



FINANCIAL INTELLIGENCE ANALYSIS UNIT

# **GUIDANCE NOTE**

**ON**

## **HIGH-RISK AND NON-COOPERATIVE JURISDICTIONS**

*A GUIDANCE NOTE ISSUED BY THE FIAU ON THE APPLICATION OF CERTAIN OBLIGATIONS UNDER THE PREVENTION OF MONEY LAUNDERING AND FUNDING OF TERRORISM REGULATIONS WITHIN THE CONTEXT OF THE PUBLIC DOCUMENTS ISSUED BY THE FINANCIAL ACTION TASK FORCE ON HIGH-RISK AND NON-COOPERATIVE JURISDICTIONS*

**Issued: 4<sup>th</sup> April 2012**

1. A number of obligations under the Prevention of Money Laundering and Funding of Terrorism Regulations (“PMLFTR”) require subject persons to assess the level of money laundering/funding of terrorism (“ML/FT”) risk emanating from a particular jurisdiction and to determine whether a jurisdiction meets the criteria of a ‘reputable jurisdiction’ as defined under Regulation 2 of the PMLFTR. This guidance note is intended to assist subject persons in the application of these obligations in the light of the Financial Action Task Force (FATF) public documents on high-risk and non-cooperative jurisdictions.

### **The FATF Public Documents**

2. The FATF issues two public documents which provide a list of jurisdictions that are considered to pose a higher risk of ML/FT in view of a number of identified strategic deficiencies within their anti-money laundering/combating the financing of terrorism (“AML/CFT”) regime. The ML/FT risks posed by the jurisdictions listed in the FATF documents vary depending on the seriousness of the deficiencies and the level of commitment made by each jurisdiction to address those deficiencies. It is to be noted that the FATF documents are issued three times a year and as a result the list changes depending on the level of progress achieved by each jurisdiction in addressing the deficiencies identified in their respect.<sup>1</sup>
3. The first public document issued by the FATF is the **Public Statement** which classifies jurisdictions into the following two categories:
  - (a) jurisdictions subject to a FATF call on its members and other jurisdictions to apply counter-measures to protect the international financial system from the on-going and substantial ML/FT risks emanating from the jurisdictions;
  - (b) jurisdictions with strategic AML/CFT deficiencies that have not made sufficient progress in addressing the deficiencies or have not committed to an action plan developed with the FATF to address the deficiencies and are subject to a FATF call on its members to consider the risks arising from the deficiencies associated with each jurisdiction.
4. The FATF also issues a second document entitled “**Improving Global AML/CFT Compliance: On-going Process**” (“On-going Process document”). This document contains a list of jurisdictions that have been identified by the FATF as having strategic AML/CFT deficiencies but that have provided a high-level political commitment to address the deficiencies through implementation of an action plan developed in conjunction with the FATF. The situation differs in each jurisdiction and therefore every country on the list presents different degrees of ML/FT risks.
5. Three different categories of higher-risk jurisdictions are therefore identified in the FATF public documents:

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<sup>1</sup> For the latest list please refer to the website of the FIAU under the section ‘Statements’ ([www.fiumalta.org/Statements](http://www.fiumalta.org/Statements)).

<b>Category 1</b>	Jurisdictions that have strategic AML/CFT deficiencies and to which counter-measures apply
<b>Category 2</b>	Jurisdictions with strategic AML/CFT deficiencies that have not made sufficient progress in addressing the deficiencies or have not committed to an action plan developed with the FATF to address the deficiencies
<b>Category 3</b>	Jurisdictions with strategic AML/CFT deficiencies that have developed an action plan with the FATF and have made a high-level political commitment to address their AML/CFT deficiencies

### **Assessing and managing the ML/FT risk posed by a higher-risk jurisdiction**

6. Regulation 4(1) requires subject persons to have in place procedures to manage the ML/FT risks posed by their customers, products and services. This obligation requires the development and establishment of effective customer acceptance policies in terms of Regulation 7(9). These procedures are mandatorily required in order for subject persons to be able to determine, *inter alia*, whether an applicant for business or a beneficial owner is likely to pose a higher risk of ML/FT. Among other things, a customer acceptance policy should include the identification of risks posed by a business relationship or a transaction to be established or carried out with a natural or legal person from a particular jurisdiction which is considered to pose a higher risk of ML/FT.
7. Section 4.1.1.2 (iv) of the FIAU's Implementing Procedure, citing the FATF Risk-Based Approach Guidance, lists a number of factors that should be assessed in determining whether a jurisdiction poses a higher risk of ML/FT. This includes the situation where a jurisdiction is identified by credible sources as lacking appropriate AML/CFT laws, regulations and other measures. Therefore, all the jurisdictions falling within Categories 1, 2 and 3 (refer to paragraph 5 above) are to be considered as posing varying degrees of higher risk of ML/FT and subject persons are required to include the risks posed by such jurisdictions within their customer acceptance policy.
8. Where, on the basis of the subject person's customer acceptance policy, it is determined that a business relationship or a transaction is connected to a jurisdiction falling within Categories 1, 2 and 3, Regulation 7(9)(c) requires subject persons to conduct enhanced customer due diligence ("ECDD") in accordance with Regulation 11(1).<sup>2</sup> A connection to a jurisdiction falling within Categories 1, 2 and 3 may take various forms. For instance, a business relationship or a transaction shall be considered to be connected to a higher-risk jurisdiction falling within Categories 1, 2 and 3 if the applicant for business,<sup>3</sup> the beneficial owner, the source of funds/wealth or the business/economic activity is situated in or originates from such a jurisdiction and shall therefore be subject to ECDD. However, not every form of connection to a higher-risk jurisdiction shall give rise to the requirement to apply

<sup>2</sup> It should be noted that the PMLFTR do not prohibit the establishment of a business relationship or the carrying out of a transaction with a person from a higher-risk jurisdiction but requires subject persons to apply enhanced due diligence measures.

<sup>3</sup> Whether such an application for business is a natural or legal person, including a financial institution as defined under the FATF Recommendations.

ECDD. For instance, where a business relationship or a transaction involves an applicant for business who is a citizen of a higher-risk jurisdiction but does not reside in such jurisdiction and the business/economic activity and/or the source of wealth/funds involved are not in any way connected to such a higher-risk jurisdiction, the requirement to apply ECDD does not arise.

9. Since Regulation 11(1) does not provide for any specific ECDD measures that must mandatorily be applied in situations which present a higher risk of ML/FT, subject persons are required to use their discretion in relation to business relationships or transactions connected to the jurisdictions falling within Categories 1, 2 and 3. However, the measures adopted must be applied on a risk-sensitive basis and be effective and proportionate to counter the ML/FT risk posed by each such jurisdictions.
10. Therefore, the enhanced due diligence measures to be applied in relation to a business relationship or a transaction connected to a jurisdiction falling within Category 1 should be more stringent than those applied in relation to a business relationship or a transaction connected to a jurisdiction falling within Category 2, since the ML/FT risks posed by the former category are considered to be higher. With respect to business relationships or transactions connected to a jurisdiction falling within Category 3, subject persons are required to assess the particular risk posed by the specific deficiencies identified by the FATF to determine which particular measures are effective and proportionate to counter that specific risk.
11. In order to assist subject persons in determining which enhanced due diligence measures should be applied, reference may be made to Section 4.1.2 of the FIAU's Implementing Procedures which provides for the procedures to be applied to control and mitigate higher-risk situations. Such procedures include the following:
  - (a) the implementation of a programme which sets out the additional measures to be applied by the subject person in relation to the jurisdictions listed in the FATF public documents, such as for instance requiring additional information and documentation to be supplied by the customer than would normally be required;
  - (b) requiring a higher standard in relation to the quality of documents obtained;
  - (c) monitoring transactions/activities to a higher degree.
12. In relation to paragraph (c) above, it should be noted that Regulation 15(2) specifically requires subject persons to pay special attention to business relationships and transactions with persons, companies and undertakings, including those carrying out relevant financial business or a relevant activity, from a non-reputable jurisdiction (refer to paragraph 13 below), and, whenever the transactions involved have no apparent economic or visible lawful purpose, the background and purpose of such transactions should, as far as possible, be examined. In such cases, written findings should be made available to the FIAU and the relevant supervisory authority.<sup>4</sup> Therefore, subject persons are required to pay special attention to business relationships and transactions with persons from the jurisdictions falling

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<sup>4</sup> The findings established by subject persons should not be automatically reported to the FIAU but should be made available to the FIAU and the relevant supervisory authority if and when the subject person is requested to do so. However, in the event that the findings of the subject person indicate a suspicion or knowledge of ML/FT, a report should be filed with the FIAU in accordance with Regulation 15(6) of the PMLFTR.

within Categories 1 and 2 and where considered necessary Category 3. Whenever the transactions involved have no apparent economic or visible lawful purpose subject persons shall proceed in accordance with the measures set out in this paragraph.

### **The reputability of a jurisdiction**

13. Regulation 2 defines a reputable jurisdiction as any country having legislative measures for the prevention of ML/FT, taking into account that country's membership of, or any declaration or accreditation by, any international organisation recognised as laying down internationally accepted standards for the prevention of money laundering and for combating the funding of terrorism, and which supervises natural and legal persons subject to such legislative measures for compliance therewith. Hence, for the purpose of the PMLFTR, the jurisdictions falling within Categories 1 and 2 shall not be considered to meet the criteria of a reputable jurisdiction as they do not have adequate legislative measures for the prevention of ML/FT and a clear and unequivocal declaration has been issued by the FATF in that respect. Those jurisdictions falling within Category 3 shall not automatically be considered to be non-reputable and subject persons are required to determine the reputability of each jurisdiction on the basis of the deficiencies identified by the FATF.
14. Subject persons shall not apply the simplified due diligence measures set out under Regulation 10, the reliance provisions set out under Regulation 12 and the provisions on permissible disclosures set out under Regulation 16 in relation to a business relationship or transaction connected to jurisdictions falling within Categories 1 and 2 and, where considered necessary, Category 3.
15. Additionally, in terms of Regulation 6(1) subject persons carrying out relevant financial business may not establish or acquire branches or majority owned subsidiaries in a jurisdiction falling within Categories 1 and 2 and, where considered necessary, Category 3.

### **Counter-measures**

16. The FATF has called on its members and has urged all other jurisdictions, including Malta, to apply effective counter-measures to protect their financial sectors from ML/FT risks emanating from the jurisdictions falling within under Category 1. Such jurisdictions have not achieved any progress and have not made any commitment to implement an action plan to address their deficiencies, despite the numerous attempts by the FATF to engage in such a process.
17. Since the FATF does not specify the counter-measures which are to be applied in relation to such jurisdictions, every jurisdiction may determine the counter-measures that are to be applied. In this regard, reference shall be made to Regulation 15(3) which states that subject persons are required to inform the FIAU of any business relationships or transactions with persons, companies and undertakings, including those carrying out relevant financial business or a relevant activity from a non-reputable jurisdiction which continues not to apply measures equivalent to those laid down in the PMLFTR. In relation to such business

relationships or transactions, the FIAU may, in collaboration with the relevant supervisory authority, require such business relationships not to continue or such transactions not to be carried out. The FIAU may also apply any counter-measures as may be adequate under the respective circumstances.

18. For the purpose of Regulation 15(3) the jurisdictions falling under Category 1 shall be considered to be non-reputable jurisdictions which continue not to apply measures equivalent to those laid down in the PMLFTR. Subject persons are therefore required to inform the FIAU, in writing, of any business relationships or transactions with such jurisdictions, in relation to which the FIAU may take the actions set out under Regulation 15(3).
19. In addition to informing the FIAU, banks are required to take measures to ensure that any correspondent banking relationships they may have in place are not being used to bypass or evade any counter-measures and risk mitigation practices by any person having a link to the jurisdictions falling within the first category of the FATF Public Statement.

#### **Status of this Guidance Note**

20. This guidance note is being issued in terms of Regulation 17(1), which shall therefore be binding on all subject persons. Failure to comply with this guidance note shall render subject persons liable to an administrative penalty of not less than two hundred and fifty euro (€250) and not more than two thousand five hundred euro (€2,500) in terms of Regulation 17(2). Penalties imposed under Regulation 17(2) shall be imposed by the FIAU without recourse to a court hearing and may be imposed either as a one time penalty or a daily cumulative basis until compliance, provided that in the latter case the accumulated penalty shall not exceed twelve thousand five hundred euro (€12,500).