LIFE INSURANCE SECTOR MONEY LAUNDERING AND TERRORIST FINANCING

SUMMARY RISK ASSESSMENT

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Prudential Authority

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Executive summary

The Prudential Authority (PA) is responsible for the supervision of the life insurance sector insofar as compliance with the provisions of the Financial Intelligence Centre Act 38 of 2001, as amended (FIC Act) is concerned.

In furtherance of achieving its mandate, the PA conducted a money laundering and terrorist financing (ML/TF) risk assessment of the life insurance sector in January 2019 to assess and better understand ML/TF risks within the life insurance sector. The assessment was conducted taking into account Financial Action Task Force Recommendation 1, which requires that countries identify, assess and understand the ML/TF risks within their respective jurisdictions and take appropriate action, including designating an authority and/or a mechanism to coordinate actions to assess these risks and apply resources aimed at ensuring that such risks are mitigated effectively.

It is important to bear in mind, when taking into consideration the content of the sector risk assessment (SRA), that this is the first SRA of its kind for the life insurance sector conducted by the PA. At the time of compiling the assessment, the PA had conducted only eight inspections in the life insurance sector, and it is against this background that the content of the SRA must be understood. The inspections were conducted across a variety of life insurers, from long standing life insurers in the industry, to those which are relatively newer medium and smaller sized in terms of turnover.

In conducting the assessment, a survey-type questionnaire was distributed to all life insurers, and information was requested from the Financial Intelligence Centre (FIC) as well as the Association for Savings and Investment South Africa (ASISA). The data was analysed and interpreted to understand potential sectoral risk levels of ML/TF.

The threats that were identified to be most prevalent in the life insurance sector were predicate crimes, comprising insurance fraud and theft. The life insurance sector industry experts stated that fraud costs the life insurance industry billions of rands annually.

Key observations

Some of the key observations are as follows:

- The ML/TF risk rating of clients in the insurance industry is mostly based on product risk rather than different categories of ML/TF risk.
- The risk of receiving cash payments for insurance products is minimised or mitigated through the implementation of appropriate controls.
- Most life insurers do not operate in high-risk jurisdictions.
- Most life insurers stated that they do not have persons from high-risk jurisdictions as their clients.
- The volumes of intelligence and regulatory reports filed by life insurers with the FIC are low and further scrutiny from the regulators is needed to ensure that reporters duly meet their obligations under the FIC Act.

Based on information received, the following are some of the industries that the insurers have exposure to:

	Number of insurers per industry	Percentage of exposure to industries
Charities and/or non-profit organisations	16	29%
Intermediaries/commission agents	23	41%
Real estate agents	14	25%
Agriculture and/or forestry	16	29%
Arms dealers	8	14%
Atomic power	8	14%
Casinos, including Internet gambling	10	18%
Digital/virtual currency providers	6	11%
Gas sector	14	25%
Health care and pharmaceutical	15	27%
High-value goods dealers	10	18%
Information and communication	16	29%
Manufacturing of dual-purpose goods	9	16%
Mining and quarrying	18	32%
Precious metals and stone dealers	10	18%
Private military firms	6	11%
Shipping	11	20%
Transport	18	32%
Utilities	15	27%

Vulnerabilities mentioned

The following vulnerabilities were identified:

- Some of the life insurers' on-boarding processes enabled clients to be on-boarded prior to the client being subjected to screening against prescribed sanctions lists.
- Some of the life insurers were still monitoring client transaction behaviour using manual interventions, therefore sophisticated automated transaction monitoring systems had not been deployed. Inadequate suspicious or unusual transaction or activity monitoring practices could lead to suspicious or unusual transactions going undetected for regulatory reporting purposes.
- Some life insurers placed reliance on intermediaries for purposes of identifying and verifying clients. This should be closely monitored by life insurers, and regular checks and monitoring should be conducted to ensure that assurance is achieved regarding the reliance placed on intermediaries that conduct customer due diligence on such persons, as this has been identified as a major vulnerability in the insurance sector.

The outcome of the SRA identified the following deficiencies:

- In some cases, life insurers had implemented inadequate processes to identify reportable cash transactions in terms of the FIC Act.

- Some management information system(s) that had been deployed to deliver timely information for detecting patterns of unusual or suspicious activity, particularly in relation to higher-risk accounts, we inadequate.

- Some staff members responsible for reviewing customer transactions did not have a good understanding of what was considered normal and reasonable activity for particular types of customers, taking into account the nature of a customer base within a life insurer.

- To a lesser extent, in some cases insurers were not conducting enhanced due diligence reviews before processing a transaction if there were circumstances that gave rise to a suspicion.

- In some cases, system rules deployed in automated transaction monitoring systems were inadequate based on the national and international experience on the methods and the prevention of ML/TF.

Risk events observed

- Failure to keep complete records of customer due diligence information

- Receipt of clients' funds prior to conducting customer due diligence

- External fraud

- Failure to provide training

- Reporting of suspicious transactions after the prescribed period

- Reporting of cash threshold amounts after the prescribed period

- Inability of some screening systems to detect some politically exposed persons' names

Rating

From the results of the 2019 ML/TF risk assessment survey and information gathered from the life insurance sector, the inherent ML/TF risk rating for the life insurance sector was considered to be low. However, the deficiencies highlighted above made the sector vulnerable to money laundering and created the ability for abuse of the sector by persons listed on United Nations Security Council Sanctions lists. In the absence of adequate mitigating controls to address the deficiencies identified, the overall ML/TF risk rating is that of medium.

SRAs are conducted by the PA every second year. The next SRA will be undertaken in 2021.