the requests referred to the VFIU in the period 2014-2016 is recorded as involving a suspected tax offence⁹, and none of the mutual legal assistance requests appears to relate to this issue. However, use of this data to help validate, or otherwise, the possible scale of ML relating to tax crimes has to be treated with care, since it is probable that foreign authorities will have been aware that, prior to the June 2017 amendments to the key AML/CFT laws, formal international cooperation would not be forthcoming in view of the

Case Study C

“A senior Vanuatu government official has been sentenced in the Supreme Court in Brisbane to five and a half-years in jail for his involvement in a four million US dollar tax fraud. Clarence Lawry Marae pleaded guilty to conspiring to defraud the Australian government.

Three Australians were convicted in 2011 and jailed for their role in the scam, which involved stripping companies of their assets so the businesses were unable to pay taxes. The fraud occurred between 1999 and 2001, with 15 companies taking part in the scheme, which used sham loans, offshore bank accounts and companies.”

Source: Radio New Zealand, 3 September 2013

⁸ It is most likely that the majority of business being recorded as emanating from Hong Kong is, in fact, business originating from beneficial owners in PRC, but using Hong Kong service providers or intermediaries.

⁹ The FIU has received STRs in relation to tax issues, but these have concerned possible evasion of domestic VAT, usually involving the channelling of business funds through personal accounts.

dual criminality concepts. The difficulty in quantifying the extent of tax evasion through the Vanuatu offshore sector does not undermine the fact that all stakeholders perceive this as the primary threat against which they must guard.

Fraud and Illicit Transnational Flows of Funds

19. Stakeholders have also identified fraud as a probable source of proceeds of crime involving the offshore sector. The only specific data relating to this type of criminal activity that is available to law enforcement authorities concern cases where residents of Vanuatu have been victims of scams perpetrated from overseas, resulting in their funds being transferred to accounts outside Vanuatu. However, these examples do not relate to any abuse of the OFC, but are examples of an international trend in cyber-crime perpetrated across international borders.

20. While the law enforcement authorities in Vanuatu have never investigated criminal cases involving international companies, such companies have featured in fraud cases in foreign jurisdictions. In these cases, the primary use of the Vanuatu company has been to receive the proceeds of a fraud, perpetrated against either individuals or businesses, into one or more accounts opened in the names of the company. Typical of this type of fraud is the use of “boiler room” telemarketing of fraudulent investments¹⁰, and the invoicing of non-existent services supposedly provided to legitimate businesses.

21. International cooperation requests submitted to the VFIU and the State Law Office appear primarily to relate to fraud investigations being investigated in Europe, Australia and the US. In terms of suspicious activity being detected overseas in relation to the flow of funds in and out of Vanuatu, the New Zealand FIU reports that, during the period 1 January 2014 to 27 April 2017, it received 360 STRs referencing over 2000 transactions that involved Vanuatu.

22. Again, although there are known cases involving the use of international companies to help perpetrate fraud, there are no broader data available that might assist in assessing the scale of such activity.

Case Study D

“A former Vodafone Ireland executive has been jailed for three years for his part in a fraud of nearly €2m from the company.

Barron ordered services, for which invoices were not provided, on behalf of a company, Tel-Q Ltd, of which he was the owner and which was registered in Vanuatu, a Pacific island tax haven. Barron approved the payment of invoices to Tel-Q for work that was never actually carried out.”

Source: *Sunday World*, October 2016

Case Study E

“More than 100 victims of notorious conman Peter Foster have moved to freeze funds held in offshore tax havens after more than \$10 million was siphoned from his online gambling company Sports Trading Club. Fairfax Media can reveal Foster and at least eight associates have been served with freezing orders over the past week, including Foster's niece, Arabella Foster, and high-profile Sydney lawyer Leigh Johnson. Corporate records reveal Ms Foster, a 29-year-old designer based in Brisbane, was linked to Hong Kong company Sports Trading Club Limited, while she also controls more than \$6 million in offshore accounts in Vanuatu, Hong Kong and the Cayman Islands.”

Source: *Sydney Morning Herald*, 5 November 2015

¹⁰ Operation Sterling carried out by the Queensland Police identified use of Vanuatu companies in a major cold-call investment fraud in the Brisbane area. See warning notice of July 2016. <https://www.police.qld.gov.au/online/Documents/ColdCallInvestmentFraud.pdf>

Insider Trading and Market Manipulation

23. Key objectives of securities regulators are to protect investors; to ensure that markets are fair, efficient and transparent; and to reduce systemic risk¹¹. A core element in achieving these objectives is that “regulation should detect, deter and penalise market manipulation and other unfair trading practices”¹². The authorities recognise that these objectives are not currently being met in Vanuatu. There is no substantive supervisory framework for the 400 licensed securities dealers¹³ on the register, and the authorities have no clear statistics on the size, nature or jurisdictional scope of the dealers’ operations. As with all securities markets, the likelihood is that illicit activities are being undertaken within this sector, but it is not possible currently to assess the type or potential scale of such activity. In June 2017, the Dealers in Securities (Licensing) (Amendment) Act was brought into force in an effort to address this issue. The new legislation strengthens the market entry requirements (including the “fit and proper” tests); requires the submission of more detailed information; gives the VFSC improved regulatory and enforcement powers; and introduces new criminal offences of market manipulation and insider dealing.

Organised Criminal Groups

24. Regional law enforcement agencies have established that organised criminal groups (OCGs) have been expanding their operations into the Pacific region in recent years¹⁴. There is currently no direct evidence that OCGs have, so far, infiltrated the Vanuatu offshore sector in order to facilitate their activities, but it is important that the public and private stakeholders should be alert to possible encroachment.

¹¹ International Organisation of Securities Commissions: Objectives and Principles of Securities Regulation, June 2010.

¹² Methodology for Assessing Implementation of the IOSCO Objectives and Principles of Securities Regulation, May 2017.

¹³ For more information, see the section on the securities dealers sector under the “vulnerabilities” section of the report.

¹⁴ Several cases have been reported of drug trafficking arrests in Australia in relation to shipments found aboard yachts and cruise ships that arrived via Vanuatu. Some of the cases are suspected of being linked to OCGs bringing shipments from SE Asia and Latin America. While the drugs are believed only to have transited Vanuatu, there is clear evidence of Vanuatu being used as a staging post in the operations. Also, in February 2016, the police identified a methamphetamine laboratory that had been set up in Vanuatu by foreign nationals.

Extent and Impact of Money Laundering Threats

25. The current shortage of data relating to criminal activity that affects the offshore sector presents a significant challenge in quantifying the extent of the respective threats and their possible impact on the integrity of the OFC. However, it is clear that not all the identified threats pose the same level of concern, although the views on this must be largely intuitive, given the circumstances. The following “heat map” attempts to distinguish the relative importance of the factors that have been identified, taking into consideration the extent to which the activity is generally identified by stakeholders and others to be a feature of the offshore sector; the ease with which the activity may be undertaken (even in the absence of empirical evidence); and the relative damage that the activity can cause to the integrity of the financial system and the broader economy.

Extent of threat		Impact		
		Low	Medium	High
High			Fraud	Foreign tax crimes
Medium			Insider trading Market manipulation	
Low				Organised crime

26. The map seeks to identify the relative priorities for Government in addressing the threats that have been identified. As a result, priority will be given to tackling abuse of the offshore sector in relation to foreign tax crimes. This will be achieved in large part by improving the exchange of information through enhanced international cooperation channels. A second level of priority will be given to addressing the threat of fraud, in part by working to ensure that CTSPs are applying robust customer due diligence and monitoring procedures; and in other part by assisting overseas law enforcement authorities through the improved cooperation channels. Challenges relating to insider dealing and market manipulation will be tackled primarily by strengthening procedures for the licensing and regulation of the securities dealers to ensure that the sector is open only to institutions with the highest level of integrity.

Money Laundering Vulnerabilities

27. The structure of the OFC, the legal framework that underpins it, the type of institutions that are active in the sector, and the institutional arrangements for supervision and oversight of their operations give rise to a number of potential ML vulnerabilities.

Structural Vulnerabilities

Government Policy towards the OFC

28. The authorities recognise that clear strategic policy direction towards the OFC is required. Successive governments and the relevant competent authorities have not benefitted from a comprehensive analysis of what the key objectives are in hosting the OFC, and what market it can reasonably serve to best effect, while mitigating the risks of criminal abuse and reputational damage for Vanuatu. To some extent, this may derive from the relative lack of political stability within Vanuatu, where governments depend on fragile coalitions, tend to be very short-lived, and are generally pre-occupied with domestic social and economic issues. The lack of a strategic policy exposes the sector to short-term initiatives (frequently for purely financial reasons), and to external influences and drivers. This results in the OFC evolving in a way that makes it vulnerable to factors that the authorities may not have properly assessed, and for which it has no policy or operational response.

29. A primary example of this is in relation to the licensing of securities dealers. Over the years, Vanuatu has enacted a number of OFC laws that have essentially laid dormant through lack of market appetite for the products. In the case of the securities dealers¹⁵, external factors suddenly sparked an upsurge of interest in such licences, but the authorities undertook no analysis of either the reasons or the associated risks, and had no clear policy on how to respond to the changed circumstances. All subsequent applications have been approved. This has resulted in the creation of a vulnerability that is very similar to what happened with the international banks prior to the reforms implemented in 2002, when the banks were almost entirely unregulated, resulting in a significant adverse impact on Vanuatu's international reputation and standing. Since 2002 the RBV has taken a number of measures to bring the banking sector under proper regulatory oversight. The Government's intention now is to take similar measures with respect to the securities dealers, following the enactment of amendments to the governing legislation.

Scope of the Money Laundering Offence

30. The mutual evaluation report prepared by the APG highlighted a number of material deficiencies in the legal framework that have a general impact on Vanuatu's vulnerability to ML, but some of which are particularly relevant to the OFC. These included the fact that the range of predicate offences for ML did not cover tax crimes, illicit arms trafficking, piracy of products, insider trading and market manipulation. This, in turn, restricted the ability of the competent authorities to provide international cooperation to assist with investigations, in view of the dual criminality concepts. In its subsequent engagement with the FATF's ICRG process, Vanuatu committed to enact amendments to 31 laws to address

¹⁵ Examples of other legislation that is effectively dormant relate to the licensing of mutual funds and unit trusts.

the deficiencies, although a significant number of the changes are consequential amendments to inter-related laws. As of June 2017, the government had enacted thirteen priority laws that addressed the concerns relating to the scope of the ML offence. The list of predicate offences now complies with the FATF standards and includes elements that are of particular relevance to the threats faced by the offshore sector (i.e. foreign tax crimes, insider dealing and market manipulation).

Regulatory and Law Enforcement Capacity

Regulators

31. The resources available to the supervisory authorities that oversee institutions that are active within the offshore sector are improving, but remain quite limited. This continues to pose a material vulnerability with respect to ensuring compliance by institutions covered by the AML/CFT law, but all the regulators have now been given appropriate statutory and administrative powers that will allow them to develop more robust supervisory frameworks over time. These powers include enhanced market entry requirements, improved due diligence procedures, and expanded prudential and AML/CFT reporting requirements that will allow for an improved analytical capability.

32. The **VFIU** has legal responsibility for ensuring ML/TF compliance by all reporting institutions in both the domestic and offshore sectors. The VFIU's compliance department has five staff members, four of whom have been brought on board since September 2016. Prior to that date, the single compliance officer was able to conduct a maximum of three inspections of reporting institutions each year. The additional resources have now allowed a significant increase in the inspection programme, which is supported by offsite reviews of material supplied by the institutions¹⁶. The annual offsite reviews, which are short in duration, are used to allocate a risk rating to each institution, which helps to prioritise the inspections. The reviews may also lead to a Compliance Direction being issued to a reporting institution. In addition, the VFIU may undertake target-based inspections where a specific breach or material deficiency has been identified.

33. As of June 2017, the VFIU has undertaken a total of nineteen onsite inspections, of which four related to the offshore sector (all CTSPs). It expects to be able to perform 8-12 inspections annually in the future. In addition, the VFIU has entered into a MoU with the RBV to cooperate on supervisory matters and to share information. In effect, some of the supervisory functions of the VFIU have been undertaken by the RBV in relation to the international banking and insurance sectors. This role has now been formalised under the June 2017 amendments to the Anti-Money Laundering and Counter-Terrorism Financing Act, which gives the VFIU the power to delegate AML/CFT supervisory functions to the RBV and any other domestic regulator (e.g. the VFSC). Where responsibility has been delegated, the regulators will also acquire the relevant enforcement powers provided under the Act. These measures will assist in strengthening the overall supervisory framework over time.

¹⁶ The offsite reviews are based on three documents submitted by institutions at the time of their initial registration, supplemented by an annual submission of their AML/CFT procedures manual. The VFIU also stores any relevant externally-sourced information in its database.

34. In March 2016, the VFIU introduced a requirement that certain reporting institutions¹⁷ should undergo an AML/CFT audit by independent auditors, covering fourteen specific areas. In principle, this is a positive move that should provide the regulators with greater insight into compliance levels, although further work is planned to try to introduce greater standardisation of the audit procedures. The first analyses of these reports were undertaken in late-2016 and early-2017, and feedback provided to the institutions. Further analysis is to be undertaken to establish the true extent to which the audits add value to the overall supervisory process.

35. The VFSC created its Supervision Department in October 2016 in particular response to the rapidly growing number of applications for securities dealer licences. Prior to that, responsibility for undertaking due diligence checks of licence applicants rested with the Legal Enforcement and Compliance Department. The new Supervision Department, which has responsibility for oversight of compliance with the prudential and conduct-of-business requirements by the CTSPs and securities dealers, has one staff member allocated to the supervision of each sector. The VFSC currently does not receive any regular financial and supervisory returns that allow it adequately to understand the business and associated risks associated with the entities that it supervises, and no substantive compliance inspections have yet been undertaken. The development of a more robust supervisory capacity is a priority issue for the VFSC, and will necessitate additional skilled resources. In addition, following the June 2017 amendment to the AML/CFT law, the VFIU may, in future, delegate formal responsibility for AML/CFT compliance monitoring to the VFSC in respect of those institutions for which it currently has supervisory responsibilities, subject to the VFSC having adequate resources to undertake the task.

36. The RBV is relatively well placed to perform its supervisory responsibilities with respect to the international banking and insurance sectors, but the resources, in terms of staff numbers, remain very limited. It maintains three supervisory units, two of which cover sectors that include offshore institutions. The Banking Supervision Unit oversees eleven institutions, including the six international banks, while the Insurance Supervision Unit has responsibility for twelve insurers, including six captives and three international insurers. Each Unit has a staff complement of three examiners (one manager and two supervisors). Since 2014, the RBV has undertaken six inspections of international banks and two of international insurers. The inspections have included some elements of AML/CFT compliance, but the primary focus has been on prudential matters. In practice, several of the recent concerns arising with respect to the regulated institutions (international banks, in particular) have been triggered by the actions of overseas regulators, rather than by the RBV's own supervisory approach. Given the limited resources, the RBV moved to adopt a risk-based approach to AML/CFT supervision in 2017. It also required the international banks to conduct AML/CFT risk assessments and audits in 2016. The RBV is using the assessments as a basis for its current AML/CFT onsite reviews.

37. As part of the overall AML/CFT regime, the NCC has mandated two Working Groups (Supervision and Law Enforcement) to work closely with the government agencies on the implementation of reforms. The Supervision Working Group has put together a national supervisory framework in line with the recent changes to the legislation. This will

¹⁷ Within the offshore sector, this included the CTSPs, international banks and insurance companies. The securities dealers were not included, but the requirement will be extended to them in September 2017.

guide how the principal AML/CFT supervisor (VFIU) and the other supporting supervisors (RBV, VFSC and DCIR) will address supervision matters.

Law Enforcement

38. Established at the beginning of 2017, the Money Laundering Unit (MLU) within the Vanuatu Police Force is the specialist team tasked with investigating ML cases. The new unit is presently investigating one ML case involving the domestic sector, but no cases relating to the offshore sector have ever been investigated by the Vanuatu Police. The MLU has a dedicated staff of two, but can seek assistance from other units within the Vanuatu Police Force as required. The Transnational Crime Unit (TCU) provides intelligence support to the MLU. The TCU has a staff of six, including one officer attached to the VFIU. The TCU's primary focus is on drug offences with a transnational connection, and other sensitive investigations, but it is also tasked with TF investigation. The MLU and TCU together form the National Intelligence Unit within the Police Force. However, neither unit has yet been able to develop capacity to undertake financial analysis, and neither has prioritised or triggered ML investigations when other investigations identify the proceeds of crime. As a result, the MLU and TCU are untested in terms of investigating potentially complex cases of ML or TF involving offshore entities. In general both units are reactive, rather than proactive, in the detection and investigation of ML/TF offences. The delivery of appropriate training to officers within the MLU is a priority, and in-country assistance is being provided by the Australian Federal Police to increase local policing capacity.

Regulatory Enforcement Actions

39. The AML/CFT law and regulations provide for both criminal and administrative sanctions for non-compliance with AML/CFT obligations. These sanctions apply to both individuals and institutions. In the case of a criminal conviction, an individual may be fined (in the range of VT1mn-VT25mn) or imprisoned (1-5 years), while an institution may be fined between VT5mn and VT100mn. The 2015 amendment to the AML/CFT law permits the VFIU to apply lower administrative penalties for the same offences, where the person or institution elects not to have the matter determined by the court. The VFIU also has the power to issue directions to an institution and to remove a director, manager, secretary or other official when they are deemed not to be fit and proper. The following table records the enforcement measures that have been taken with respect to the offshore sector.

Table 1: Enforcement undertaking measures (2014-2016)

Enforcement Measure	Securities Dealers			International banks			Insurance			CTSPs		
	2014	2015	2016	2014	2015	2016	2014	2015	2016	2014	2015	2016
Compliance Direction	0	0	2	1	4	6	2	2	4	4	15	18
Compliance Report	0	0	4	0	3	4	0		6	0	10	19
Warning	0	0	4	0	2	7	0	2	7	0	10	17
Penalty Notice	0	0	1	0	0	0	0	0	0	0	0	1
Payment	0	0	0	0	0	0	0	0	0	0	0	0
Removal of Entity	0	0	0	0	0	0	0	0	0	0	0	0
Removal of Director, Manager, Secretary or Officer	0	0	0	0	0	0	0	0	0	0	0	0

40. The VFIU routinely uses its power to issue directions and warnings in cases where it identifies AML/CFT deficiencies through its offsite or onsite procedures. The VFIU has also progressed, in a very few cases, to the stage of issuing penalty notices to institutions for failure to address the deficiencies, but no financial penalties or other sanctions have actually been enforced. The VFIU policy in the period 2014-16 has been to engage with the private sector to encourage compliance rather than resorting to enforcement. The June 2017 amendments to the AML/CFT law provide more expansive enforcement powers (particularly with respect to civil money penalties), and the VFIU will be examining how best it might ensure that future enforcement actions can be rendered effective, proportionate and dissuasive.

Transparency

41. Since 2016, the government has taken significant measures to improve transparency within the offshore sector. Amendments to the International Companies Act in 2016 included changes to address aspects of the law that deliberately drew a veil over the ownership and business of ICs. These aspects included the ability to issue bearer shares and bearer share warrants, the use of nominee shareholders and directors, and stringent secrecy provisions that made it a criminal offence for any person to disclose or seek information relating to the shareholding, beneficial ownership, management, business, affairs or transactions of an IC, except under a court order. The 2016 amendment required bearer shares to be registered and introduced an obligation for ICs to file details of beneficial ownership with the VFSC.

42. By end-2016, approximately 90% of ICs had provided information on their ownership, and the VFSC has started action to strike off those companies that have not complied. These amendments help to improve transparency of company ownership,

provided that the CTSPs, which have the obligation to file the information with the VFSC on behalf of their clients, have robust customer due diligence procedures that permit them to establish the true ultimate beneficial owner of the companies for which they act as agents. These provisions were further strengthened by the June 2017 amendment to the International Companies Act, which expands the definition of beneficial ownership, abolishes bearer share warrants, and requires nominee directors and shareholders to file details of their nominator.

43. The 2016 amendment also made changes to the secrecy provisions, but it retained the basic criminal offence for disclosure of company records, subject to certain gateways for disclosure that remained subject to strict conditionality. Further amendments were made in June 2017 to improve the facility of the VFSC to exchange information in relation to international companies with domestic and foreign law enforcement and regulatory authorities.

44. Overall, the 2016 and 2017 amendments represent a significant step forward towards providing greater transparency of the international company sector. It is the intention of the VFSC to review its resources and procedures to ensure that it can respond fully and promptly to future requests for information in relation to the IC sector, including ICs that hold licences to engage in offshore financial services.

Corruption

45. Corruption is an issue of concern in Vanuatu¹⁸. In a recent case, 14 elected members of parliament were imprisoned on corruption charges. While corruption has a material impact on broader social and economic issues, it can also impact the integrity of the overall context in which the financial sector operates. The Government is giving priority to such matters, and has been seeking to increase awareness within the public and private sectors through various initiatives. It is currently preparing a National Anti-Corruption Strategic Framework, which will be overseen by the newly created Anti-Corruption Committee.

International Cooperation

46. Both the VFIU and the State Law Office¹⁹ (SLO) have received a small number of international requests for cooperation over recent years. In some cases, these are related to investigations into fraud, potentially involving Vanuatu international companies. In general, the response times to these requests has been slow, with the SLO taking between five months and nearly two years to respond to MLA requests over the period 2014-2016. This has been due, in part, to the lack of a dedicated unit within the SLO possessing the resources and skills to process formal requests; and, in other part, to challenges in identifying the source of, and subsequently obtaining, the relevant information. Such delays in handling MLAs can frustrate criminal investigations taking place in other jurisdictions, and can allow the dissipation of illicit funds that are the subject of investigation. In addition, as discussed elsewhere in this report, there remained a number

¹⁸ Transparency International's 2014 National Integrity System Assessment of Vanuatu concludes that: "The functioning of most pillars [representing key public and private institutions in a country's governance system] is weakened by failures within the legislature and executive to play their role in the "cycle of accountability" and to maintain a stable policy direction. These failures largely stem from lack of political integrity. Unless lack of political integrity is addressed it will be impossible to consistently develop laws, policies and practices that support national integrity".

¹⁹ The Central Authority for processing mutual legal assistance requests.

of legal obstacles to effective international cooperation by the regulators and law enforcement in relation to entities in the offshore sector (e.g. secrecy provisions and weaknesses in relation to dual criminality).

47. The government has now amended legislation (June 2017) to remove those obstacles, which should assist the authorities to respond to international cooperation requests on a more comprehensive and timely basis, subject to the allocation of appropriate resources to the task. The Central Authority's responsibilities for dealing with mutual legal assistance requests (including extradition) are being moved from the State Law Office to the Office of the Public Prosecutor (OPP) during 2017. The OPP is in the process of training staff to take on this role, and it is committed to providing an efficient and timely response to future requests for cooperation.

Institutional Vulnerabilities

International Companies

48. As at May 2017, there were approximately 4,500 active ICs on the register. The turnover is high, suggesting that the average company has a relatively short life-span, and that ICs are predominantly used for one-off or very time-limited functions, rather than for long-term business or commercial purposes.

Table: Annual Turnover of International Companies

Year	Incorporated	Struck-off
2014	2,679	1,667
2015	850	387
2016	713	868

49. According to VFSC estimates, the top five countries from which the owners of the companies originate are China, Hong Kong, Australia, New Zealand and Malaysia. The only growth area is the business from China, but this has not compensated for the general decline of business.

50. Until the 2016 amendment to the International Companies Act, the register contained only very basic information on the companies' legal structure, shareholding and governance. Following the amendments in 2016 and 2017, companies (and their registered agents) are now required to file details of the ultimate beneficial ownership. As of end-2016, approximately 90% of the companies had complied with this requirement. The VFSC has started action to strike off those companies that have not complied.

51. There is no obligation under the Act to prepare and submit audited financial statements to the VFSC, and the books and records may be held at any location of the directors' choosing, not necessarily at the registered office. Consequently, the VFSC (as administrator of the company registry and as regulator) does not have immediate access to, information on the real nature of a company's business or its financial position. Equally, such information is not routinely available to the companies' registered agents. The June 2017 amendments to the International Companies Act have helped improve materially the VFSC's ability to obtain information promptly, by giving it the power to require a company to provide information, on demand, in relation to its "integrity, competence, financial

standing or organisation”. The use of this power will allow the VFSC to assist more comprehensively than in the past with law enforcement and regulatory enquiries and investigations.

52. The number of ICs that are truly active may be substantially lower than the headline statistics suggest. A total of 21,156 ICs were incorporated in relation to the government’s Permanent Residence Visa Program. This program was directed primarily at citizens of the PRC, with the objective of using the visa to obtain transit rights that permit them to stay temporarily in Hong Kong or Macau. As part of the program, the Government of Vanuatu required the applicant to establish an international company²⁰. In practice, the VFSC estimates that the majority of these companies are struck off at the end of each year, since there is no obligation to maintain them after the visa has been issued, and they have no specific business purpose. Over 16,000 ICs have now been struck off the register, but some companies linked to the Visa Program may still remain, and may be expected to lapse in the near future. This Program was terminated in January 2015.

53. Excluding the visa program and those entities that require licences to conduct financial services, the private sector service providers estimate that the majority of the companies are single asset-holding vehicles, mostly linked to real estate or other high-value items, although this does not preclude the possibility that there is an income stream into such companies resulting, for example, from property rental payments. The following data obtained from a survey conducted of some 75% of its membership by the Vanuatu Finance Centre Association (VFCA)²¹ provides the only analysis that is available.

Table: Type of business conducted by International Companies

Type of activity	Proportion of ICs
Holding companies (e.g. single asset)	34%
Investment companies (forex, securities, hedge fund, mutual fund, private equity)	32%
Trading companies (export, import, retail, wholesale)	9%
Services industries	9%
Manufacturing companies	4%
Raw materials (resource extraction, agriculture)	4%
Transport	2%
Non-Profit organisations	1%
Technologies	1%
Education and research and development	1%

54. This survey captured only 1500 of the 4500 registered international companies (i.e. 32%). While the characterisation of their activities from the survey cannot necessarily be extended to all companies on the register, the survey provides a valuable guide to the

²⁰ The program was substantially outsourced to a Hong Kong service provider (Pacific Resources Group) and the VFSC had a secondee posted in Hong Kong to facilitate the company incorporations.

²¹ The survey was specifically commissioned in order to provide input to this assessment. It provides the only direct analysis that is available of the purposes for which ICs have been established..

primary purposes for which Vanuatu ICs are being used beyond those linked to the Permanent Residence Visa Program.

55. The VFCA survey also examined the motives behind the use of Vanuatu as an offshore centre. The breakdown in the following table tends to confirm that tax planning (including succession provisions) and the strict confidentiality provisions have been the key drivers in the past.

Table: Reasons for use of OFC

Reason	Percentage
Cheap savings vehicle to hold assets and conduct international activities	30%
Tax planning	25%
Confidentiality	23%
Succession planning	13%
Visa or citizenship programs	6%
Risk diversification	3%

56. The VFCA survey also indicates that about 25% of the business comes through third-party introductions, where the local service provider is relying primarily on the documentation relating to the client being supplied by the introducer. However, the majority of business results from three sources: direct contact with the client, either online or a physical visit to Vanuatu; through existing client referrals; or through overseas networks owned by the service provider. The service providers report that approximately 10% of potential business is rejected on the grounds that satisfactory evidence of beneficial ownership cannot be established. It is difficult to draw any firm conclusions from these data, but they do tend to suggest that the service providers are effective, to some extent, in filtering out some of the potentially suspect business. However, approximately one-third of the service providers suggest that, once the business relationship has been established, they do not consider that they have the duty to monitor the clients' business to establish that they are using the companies for the purposes stated at the outset. Section 8 of the AML/CFT regulation states that, "a reporting entity must have a customer monitoring process where it can monitor its relationship with its customer to ensure that the customer's activities being conducted is consistent with its knowledge of the customer, the customer's business, source of funds and risk profile". This requirement extends to CTSPs providing purely registered office facilities. The failure to comply fully with the regulation potentially undermines the objectives of the suspicious activity reporting obligations.

57. Only two of the domestic banks are willing to provide banking services to ICs, based on their own risk assessments, and the VFCA reports that it is extremely difficult to open accounts in Vanuatu for clients using such companies. The domestic banks state that they face a particular challenge in being able to establish the ultimate beneficial ownership of ICs, to the extent that they feel it necessary to take additional steps to those that they would normally employ. This had led to an increased unwillingness to continue dealing with business linked to the OFC, including with the CTSPs. The consequence is that, where ICs wish to have access to financial services, they will mostly have to deal with institutions based outside Vanuatu.

58. The VFSC data indicate that, in the period 2014-2016, only four requests were made for information on international companies by domestic and foreign law enforcement. The small number of international cooperation requests made to the VFIU and SLO relate primarily to fraud investigations, where a Vanuatu international company has been used as a channel for illegal proceeds.

Trusts and Other Legal Arrangements

59. There is no specific trust law in Vanuatu, but trusts can be created under common law principles that are evolving in Vanuatu. There are no comprehensive data on the number of trusts that have been created, although the survey of its membership by the VFCA provides some helpful analysis of the location of the trust settlors.

Table: Location of trust settlors

Location	Number	Percentage
Australia and New Zealand	91	41%
Europe	50	22%
Other Pacific	14	6%
Africa	5	2%

60. The numbers recorded in this survey appear to be very low relative to what might be expected in other common law jurisdictions. The absence of an established legal framework for trusts may be a disincentive for non-residents to use Vanuatu as an offshore jurisdiction of choice. The ML risks deemed, through study of international typologies, to be associated with trusts may well exist in Vanuatu, but the creation of trusts does not appear currently to be a material business within the jurisdiction that might give rise to any significant AML/CFT risk. However, it is recognised that the information currently available to the authorities on the trust business in Vanuatu is insufficient to allow a reasoned judgement.

61. In order to obtain an improved picture of the sector, the VFIU has included a reference to such activities in its new registration form (issued in March 2017). Where trust activities form part of an institution's business profile, the VFIU intends to request additional information on their nature and scale. This will enable the VFIU, in due course, to improve the analysis and understanding of the potential ML/TF risks associated with the trust business in Vanuatu. In addition, the authorities have recently commissioned a specific project to gain a better understanding of the extent to which trusts are a feature of Vanuatu's offshore sector, and to consider whether a statutory framework for trusts should be developed.

International Banks

62. As previously described, the supervisory regime applied to the international banks has been tightened significantly since 2003, and the number of licensed entities has fallen dramatically (from 35 in 2003 to six, as at May 2017), although new applications continue to be received on a regular basis. According to RBV records, ultimate ownership of the existing banks rests with persons based in Lithuania, Indonesia, Denmark, Canada, China,

Hong Kong, Singapore and Japan. The recent applications have tended to originate from China and Hong Kong²².

63. The scale of the operations of the banks is relatively very small, with the largest having total assets of around USD90 million, with the sector as a whole reaching a total of only USD106 million. The scope of the activities of the banks is limited, with some focusing on private client business and others acting as intra-group or family banking operations. As part of the routine reports filed by each bank, the RBV receives a list of all the bank's clients, which allows the RBV to monitor the trend in the customer base.

64. The primary vulnerability of the banks (recognised by both the private sector and the regulators) is to tax evasion by their clients, but the very small size of the sector (in terms of both assets and client base) means that the potential scale of any such activity is quite restricted. In 2016 the RBV required all the international banks to submit copies of their internal risk assessments and AML/CFT audits, but, in the opinion of the RBV, the former have tended, with one exception, to be very generic documents that provide little insight into how the banks apply mitigating measures against their key risks. The RBV is seeking to focus greater attention on potential tax evasion through the international banks, in recognition of the particular risks that have been identified.

65. A second vulnerability is to criminal abuse of an international bank by its owners or management. Although the RBV undertakes "fit and proper" assessments of prospective owners and management, these tend largely to be desk-based reviews, relying largely on information taken from proprietary databases. These are of limited value in establishing the *bona fides* of applicants, especially since the applicants appear rarely to have direct previous experience in banking. Moreover, the on-going contacts with the ultimate "mind and management" of the banks is limited. Although the banks are now required to maintain a physical presence (and their books and records) in Vanuatu, in the majority of cases the true management of the entity is located outside the jurisdiction, and the role of the local staff is often simply to respond to instructions from the principals. This does not apply to the single largest of the international banks (accounting for 85% of the sector's assets), which has a more substantial management team based in Vanuatu. In other cases, the RBV has little opportunity to form a proper supervisory relationship with the substantive management.

66. In recent years, the RBV has become aware, through actions taken by authorities overseas, of suspected illicit activities being undertaken by Vanuatu international banks²³. The RBV, itself, had not been in a position to identify the problems through its own supervisory oversight, but has subsequently taken action to revoke the licences based on the available information. Given that the business of most of the international banks is driven primarily by principals based outside Vanuatu, the RBV has attempted to develop informal

Case Study F

"Kevin Lai, the 49-year-old Malaysian President of the United Development Bank of the Pacific (UDBP) and Charge D'Affaires for the Honorary Consul of Vanuatu in Thailand has been arrested and charged in Thailand.

Lai was arrested over alleged money laundering and running an illegal pyramid Ponzi scheme allegedly milking Vt945 million from over 8000 investors from China, Malaysia and Thailand and sending money invested through Malaysia to UDBP Bank in Vanuatu."

Source: Vanuatu Daily Post, 25 May 2015

²² One such application was rejected in 2016.

²³ This has included at least one case where an international bank was seeking to raise deposits illegally (i.e. without an appropriate licence) in a foreign jurisdiction.

contacts with overseas regulators to help improve its understanding of the operations.

Securities Dealers

67. Although the legislation governing the licensing of securities dealers has been on the statute book for many years, it is only since 2015 that any real interest has been shown by potential licensees. Since then, the number of licences issued has risen dramatically (with over 400 by May 2017). According to the VFSC estimates, the top five jurisdictions from which the applications originate are Peoples Republic of China, Israel, Russia, Ukraine and the UK. Stakeholders believe that the upsurge in applications has been linked to low capital requirements, relatively cheap licence and incorporation fees, a small bond deposit, a perception of minimal supervision, and actions in other offshore jurisdictions to tighten their licensing and bonding requirements. Just short of 300 licences were issued in the three years 2014-2016, during which time no applications were rejected.

68. Vanuatu has, in the past, exercised minimal supervision over this sector. The application process has been limited in scope; there have been no substantive routine reporting requirements; and the VFSC has not had the capacity or practical capability to supervise the securities dealers, which operate almost exclusively via the Internet. The structure of the sector and the absence of any real supervisory capacity have resulted in it being extremely difficult for the authorities to understand how licensees, in general, are conducting their business, and the extent to which they are vulnerable to the risk of money laundering and the commission of predicate offences.

69. The June 2017 amendments to the Dealers in Securities (Licensing) Act have strengthened the market entry requirements to include details of beneficial ownership; information on each director, controller or manager; the source of funds for the business; information on whether the principals are involved in regulated activities in other jurisdictions; and a substantive business plan. The amendments also provide the VFSC with significantly enhanced supervisory and enforcement powers; increase the bond deposited by licensees from VT200,000 to VT5 million; and introduce new offences of insider trading and market manipulation. Furthermore, the VFIU intends, in September 2017, to extend to the securities dealers the requirements to submit AML/CFT risk assessments and annual AML/CFT audits. These measures provide the authorities with appropriate tools to supervise the securities dealers sector, subject to their acquiring adequate resources to address the number of licensees and the complexity of their business.

70. There is a degree of evidence to suggest that some existing licensees are engaging in questionable activities. A search of some of the websites gives rise to a number of “red flags” in relation to the claims being made about guaranteed returns and 100% security of funds placed by investors with the institution. Many of the websites also make unrealistic claims about the extent of supervision exercised by the VFSC. Since December 2015, the VFSC has received over 250 complaints from investors who claim to have been defrauded by licensees, but there has been sufficient information on which to pursue an active enquiry in only a handful of cases. In addition, the VFIU has received several international requests for assistance in relation to alleged fraudulent marketing/promotions and customer complaints alleging fraud by licensed dealers. The names of Vanuatu licensed dealers also feature regularly on fraud alert websites run by private sector “watchdogs”.

71. It is also apparent that some of the licensees are marketing their services in contravention of laws in other countries, where they should require local authorisation to

conduct securities business with residents. Warnings appear on the websites of numerous securities regulators in Europe and elsewhere, alerting people to the fact that certain named broker dealers registered in Vanuatu do not have authorisation to provide services in the jurisdiction in question²⁴. At the very least, this brings into question the ethics of those involved in some of the licensees, and poses a material reputation risk for Vanuatu. The new Financial Dealers Licensing Rules, introduced in June 2017, now also require applicants and existing licensees to provide certified copies of registration and licence certificates from countries in which they operate or deal in securities to ensure that licensees are not operating illegally in trading jurisdictions.

Insurance companies

72. Only one of the ten licensed offshore insurers²⁵ offers life or investment-related policies. The focus of the others is diverse, including policies relating to funeral benefits, sports liability, property, after-the-event legal expenses and freight forwarding. There is no evidence to suggest that the Vanuatu offshore insurance sector is attractive for the establishment of entities wishing to engage in investment-related activities, and the risks associated with this sector are considered to be low.

Company and Trust Service Providers

73. The CTSPs are essentially the gatekeepers to the OFC, as they act for clients in the incorporation of international companies, the provision of nominee shareholders and directors, the provision of registered offices, and the application for licences, where they are necessary. There is a broad cross-section of businesses and individuals that provide these services, and this is reflected, to some extent, in the range of different types of licence issued to service providers.

74. As is the case with most entities that are active in the offshore sector, the CTSPs have been subject to only basic application procedures, and minimal on-going supervision for either prudential or AML/CFT compliance. There has been no requirement for licensed CTSPs to file routine prudential or conduct-of-business reports to the supervisor. The VFSC has only one person employed on general supervision of this sector, and the VFIU has undertaken very few inspections of CTSPs. Therefore, the authorities recognise that they lack any substantive assessment of whether the CTSPs are meeting their AML/CFT obligations, specifically in relation to record-keeping, customer due diligence, the identification of ultimate beneficial ownership, risk profiling and on-going due diligence based on an understanding of the client's business. The VFSC will seek to address this matter in late-2017. In addition, the introduction of the annual AML/CFT audit may assist in improving the understanding in these areas.

Standards of Compliance

75. Despite the limitations to their supervisory practices, the regulators have identified a number of common AML/CFT deficiencies across both the domestic and offshore sectors. These include a failure to undertake proper AML/CFT risk assessments and to implement risk-based systems and controls; inconsistent application of customer due diligence (CDD)

²⁴ E.g. British Columbia, Denmark, Italy, Estonia. The services are often provided under trading names that link back to the Vanuatu licensed dealer.

²⁵ Two hold "international" licences, six are "captives" and one is a "re-insurer". In addition, there are two external insurers providing domestic cover.

procedures; poor staff awareness of AML/CFT issues; and poor financial reporting to the VFIU. Institutions have been found generally to have good transactional record-keeping procedures, but perform less well with respect to CDD records. Going forward, the supervisors will seek to ensure that, in the short term, there are significant improvements in the problem areas.

76. All institutions covered by the AML/CFT legislation have an obligation to report to the FIU any transactions or activity that they suspect or have reasonable grounds to suspect involve proceeds of crime. In practice, the reporting regime for institutions within the offshore sector does not appear to function properly, based on the very limited number of reports filed by key entities within the sector.

Table: Combined Totals of Suspicious Transaction Reports (STRs) and Suspicious Activity Reports (SARs) filed by Reporting Entities

Sector	2014	2015	2016
Domestic banks	35	40	76
International banks	4	0	0
Insurance companies	0	0	0
Securities dealers	0	0	0
CTSPs	0	0	0
Money remitters	15	6	25
Lawyers	1	0	0
Accountants	2	1	4

77. The VFIU data indicates that, apart from the four STRs submitted by the international banks in 2014, there have been no reports emanating from the offshore sector, although those submitted by the accountants may well be in their capacity as CTSPs. The low level of reporting by the international banks may be explained by the small size of their operations, the very narrow (and, in some cases, related-party) customer base, and the small number of transactions performed on a daily basis. Elsewhere, the explanation for the failure to file STRs is less easy to explain, and appears to indicate either a lack of awareness of the reporting obligations (entirely possible with respect to the securities dealers that have no physical presence in Vanuatu), or a failure to implement effective ongoing CDD and transaction monitoring procedures (issues already identified through the VFIU's supervisory programme).

78. The VFIU data indicate that the CTSP sector as a whole (including the lawyers and accountants) has filed very few STRs since the legal obligation was introduced. Accountants and lawyers have filed only eight reports over the three years 2014-2016, but none of these have related to matters associated with ICs or other offshore entities. This is very difficult to understand, given the gatekeeper role of the CTSP sector, and the fact that the reporting obligation relates to actual and attempted suspicious transactions and activity.

79. The absence of an effective reporting regime deprives the VFIU and law enforcement of essential intelligence on which investigations into criminal behaviour in the offshore sector might be based. This is an area to which the VFIU and other regulators will

continue to pay particular attention in their outreach and inspection programmes to ensure awareness of, and attention to, the reporting obligations.

Significance and Likelihood of Money Laundering Vulnerabilities

80. As is the case when considering the money laundering threats, the shortage of data on some of the issues presents a significant challenge to developing a picture of the relative importance of the institutional vulnerabilities that have been identified. However, this does not apply to the same extent to the structural vulnerabilities, for which there is a reasonable degree of evidence to support the assessment. Again, the following “heat map” has to rely to some extent on intuitive rather than empirical factors, although there is a relatively sound basis for allocating the majority of the issues within the matrix.

81. The factors considered when assessing the likelihood that a particular vulnerability will be exploited vary depending on whether the vulnerability is structural or institutional. For structural matters the key considerations are: the extent to which the issue is central to good governance, generally; the integrity of the legal framework; and the degree to which there is a proper regulatory and law enforcement capacity. For the institutional vulnerabilities, the following apply: the relative scale and complexity of the activity; the extent to which an activity represents a “gatekeeper” role to the OFC; the ease with which illicit funds may enter or be moved within a particular sector or activity; and the extent to which there is an effective regulatory regime in place to ensure AML/CFT compliance.

		Likelihood of Occurrence		
		Possible	Probable	Very Likely
Significance of vulnerability	High		International cooperation Standards of compliance International companies International banks CTSPs	Policy framework Regulatory capacity Transparency Securities dealers
	Medium	Corruption	Legal framework Trusts	Investigative capacity
	Low	Insurance companies		

82. A priority of the Government will be to establish a clear policy framework within which the offshore sector will operate, as this will help determine the extent of the measures and resources that will be needed to address the key vulnerabilities that have been identified, such as the issues relating to regulatory capacity and the securities dealers. At the same time, the authorities will work to ensure that measures to improve transparency of the activities within the offshore sector are fully implemented, so that Vanuatu may be able to provide rapid and constructive assistance to overseas counterparts where appropriate.

Part Two: Terrorist Financing

83. There have been no recorded cases of domestic terrorism in Vanuatu, which has resulted in a presumption, among some stakeholders, that there is no TF risk within the country. In practice, however, terrorist financiers and criminals employ similar methods to raise, store and transfer funds, and so the vulnerabilities that exist with respect to ML may also be applicable to some extent to TF. The absence of a domestic terrorism threat does not mean that a country's financial system and institutions cannot be used to raise funds for terrorist activities abroad, or to transfer funds from one foreign jurisdiction to another.

Terrorist Financing Legislation

84. TF is criminalized under the Counter Terrorism and Transnational Organised Crime Act. The legislation is broadly in line with international standards, following amendments to the Act in June 2017, when the definition of the terrorist financing offence was broadened. The authorities have no experience of investigating or prosecuting TF offences, and the legislation is entirely untested in Vanuatu. Awareness of the threat and techniques of TF has generally been poor within law enforcement and regulatory authorities, and there have been no policies, procedures or mechanisms in place to identify and investigate TF offences, but measures are now being implemented to improve awareness and to implement an appropriate framework.

Scope of the TF Threat

85. The most likely potential threat faced by Vanuatu in relation to TF comes from its role as an OFC, which presents the opportunity for terrorist financiers to create and employ international companies, legal arrangements and other structures to raise, conceal, move and distribute funds. That said, it has not been possible to identify any evidence that Vanuatu offshore entities have been used for TF purposes. Moreover, there have never been any STRs relating to TF filed with the VFIU, none of the international cooperation requests have been focused on TF, and the law enforcement agencies have not had any basis on which to investigate potential TF or terrorist activity.

Targeted Financial Sanctions

86. The Government accepts that there have been material weaknesses in the procedures relating to targeted financial sanctions that might mask, to some extent, the TF threat posed to Vanuatu. Critically, the 2015 APG mutual evaluation report concluded that no procedures and mechanisms existed for the update and dissemination of the UN Security Council's sanctions list to private sector reporting entities; no outreach had been undertaken to the private sector on implementation of targeted financial sanctions; and no steps had been taken to address proliferation financing. In effect, there has been no process in place to ensure that the assets of designated persons may be identified and frozen without delay. No reports of matches with the names of designated persons (including "false positives") have ever been filed with the VFIU.

87. The Government of Vanuatu has committed to address these deficiencies. Outreach has already been made to the private sector to raise awareness²⁶ and to verify that the

²⁶ It is recognised that many institutions within the private sector currently undertake routine checking of clients against lists of designated persons using third-party providers' watchlists, and those published by foreign governments.

institutions have not engaged in business with any designated persons. In addition, new legislation was brought into force in June 2017 (United Nations Financial Sanctions Act) to establish a firm basis for implementing procedures to comply with Vanuatu's international obligations.

Non-Profit Organisations

88. There is a substantial number of NPOs operating in Vanuatu, but the exact number is unknown. While there are two laws relevant to the NPO sector - the Charitable Associations (Incorporation) Act and the Foundation Act - registration of charitable associations has, in the past, been voluntary, and was only available to those associations that had a committee of six members or more. A primary advantage of being registered is that it gives limited liability to members and grants incorporation status, which facilitates the opening of a bank account. As of May 2017, there were 273 registered charitable associations and 9 foundations. There are no estimates of the number of unregistered NPOs, but proposed amendments to the Charitable Associations (Incorporation) Act (expected to be considered by parliament in late-2017) will make registration mandatory for all NPOs.

89. While NPOs are reporting entities under the AML/CFT legislation, there is currently no supervisory process in place to monitor compliance with the obligations. The VFIU has been undertaking extensive outreach to the sector, and the registration process under the AML/CFT law is underway. Prior to 2015, the only regulatory obligations imposed on the NPO sector took effect at the registration stage, when applicants were required to submit a constitution or charter, a list of members, and a statement of assets and liabilities. In 2015 an amendment to the Charitable Associations Act introduced a requirement for registered NPOs to submit annual reports of their activities to the VFSC, and gave the VFSC the power to inspect the NPOs' books and records and to require members to respond to any enquiries that the VFSC may initiate.

90. While the new annual reporting requirements will, in due course, provide the VFSC with some knowledge of the NPOs' activities (once the process is fully in place), neither the VFSC nor the VFIU has yet been in a position either (a) to use its sources of information, in order to identify the features and types of NPOs which, by virtue of their activities or characteristics, are likely to be at risk of terrorist financing abuse; or (b) to identify the nature of threats posed by terrorist entities to the NPOs that are at risk, as well as how terrorist actors abuse those NPOs.

91. In principle, the key threats within the NPO sector in most jurisdictions can be characterised as:

- The raising of funds from the public under the pretence of being a charity, with or without registration;
- The abuse by NPO members or staff to divert funds to TF;
- Looting or diversion of NPO assets by terrorists in high-risk jurisdictions; and
- NPOs being subject to extortion by terrorists that exercise control in conflict zones.

92. Since there is no known domestic terrorism threat, the primary perceived risk to the registered NPO sector in Vanuatu would be (a) in relation to insider abuse within the organisation, or (b) with respect to the misuse of funds that are raised in Vanuatu for charitable purposes overseas. The VFSC has no evidence to suggest that any of the

registered NPOs do anything other than disburse charitable funds locally²⁷. Equally, there is no evidence to suggest that any type of NPO has been registered under offshore legislation. However, in the absence of a mandatory registration scheme for NPOs, there can be no certainty that unregistered charities are not engaged in channelling funds overseas. With respect to misrepresentation or insider abuse of individual NPOs, the authorities have no evidence that this has occurred, and have received no complaints from the public or from whistle-blowers.

93. The VFSC currently has no capacity to apply any form of meaningful oversight to the NPO sector, and the registration process under the AML/CFT law is not yet complete. Consequently it is recognised that there remains a material vulnerability within this sector until such time as the institutional risk assessments can be undertaken (based upon the new reporting requirements), and a targeted supervisory or monitoring process can be applied to those organisations (if any) that may be deemed to be at risk of TF abuse²⁸. Based upon the current understanding of the structure and composition of the NPO sector, there is little to suggest that the sector poses anything other than a low risk for terrorist financing.

Foreign Terrorist Fighters

94. Current global events necessitate consideration of the potential TF threat linked to the funding of foreign terrorist fighters (i.e. persons who travel to conflict zones in support of terrorist organisations). The most obvious risk at present relates to potential involvement in Islamic extremist causes. According to the national census, over 80% of the population of Vanuatu identifies itself as being Christian, with a further 6% Jewish. The balance comprises adherents to a range of different religions, including Bahais, Muslims and followers of the John Frum Movement. In principle, religious groups are required to register with the authorities, but this law is not enforced in practice.

95. In recent years, the Muslim population in Vanuatu has risen to about 1,000 following the establishment of an Islamic community in Mele Village. The population comprises mostly inward migrants and converts from among young Ni-Vanuatu who often feel marginalised in local society. The community funds students to undertake religious studies in Iran, Pakistan, Malaysia, Australia, New Zealand and Indonesia²⁹. There is no intelligence to suggest that residents of Vanuatu have been radicalised in the course of such studies, or that members of the Islamic community have travelled to conflict zones. However, immigration data indicates that a number of Islamic teachers have visited Vanuatu from known conflict zones. The awareness of, and attention to, terrorism and TF issues within the law enforcement agencies have been extremely limited in the past, and it is essential that the relevant skills and intelligence base be developed to ensure that any adverse developments are identified at an early stage.

²⁷ But note subsequent discussion of the Islamic community in Mele Village.

²⁸ In June 2016, the FATF standards in relation to NPOs were amended. They now require countries to identify which subset of NPOs falls within the FATF definition of a NPO, and then to identify the features and types of NPOs that, by virtue of their activities and characteristics, are likely to be at risk of terrorist financing abuse. In practice, this will require a detailed study of the NPO sector in Vanuatu to gain a clear understanding of what entities exist, what activities they undertake, and what type of governance structure is in place.

²⁹ Interview with Imam Mohammed Siddiq Sambo, quoted in Daily Post of 27 October, 2016.

Remittance Sector

96. There are five money remitters registered with the VFIU. Two are franchises of Western Union and another two are telecom companies using mobile technology. Anecdotal information³⁰ suggests that there may be a number of informal remitters who have not yet registered with the VFIU. Recently, the VFIU has extended its outreach to the remittance sector, and has not developed any evidence to suggest that there are any unregistered entities that may be providing a channel for illicit transfers.

97. Remitters are generally considered to present a high risk for the transfer of funds destined for terrorist organisations or individual terrorists because the sums involved in many aspects of TF are frequently small, there are no identification requirements below certain thresholds, and the usual absence of an on-going business relationship with the person remitting the fund means that it is difficult to develop a customer profile. In Vanuatu, there are no data available to the authorities on the destination of remittances made by registered institutions, other than in relation to large wire transfers³¹. Therefore, it is not known whether funds are being directed towards conflict zones or to neighbouring countries from where funds may be further transferred. The remitters provide the second largest number of STRs to the VFIU, but none has so far related to a suspicion of TF³².

Proliferation Financing

98. Until very recently, Vanuatu has not taken any steps to implement targeted financial sanctions in relation to proliferation financing (PF). The United Nations Financial Sanctions Act, enacted in June 2017, now provides a proper legal basis for meeting international obligations in this respect, although the relevant procedures have yet to be developed.

99. Vanuatu's greatest exposure to PF risk rests in (a) the misuse of international companies to mask ownership of businesses and assets; and (b) the registration on the Vanuatu shipping registry of vessels that may be used to transport weapons of mass destruction by designated entities. The general vulnerability to abuse of the international companies has been discussed previously in this assessment.

100. The Vanuatu shipping registry is managed under contract by a private sector company, Vanuatu Maritime Services Limited (VMSL), which maintains a central administration office in New York. The registry lists approximately 650 vessels of all types (bulk carriers, tankers, fishing vessels, cruise ships, etc.), but the predominant types of vessel are those working in support of the offshore oil industry. About 45% of the registered vessels are US-based and primarily involved in the offshore oil industry. A further 25% are Japanese-owned, involving bulk carriers, refrigerated carriers, etc. The register contains very few general cargo ships. VMSL has recently started to target potential business in Korea, but no such registrations have yet taken place.

101. Responsibility for complying with UN sanctions relating to proliferation financing rests with the administrative office of the VMSL in New York. It remains unclear the

³⁰ Referenced in the APG mutual evaluation report.

³¹ These frequently relate to transfers to Nigeria and Kenya.

³² The majority of the reports relate to transfers to countries considered as a high-risk source of fraudulent activity.

extent to which appropriate screening measures are being applied. The authorities recognise the importance of this matter and will work to ensure that full compliance is being achieved.

Part Three: Conclusions and Mitigation Strategy

Money Laundering through the Offshore Financial Centre

102. Based upon the data that are available, Vanuatu's offshore sector is very small compared with the scope and scale of the activities that have been developed in many other OFCs. Furthermore, the centre has been in decline for many years (with the exception of the licensing of securities dealers), and most stakeholders are of the opinion that this trend will continue in the foreseeable future. That said, the centre has been vulnerable to abuse in terms of ML and the commission of associated predicate offences, not least of all because it has been perceived (and often marketed) internationally as being a low-cost jurisdiction with relatively little regulation and a culture of secrecy. The Government is committed to pursuing the reforms that it has already adopted. The legal framework will be amended further in order to meet international standards; reform of the cultural tendency towards excessive secrecy relating to offshore activities will be completed; proper supervision will be extended to those OFC sectors that have previously remain substantially unregulated; and the government strategy towards the objectives and composition of the OFC will be developed.

103. Progress is being made in addressing many of these issues, but full implementation of the proposed reforms will take some time, and the degree of effectiveness of implementation will not be known in the near-term. In the meantime, the OFC remains vulnerable, not only from sophisticated criminal schemes, but also from very basic levels of tax evasion and fraud. However, there is little evidence to suggest that this is taking place on a significant scale, given the overall size and relative lack of development of the offshore sector, but the government is committed to addressing the current vulnerabilities, in conjunction with the international community.

Terrorist Financing

104. There is currently no evidence to suggest that Vanuatu is either a source of, or transit country for, funds destined to support terrorist activities. In addition, there is nothing to suggest that it might be the source of foreign fighters engaged in terrorist activities in conflict zones, who might be receiving financial and other material support from domestic sources. While the legal deficiencies have largely been addressed by the most recent amendments, the institutional arrangements in relation to combating terrorist financing require further strengthening, and many of the reforms required to counter money laundering through the OFC are also necessary to combat any threat of terrorist financing. It is also important that greater awareness of the issues (threats and prevention) relating to terrorist financing should be developed within both the public and private sectors.

Mitigation Strategy

105. The Vanuatu Government will, in due course, develop a full strategic plan to address the issues raised in this risk assessment. It will also continue to work with the private sector to help institutions to take account of the NRA findings within their own risk assessments. The strategic plan will seek to itemise the specific actions required by each department or agency (and within what timelines) to help counter the threats and address the vulnerabilities that have been identified. The plan will draw on the following high-level

objectives³³, several of which are already incorporated within the action plan that the Government agreed with the FATF in February 2016, in the context of the ICRG process.

³³ The objectives listed in the table are not necessarily in priority order. This will be a matter for Government and the authorities to decide based on resource and other considerations.

Strategic Mitigation Objectives	
1	Develop a clear strategy towards the future of offshore sector, drawing on the views of all relevant stakeholders.
2	Build the capacity of the regulatory bodies (RBV, VFSC and VFIU) to supervise and ensure compliance by the offshore financial sector (including relevant “gatekeepers”) with money laundering and terrorist financing preventive measures.
3	Ensure that the local agents of entities within the offshore sector are undertaking appropriate procedures for on-going customer due diligence (including understanding the nature of the customer’s business and its ownership and control structure), and are maintaining proper records that are accessible by the authorities.
4	Ensure that the suspicious activity reporting regime is extended, in practice, and properly enforced with respect to all relevant entities within the offshore sector.
5	Review the policy with respect to the large-scale licensing of securities dealers, with particular reference to the authorities’ understanding of the licensees’ business and the capacity to implement effective supervision of their activities.
6	Build the capacity within the law enforcement agencies (especially the Money Laundering Unit) to undertake proactive investigations of money laundering activity (and associated predicate offences) in the offshore sector.
7	Establish procedures and apply appropriate resources to ensure that requests for international cooperation are handled promptly, and that substantive information is provided wherever possible.
8	Establish appropriate mechanisms to collect, on a systematic basis, relevant data (both regulatory and law enforcement) that will assist in understanding the nature of the activities in the offshore sector and the criminal threats.
9	Undertake a detailed review of the NPO sector in order to establish the exact nature of the activities being undertaken, and to identify whether any entities might be subject to potential abuse for terrorist financing.
10	Institute proper procedures for implementing the international obligations with respect to targeted financial sanctions relating to both terrorist and proliferation financing.
11	Undertake a detailed review of the shipping registry in order to establish the exact nature of the activities being undertaken, and to identify whether it may be subject to potential abuse for proliferation financing.

Annex 1: List of stakeholders engaged in providing input to the NRA

National Coordinating Committee on AML and CFT

Ministry of Finance and Economic Management

State Law Office

Attorney General's Office

Department of Customs and Inland Revenue

Immigration Department

Citizenship Office

Office of the Public Prosecutor

Vanuatu Police Force

Reserve Bank of Vanuatu

Vanuatu Financial Services Commission

Vanuatu Financial Intelligence Unit

Vanuatu Bankers Association

Vanuatu Finance Centre Association

Vanuatu Maritime Services

Annex 2: List of Acronyms

AML/CFT	-	Anti-Money Laundering/Countering the Financing of Terrorism
APG	-	Asia Pacific Group on Money Laundering
CDD	-	Customer Due Diligence
CTSP	-	Company and Trust Service Provider
DCIR	-	Department of Customs and Inland Revenue
FATF	-	Financial Action Task Force
IC	-	International Company
ICRG	-	International Cooperation Review Group
ML	-	Money Laundering
MLA	-	Mutual Legal Assistance
MLU	-	Money Laundering Unit
MoU	-	Memorandum of Understanding
NCC	-	National Coordinating Committee
NPO	-	Non-Profit Organisation
NRA	-	National Risk Assessment
OCG	-	Organised Criminal Group
OFC	-	Offshore Financial Centre
OPP	-	Office of the Public Prosecutor
PF	-	Proliferation Financing
RBV	-	Reserve Bank of Vanuatu
RRG	-	Regional Review Group
SLO	-	State Law Office
STR	-	Suspicious Transaction Report
TCU	-	Transnational Crime Unit
TF	-	Terrorist Financing
UNSCR	-	United Nations Security Council Resolution
VFIU	-	Vanuatu Financial Intelligence Unit
VFCA	-	Vanuatu Financial Centre Association
VFSC	-	Vanuatu Financial Services Commission
VMSL	-	Vanuatu Maritime Services Limited