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# The Legal 500 Country Comparative Guides

## Isle Of Man

# **BANKING & FINANCE**

### Contributing firm

Cains

The Cains logo consists of a white square with the word "CAINS" in black, uppercase, sans-serif font centered within it.

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This country-specific Q&A provides an overview of banking & finance laws and regulations applicable in Isle of Man.

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## ISLE OF MAN BANKING & FINANCE



### 1. What are the national authorities for banking regulation, supervision and resolution in your jurisdiction?

All banks in the Isle of Man are subject to a licensing and supervision regime administered by the Financial Services Authority (“**FSA**”). The FSA is an independent statutory body whose functions include the licensing, supervision and regulation of deposit takers, insurance companies, money transmission services and credit unions.

The Isle of Man Office of Fair Trading (“**OFT**”) has a role in the registration and regulation of moneylenders.

### 2. Which type of activities trigger the requirement of a banking licence?

Absent a relevant exemption or exclusion, deposit taking by way of business in or from the Isle of Man is a regulated activity which requires a Class 1 licence. “Deposit taking” means: (i) accepting deposits of money from any persons and where such money is lent to others, or any other activity of the person accepting the deposit is financed out of the capital of or interest received on the deposited monies; or (ii) operating a representative office of a foreign bank.

For completeness, the provision of loans in the Isle of Man may require registration with the OFT unless such activity falls outside the scope of the Money Lenders Act 1991 (such as where lending is by a body corporate (wherever incorporated) to another body corporate (wherever incorporated) or to any other person apart from a sole trader).

### 3. Does your regulatory regime know different licenses for different banking services?

There are three sub-categories under a Class 1 licence:

- i. Class 1(1) retail/non-restricted deposit taking

- business;
- ii. Class 1(2) restricted deposit taking business (under which banks may not accept deposits from retail customers and such deposits are not covered by the DCS (see response to question 23 below);
- iii. Class 1(3) representative office of a foreign bank (under which representative offices may only undertake marketing and business development activities; the foreign bank must not undertake any transactions in or from the Isle of Man).

Additional classes of licence apply to other regulated activities such as investment business and money transmission services (including the issuance of electronic money).

### 4. Does a banking licence automatically permit certain other activities, e.g., broker dealer activities, payment services, issuance of e-money?

Separate licences will need to be obtained depending on the type/nature of regulated activity intended to be undertaken.

### 5. Is there a “sandbox” or “license light” for specific activities?

No. However, a Class 1(3) licence permits banks (on a restricted basis) to establish a place of business in the Isle of Man to “test the waters” (though such entities are unable to accept deposits other than from their head office outside the Isle of Man).

### 6. Are there specific restrictions with respect to the issuance or custody of crypto currencies, such as a regulatory or voluntary moratorium?

Currently no specific legislation exists with respect to the issuance or custody of cryptocurrencies in the Isle of Man. The FSA has issued some guidance in respect of its licensing attitude to token/crypto asset activity and regulation, which can be found at the following link: <https://www.iomfsa.im/media/2717/regulatory-perimeter-faqs.pdf>. Any entity issuing or providing custody of crypto currencies in or from the Isle of Man or running a token exchange for cryptocurrencies (e.g. Bitcoin) should register with the FSA under The Designated Businesses (Registration and Oversight) Act 2015 (as amended June 2019), and additionally shall be required to have at least two Isle of Man resident directors and be managed and controlled from the Isle of Man. However running an exchange for tokenised securities (as described in the FSA's guidance note at the following link: <https://www.iomfsa.im/media/2720/regulatory-perimeter-for-tokens.pdf>) would require such an exchange to be operated as a crowd funding platform and the operators of the same are required to be appropriately licensed by the FSA.

Guidance to consumers concerning cryptocurrencies can be found on the FSA's website at: <https://www.iomfsa.im/fsa-news/2020/oct/consumer-awareness-cryptocurrencies/>.

### **7. Do crypto assets qualify as deposits and, if so, are they covered by deposit insurance and/or segregation of funds?**

Crypto assets do not qualify as "deposits" for the purposes of the Regulation Activities Order 2011 (as amended).

### **8. What is the general application process for bank licenses and what is the average timing?**

A Class 1 deposit taking licence is issued to banks with a full presence on the Isle of Man, and to subsidiary companies or branches of banks licensed in other jurisdictions applying equivalent regulatory standards to those on the Isle of Man. In the case of branches of banks licensed elsewhere, a deposit taking licence is only granted when the regulator of the head office of the bank agrees to exercise consolidated supervision with the FSA, which includes consideration of capital adequacy.

Any entity looking to undertake a regulated activity should contact the FSA to arrange a meeting as soon as possible in advance of the desired date for commencing business. Following which, a thorough evaluation will be

undertaken by the FSA to ensure various criteria (such as integrity, competence and solvency) are met.

To apply for a licence, the relevant sections of the application form (which may be found on the FSA's website) together with a full suite of supporting documents (which includes a business plan) must be completed and submitted to the FSA. A non-refundable fee is also payable upon a licence application.

The FSA's current published service standard for processing an application, from receipt of a *complete* application to an issuance of its decision, is approximately six months. An application may take considerably longer than six months to process if it is incomplete or if there are issues in relation to the applicant or any of its key persons which may require further investigation.

### **9. Is mere cross-border activity permissible? If yes, what are the requirements?**

Where a regulated activity is not carried out *in or from* the Isle of Man (i.e. on a pure cross-border basis), there will not be any requirement to hold a licence. Although there is some statutory guidance as to what "in or from" the Isle of Man means for the purposes of the Financial Services Act 2008 (as amended) (the "**Act**"), this is largely a question of fact and must be based on the circumstances upon which the regulated activity is conducted in connection with the Isle of Man.

### **10. What legal entities can operate as banks? What legal forms are generally used to operate as banks?**

The banking sector in the Isle of Man is dominated by branches and subsidiaries of the main UK clearing banks. Many other UK and foreign banks are also established on the Isle of Man, together with branches and subsidiaries of major UK building societies. As such, banks tend to take the form of limited companies, with larger banks typically being public limited companies and smaller ones being both public companies and private companies.

### **11. What are the organizational requirements for banks, including with respect to corporate governance?**

The FSA has issued a guidance note relating to the corporate governance of licensed deposit takers on the

Isle of Man, within which the FSA has emphasized the need for sound corporate governance for the protection of investors and the security of business, risk management, and the adherence of directors to the duties and responsibilities of directors under the laws of the Isle of Man. A copy of this guidance note may be found on the FSA's website (iomfsa.im).

The Financial Services Rule Book 2016 (as amended 2019) (the "**Rule Book**"), which applies to certain licenceholder (eg. other than Class 1(3) licenceholders), further contains rules relating to corporate governance, such as ensuring that regulated activities are managed and controlled from the Isle of Man.

## 12. Do any restrictions on remuneration policies apply?

There are no specific restrictions on remuneration though the Rule Book sets out a remuneration policy which requires a licenceholder to establish an effective remuneration policy that, amongst other things, addresses the risk of inappropriate remuneration and contains measures for the proper management of incentive schemes.

## 13. Has your jurisdiction implemented the Basel III framework with respect to regulatory capital? Are there any major deviations, e.g., with respect to certain categories of banks?

The Isle of Man has taken a flexible approach to rolling out key elements of Basel III and specific implementation proposals have been and continue to be, subject to local consultation. The first phase of implementation (effective 1 July 2017) saw amendments being made to the Rule Book to set out new capital adequacy rules which apply to all Isle of Man incorporated entities holding either a Class 1(1) or Class 1(2) licence. Under the Rule Book, such a Class 1 licenceholder must from 1 July 2017, inter alia:

- i. establish and maintain an internal capital adequacy assessment process ("**ICAAP**") appropriate to the nature and scale of its business;
- ii. ensure that its capital requirements does not fall below the prescribed minimum (being a CET1 ratio of 85%, Tier 1 ratio of 8.5% or Total capital ratio of 10% (or such other ratio as prescribed by the FSA)); and
- iii. immediately notify the FSA if at any time it has reason to believe that its CET1 ratio, Tier

1 ratio or Total capital ratio is below the minimum capital requirements set out in (ii) above, or is within 1% of the minimum capital requirement (for Total capital ratio only).

The FSA has a duty to review a bank's ICAAP and each bank must be able to explain its ICAAP to the FSA.

## 14. Are there any requirements with respect to the leverage ratio?

Currently no decision has been made with respect to the implementation of a leverage ratio requirement though pursuant to a discussion paper produced by the regulators of the British Crown Dependencies (including the Isle of Man) (the "**Tri-Party Group**") on Basel III Leverage Ratio (the "**Basel III Paper**"), it was proposed that only locally incorporated banks should be included within the scope of any proposed leverage ratio reporting requirement.

Under the Basel III Paper, it was proposed that the leverage ratio is defined as the Capital Measure (the numerator) divided by the Exposure Measure (the denominator), with this ratio expressed as a percentage. It was also proposed that the Capital Measure for the leverage ratio is Tier 1 capital as defined in section 5 of the Tri-Party Group Discussion Paper on Basel III: Capital Adequacy issued in December 2013, and the Exposure Measure for the leverage ratio should generally follow the accounting measure of assets subject to certain principles.

## 15. What liquidity requirements apply? Has your jurisdiction implemented the Basel III liquidity requirements, including regarding LCR and NSFR?

The FSA has not yet implemented the Basel III liquidity framework though understand consultations on the same are to be undertaken during the course of 2020. The FSA's proposals with regards the implementation of Basel III in the Isle of Man are intended to establish a robust liquidity standard, whilst recognising international best practice. Whilst in some areas they diverge from Basel III, this reflects local circumstances, including the fact that almost all banks in the Isle of Man (and across the Crown Dependencies) are part of wider groups that manage liquidity on a consolidated basis.

It is considered that commencing the reporting of NSFR data and an NSFR ratio would be beneficial as, amongst other things, the data would be useful in itself, providing a snapshot of the balance of longer term funding vs

longer term lending, and the data will enable the evaluation of the benefits of the NSFR and whether any changes should be made to it to reflect local circumstances. Based on feedback received to the Discussion Paper "Basel III: Liquidity" (the "**Liquidity DP**"), no respondents raised objections to the proposal to require NSFR reporting and this will be developed in due course alongside LCR reporting.

The FSA notes in the Liquidity DP that the Basel III LCR standard is similar to the approaches already prescribed locally in that it requires predicted outflows to be met by a mixture of predicted inflows and High Quality Liquid Assets ("**HQLA**"), and predicted flows are based on a mixture of contractual and behaviourally based projections. The main differences are:

- i. the definition of HQLA in the Basel III LCR standard is different to the types of marketable assets used in the Crown Dependencies; generally, the definition in Basel III is tighter;
- ii. the LCR limits the extent to which inflows may offset outflows and obviate the need to hold HQLA; HQLA must exceed 25% of adjusted outflows in all cases;
- iii. the allowance for depositor behaviour is different: the FSA allows percentages that vary across banks, based on individual submissions; and
- iv. the FSA applies in addition, a one-week metric.

The Tri-Party Group is of the view that significant adverse impacts, if the LCR were implemented unaltered, would perhaps most likely arise from: (1) the treatment of fiduciary deposits; (2) more limited recognition of inflows; and (3) the tighter definition of liquid assets.

The Liquidity DP, together with feedback on the same, may be viewed on the FSA's website ([iomfsa.im](http://iomfsa.im)).

### **16. Do banks have to publish their financial statements? Is there interim reporting and, if so, in which intervals?**

All Class 1 licenceholders incorporated in the Isle of Man are required to make their audited financial statements available for public inspection within 4 months of its annual reporting date. The contents of such a Class 1 licenceholder's annual financial return must comply with the requirements under the Rule Book.

A relevant Class 1 licenceholder must also display a notice in its registered office (and all other offices in the

Island) stating that (i) a copy of its latest audited Statement of Financial Position together with the last auditor's report (as it appears in the audited financial statements) may be inspected by any person on demand; and (ii) copied are available to be taken away. Such a Class 1 licenceholder's annual financial statements must also be available for public inspection on its website.

The requirement to comply with interim reporting will apply to public companies (which are subject to relevant disclosure rules of a stock exchange). No Isle of Man interim reporting requirements are currently present though the Rule Book requires all relevant Class 1 licenceholders to prepare deposit taking returns as at each quarter end.

### **17. Does consolidated supervision of a bank exist in your jurisdiction? If so, what are the consequences?**

When licensing a foreign subsidiary or branch, the FSA requires prior approval by the home regulator and will not grant a license to a branch unless it is satisfied that the regulator of the home country is prepared to exercise consolidated supervision over the Isle of Man branch. As almost all the licensed banking activities in the Isle of Man are foreign owned, cooperation with the supervisory authority of the home country is of essential importance to the FSA.

The FSA believes that appropriate international cooperation between regulators is fundamental to the integrity of the international financial system and is committed to meeting its international obligations. The FSA is able to provide assistance to overseas authorities in relation to the regulation and supervision of licensed financial services businesses. This power is of particular importance in the global financial services market place to ensure consolidated supervision of regulated groups. Examples include:

- i. obtaining information from, and providing information to, overseas authorities in respect of new applications for licensing and/or approval in the overseas jurisdiction, or in respect of applications on behalf of principal persons (beneficial owners and senior management of financial institutions);
- ii. Obtaining and providing information where it is suspected that a person is conducting financial business in an overseas jurisdiction without a licence; and
- iii. assisting overseas authorities to undertake onsite examinations of branches of overseas

companies based in the Isle of Man.

Consequently one of the main consequences of such consolidated supervision of a bank is that, where an overseas securities regulator has entered into a mutual assistance agreement with the FSA, the FSA is empowered to exercise powers on their behalf to assist in the exercise of their functions. Thus, the FSA can exercise its powers of inspection and investigation, including the power to obtain written and oral explanations and to require the production of documents, on behalf of that regulator. The FSA may also communicate to that regulator information which is in its possession, whether or not as a result of the exercise of any of its powers, subject to certain legal safeguards and conditions.

### 18. What reporting and/or approval requirements apply to the acquisition of shareholdings in, or control of, banks?

A Class 1 licenceholder incorporated in the Isle of Man must obtain the FSA's prior consent before:

- i. any person acquires a controlling interest in it; or
- ii. any changes take place to an existing controlling interest in it, which would take that controlling interest from either: (a) 50% or less to over 50%; or (b) 75% or less to over 75%.

For these purposes a "controlling interest" is interpreted by reference to the definition of "controller" in the Act (ie. A person who alone or with others can exercise 15% or more of the voting rights at any general meeting of the licenceholder or another body corporate of which it is a subsidiary).

### 19. Does your regulatory regime impose conditions for eligible owners of banks (e.g., with respect to major participations)?

All persons with responsibility for the management and control of the business and key persons holding Controlled Functions must satisfy the FSA that they are "fit and proper". Guidance as to what would be considered to be "fit and proper" are found on the FSA's website and includes such factors as whether an individual's holding of a particular role or interest would expose the bank to undue risk.

The concept of fitness and propriety appears in a number of pieces of regulatory legislation, and the overarching interpretation of the term includes the

consideration of an individual's integrity, financial standing and their competence and capacity.

### 20. Are there specific restrictions on foreign shareholdings in banks?

There are no specific restrictions on foreign shareholdings in banks.

### 21. Is there a special regime for domestic and/or globally systemically important banks?

The Isle of Man's framework for dealing with domestic systematically important banks ("D-SIBs") is drawn from the Basel Committee's framework (the "D-SIB Framework"). The FSA's assessment is based on the following four factors, with appropriate weightings: (i) size; (ii) interconnectedness; (iii) substitutability/jurisdiction's financial institution infrastructure; and (iv) complexity.

A two-stage approach is used to assess and then identify D-SIBs. The first, involves assessing the quantitative factors of size and substitutability, using an indicator-based approach and the second qualitative stage, involves judgement and therefore is naturally more subjective.

The D-SIB identification methodology applies both to branches of overseas banks as well as banks incorporated in the Isle of Man.

The FSA will notify individual banks of their designation as a D-SIB and provide details of the analysis which has led to that designation. The FSA plans to introduce a more graduated impact assessment for the banking sector, with D-SIBs considered the highest impact firms. This will lead to the FSA fine tuning and tailoring its strategy for supervising banks generally, and, for individual D-SIBs will include:

- i. more in depth assessments of D-SIBs (such as more frequent on-site assessments, and / or dialogue and engagement on specific areas of risk or importance, for example through more formal regular meetings);
- ii. an increased focus on the risk management, governance structures, and risk profiles, including more frequent engagement with boards (for Isle of Man incorporated D-SIBs), senior management, and receipt of risk and audit reports; and
- iii. a deep and thorough understanding of the recovery planning, resolution planning and

resolution strategy for the D-SIB, both at a local and a group level.

## 22. What are the sanctions the regulator(s) can order in the case of a violation of banking regulations?

Depending on the nature of the breach, sanctions range from reprimands to fines (including discretionary civil penalties) to suspension or loss of licence. There are also criminal sanctions for certain violations (e.g. where a regulated activity is being carried on by a person who is not permitted to do so).

## 23. What is the resolution regime for banks?

Following a public consultation undertaken by the Isle of Man Treasury (the “**Treasury**”) in 2020 regarding the Bank (Recovery and Resolution) Bill 2020 (the “**BRR Bill**”), the BRR Bill has been considered by Tynwald and the Bank (Recovery and Resolution) Act 2020 (the “**BRR Act**”) came fully into force on 4 January 2021. Since such date, the FSA has been the resolution authority for the Isle of Man for the purposes of the BRR Act.

The BRR Act is similar in scope and content to legislation enacted in the European Union (i.e. the EU’s Bank Recovery and Resolution Directive 2014/59/EU) and the UK (i.e. the Banking Act 2009). It provides the FSA (as resolution authority) with new powers to deal with banks which are “failing or likely to fail” (e.g. see our response to question 24 below, regarding the bail-in tool included within the BRR Act). Such powers are intended to minimize the impact of a bank failure on the real economy and the public finances.

Pursuant to part 5 of the BRR act, a Bank Resolution Fund (the “**Fund**”) will be established to fund the work of the FSA acting in its capacity as the Island’s resolution authority. Funding for the Fund will partly come from levying contributions on banks and partly from the Treasury. The FSA (as resolution authority) is also permitted to borrow and to take out insurance for the purposes of the BRR Act. The maximum amount which can be paid out of the Fund is £60 million and the FSA (as resolution authority) must seek to recover from the bank in resolution any funds paid out and may, if there is any negative balance left to the Fund following recovery of as much as possible from the bank in resolution, recover such balance from other banks over a period of 10 years.

Part 11 of the BRR Act provides a framework for the FSA to recognize and assist foreign resolution actions (e.g. by

the Bank of England as the resolution authority for the UK), although the FSA (as resolution authority) is required to consult with the Treasury prior to making a “recognition order”. The FSA may make such an order in respect of a bank which is an Isle of Man subsidiary of a foreign bank.

Part 13 of the BRR Act sets out a dedicated winding-up procedure for banks in the Isle of Man which are incapable of being resolved. Consequently, since the BRR Act came into force it is no longer possible to wind-up a bank in the Island using our normal corporate winding-up legislation. An application for a bank winding-up order under the BRR Act may be made by the FSA (as resolution authority), the Treasury, the bank or any shareholder or creditor of the Bank. The Isle of Man Court is required to consult the FSA (as resolution authority) before making a decision on such an application and to give “due consideration” to the FSA’s views.

## 24. How are client’s assets and cash deposits protected?

The FSA requires banks to have contingency arrangements in place to cope with increased depositor withdrawals and may also require enhanced reserves when more difficult conditions arise. In the case of a branch, the FSA normally relies upon the overseas regulator in the country where the bank has its head office to undertake supervision of the bank’s financial strength. In such cases, to gauge the safety of placing funds with the Isle of Man branch, depositors are well advised to review information available about the ‘head office’ and the company. In the case of banks that are incorporated in the Isle of Man (i.e. they are Isle of Man companies) the Isle of Man’s regulatory regime has established requirements designed to protect a bank’s viability. The international standard, Basel II, was adopted in the Isle of Man in line with all main European and other jurisdictions in January 2008. In addition to applying standard minimum capital requirements for a range of risks, Basel II facilitates the specific analysis of each bank’s full risk profile and enables their capital requirements to be increased to reflect these. The FSA is currently considering the implementation of Basel III in the Isle of Man which is the revised international standard in relation to capital and liquidity.

Although there is no ultimate safeguard, the FSA considers the following factors relevant to the protection of client’s assets and cash deposits:

- i. the quality of banks operating in the Isle of Man;

- ii. the regulatory requirements and supervisory oversight applied by the FSA to banks in the Isle of Man (such as, stringent requirements under the Rule Book which apply to licenceholders holding client assets); and
- iii. the availability of a depositor compensation scheme (“**DCS**”), which ensures that personal depositors are covered for up to £50,000 of their savings with any Class 1(1) deposit taker. Most other categories of depositor (companies, trusts etc) are covered up to a maximum of £20,000 but only for deposits with Class 1(1) licenceholders.

## 25. Does your jurisdiction know a bail-in tool in bank resolution and which liabilities are covered?

The BRR Act has introduced the bail-in tool and sets out the purposes for which it may be applied by the FSA (as resolution authority). Part 8 of the BRR Act sets out the entire gamut of Resolution Tools, including the bail-in tool. Such tool allows the FSA (as resolution authority) to write-down, or cancel entirely, part or all of the liabilities owed by a bank and/or potentially convert them into equity, all with the aim of restoring it to financial soundness and long-term viability. However, certain liabilities are excluded from the scope of the FSA's write-down or conversion powers: including covered deposits, secured liabilities, liabilities of the Bank acting as fiduciary, salaries owed to employees of the bank and liabilities in respect of the DCS (as defined in question 24 above).

## 26. Is there a requirement for banks to hold gone concern capital (“TLAC”)?

There are currently no requirements for Isle of Man incorporated banks to hold gone concern capital. However, non-Isle of Man incorporated banks will tend to follow the regulations of its head office and the relevant regulations applicable to its head office as to capital requirements.

## 27. In your view, what are the recent trends in bank regulation in your jurisdiction?

In the wake of the global financial crisis of 2008, international governments have been working to ensure that the cost burden of any future bank failure is for the account of its shareholders and creditors, and not for the taxpayers. One learning from the financial crisis was the

need for banks themselves to develop detailed resolution plans (sometimes referred to as living wills) as to how they would seek to recover from a stress event, or events, serious enough to threaten the viability of the bank. The FSA requires banks incorporated in the Isle of Man to prepare recovery plans and to keep them up to date as detailed in the FSA's Guidance Notes for Deposit Takers entitled “Recovery Planning” published in January 2021. The BRR Act (as defined in question 22 above) is the Isle of Man's response and adaptation of the “Key Attributes of Effective Resolution Regimes for Financial Institutions”, published by the Financial Stability Board, a body created by the G20 Governments in response to the financial crisis.

There has also been a wave of recent reforms on the Island following MONEYVAL's assessment in 2016 and published mutual evaluation report in December 2016 (“**MER**”). The MER demonstrated that, whilst the Isle of Man had a strong technical framework, more work needed to be carried out to make it effective in practice. In particular there were a number of important recommendations made concerning financial intelligence, financial investigation and prosecution and recovering the proceeds of crime. The Isle of Man government, regulatory and law enforcement authorities have undertaken a considerable amount of work to address the issues identified in the MER. This includes significant investment in the Financial Crime Unit, the Economic Crime Unit (which conducts investigations) and the introduction of a dedicated Asset Recovery Unit, specifically to identify restraint and confiscate the proceeds of crime. The Isle of Man continues to report back to MONEYVAL on an annual basis to confirm the improvements that have been delivered in relation to the recommendations made within the MER.

## 28. What do you believe to be the biggest threat to the success of the financial sector in your jurisdiction?

The Isle of Man has a long standing and deserved reputation for its prudent fiscal policies. In September 2021 the Isle of Man government issued £400 million of sustainable bonds with a coupon of 1.625% which were given a credit rating of Aa3 from Moody's. Despite the recent economic challenges as a result of the ongoing COVID-19 pandemic and the UK exit from the EU, the annual GDP of the Isle of Man continues to grow.

However, as set out in the Isle of Man Government's second National Risk Assessment of Money Laundering and the Financing of Terrorism (“**NRA**”), the relevant authorities and professional service providers in the Island, in keeping with those in all other responsible

international financial centres, must remain vigilante of the risks posed by such activities. The NRA sets out,

among other things, certain sectoral risk ratings (for ML and TF Risk) with “Banking” rated as Medium risk and “Convertible Virtual Currencies” as Medium High risk.

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