OUTREACH EVENT
on the CBUAE AML/CFT Guidances for LFIs Providing Services to: Legal Persons and Legal Arrangements and Dealers in Precious Metals and Stones and the Real Estate Sector

4 August 2021

Outline of this Presentation

- Introduction
- Purpose and Structure of the Guidance Documents
- The Risk-Based Approach
- Customer Due Diligence
- Suspicious Transaction Reporting and Other Measures
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Purpose & Applicability of the Guidance Documents

Purpose

- The guidance documents are NOT regulations and do NOT introduce new legal obligations.
- They are designed to help CBUAE's LFIs understand the purpose and context of their existing legal obligations, as well as the CBUAE's expectations for how those obligations will be fulfilled.

Applicability

The guidance documents apply **to all financial institutions licensed or registered by the CBUAE.**

Structure of the Guidance Documents

Both guidance documents have similar structures. They are divided into two main parts:

Understanding Risk

This section discusses why the specific customer types that are the subject of the guidance pose elevated risks to LFIs, and describes aspects of these customers that increase or decrease their risk.

Managing Risk

This section discusses how LFIs can use *existing aspects* of their compliant AML/CFT program to manage the specific risks of these customers.

Understanding Risk

Understanding and Assessing Risks of LP-LA

ML/TF Risks of Legal Persons and Arrangements

- Legal persons and arrangements are attractive to illicit actors because they can assist criminals and their associates to:
- Hide the identify of the individuals directing a transaction or controlling an account;
- Obscure the true nature and purpose of an account or transaction; and
- Conceal the source of funds involved in a transaction or account.

Features and Controls that Mitigate Risks

Certain rules governing the formation and operation of legal persons can, if enforced, reduce the risk that they will be abused by illicit actors:

- Formation processes that deter creation of shell companies;
- Collection of beneficial ownership information for all legal persons and arrangements;
- Requiring legal persons and arrangements to keep certain records and make regular reports;
- Supervision and monitoring by appropriate government authorities.

Legal Persons and Arrangements in the UAE

Identification of Beneficial Owners

- Legal persons and arrangements in the UAE (with some exceptions) are required to identify all individuals who own or control at least 25% of the legal person or arrangements.
- Legal persons and arrangements must hold this information, and legal persons must also report it to their registrar. They must maintain and update this information when their beneficial owners change.

Legal Arrangements Under UAE Law

- UAE law allows for the creation of two types of legal arrangements: trusts and awqaf.
- Trustees and waqf supervisors must comply with certain requirements related to identifying the individuals party to the legal arrangement.

Economic Substance Requirements

- Companies operating in certain sectors must prove on an annual basis that they in fact do conduct business in the UAE by submitting certain required information to their registrar.
- LFIs can request the information from legal person customers.

Understanding and Assessing Risks of DPMS-RE

ML/TF Risks of DPMS-RE

- DPMS present higher risks to LFIs because their services and products are attractive to illicit actors.
- The RE sector presents a higher risk to LFIs because the sector offers an attractive way for illicit actors, criminals, and corrupt officials to move and store value while hiding their identity.
- Both sectors are also often inadequately governed and regulated.

Higher Risks: DPMS

- Operating in jurisdictions with lax or non-existent regulation or that are high risk for crime and terrorism;
- Offer products and services—such as the sale of gold bullion or of uncut stones—that allow customers to access a widely traded, fungible, anonymous form of value; or
- Serve a high-risk customer base, such as a high proportion of PEPs.

Higher Risks: RE Sector

- Weak regulation and/or supervision of real estate brokers and agents;
- Widespread use of cash to purchase real property;
- Lack of transparency on beneficial owners of real estate;
- Openness to foreign purchasers, including 'golden visa' programs; and
- High liquidity and rising prices.

DPMS-RE in the UAE

Regulation of DPMS in the UAE

- DPMS in the UAE may qualify as DNFBPs if they conduct cash transactions above AED 55,000. If so, they are required to apply AML/CFT controls like those used by LFIs.
- If not, they are required to be licensed, but are not required to have an AML/CFT program.

Regulation of RE in the UAE

- The RE sector in the UAE is complex, with each emirate applying its own rules.
- Foreign purchasers can purchase freehold property in certain areas of Dubai and Abu Dhabi (the largest markets), and throughout the UAE foreign purchasers who purchase property above a certain value gain residency rights.
- Real estate brokers and agents are regulated as DNFBPs.

Taking a Risk-Based Approach

Risk-Based Approach

In assessing the risk of a **LP-LA customer**, LFIs should consider at least the following factors:

- The legal form of the customer;
- The controls governing the formation of that type of customer;
- The controls in place to ensure that the customer identifies and reports its beneficial owners;
- Whether the customer is subject to recordkeeping and reporting requirements;
- Whether the customer is appropriately supervised for its compliance with these requirements.

In assessing the risk of a **DPMS and RE sector** customer, LFIs should consider at least the following factors:

- The jurisdiction(s) in which the customer is based or does business, including both the jurisdictional risk of crime and terrorism but also the regulation in place on the DPMS and real estate sectors;
- The products and services the customer supplies to its customers;
- The customer’s customer base;
- The quality of the customer’s AML/CFT controls, where they exist.

Customer Due Diligence

Customer Due Diligence: ID of Customers and Beneficial Owners

Customer Identification: As part of the customer identification process, LFIs should collect information necessary to assess the customer on the risk factors discussed above:

- The controls governing the formation of that type of customer;
- The controls in place to ensure that the customer identifies and reports its beneficial owners;
- Whether the customer is subject to recordkeeping and reporting requirements;
- Whether the customer is appropriately supervised for its compliance with these requirements

Identification of Beneficial Owners: Beneficial ownership identification should be risk-based; the threshold in the AML-CFT Decision is a starting point. LFIs should assess whether identification of additional owners holding smaller stakes might assist them to manage the risk of a particular customer.

Many **DPMS and RE sector** customers will be legal persons. LFIs should, along with the steps described above, make sure that their customer has the appropriate licenses and an active registration with a UAE company registrar.

Identifying Beneficial Owners

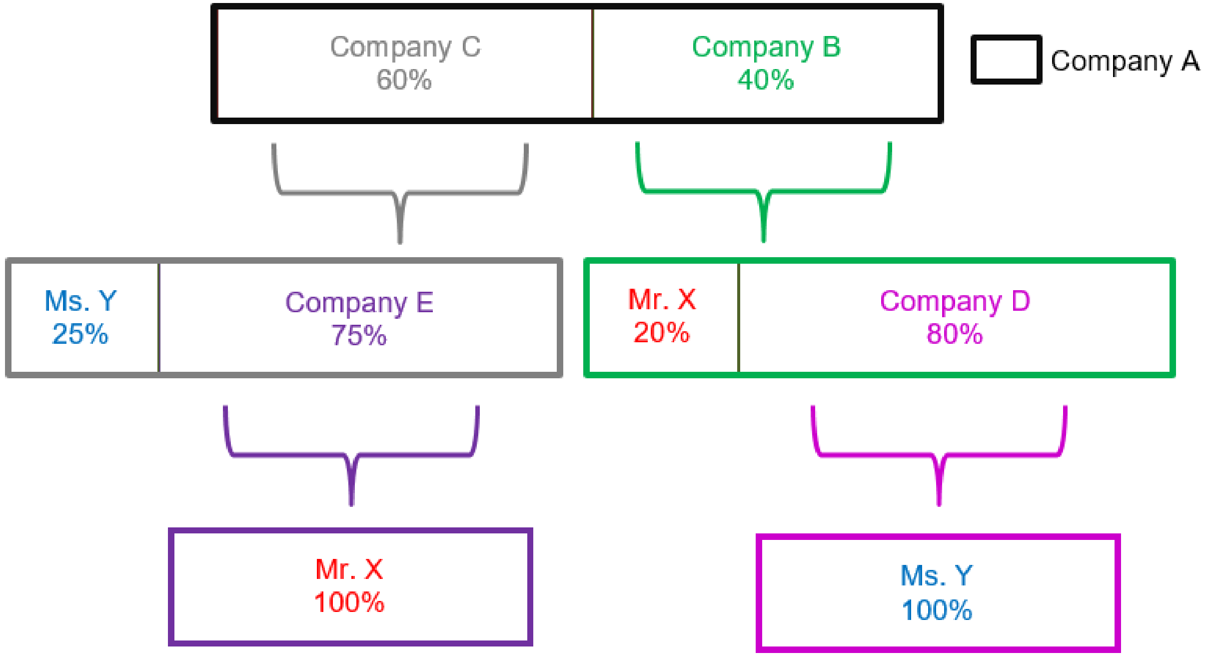
Simple Scenario

Mr. X 50%	Ms. Y 50%

Company A

Identifying Beneficial Owners

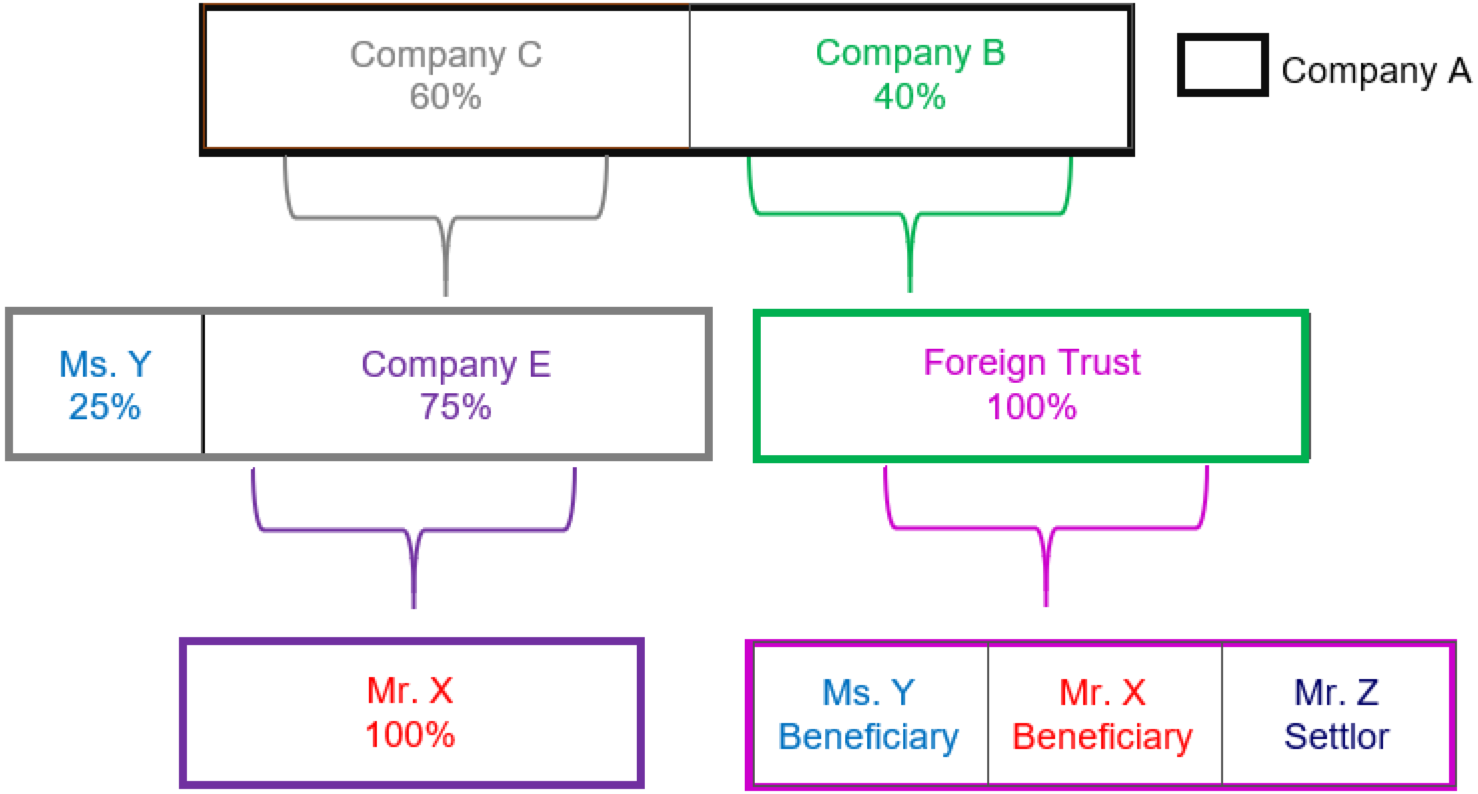
Indirect Ownership



Owner	Share	Source
Mr. X	8%	Ownership of Company B
Ms. Y	15%	Ownership of Company C
Mr. X	45%	Ownership of Company E
Ms. Y	32%	Ownership of Company D

Identifying Beneficial Owners

Legal Arrangement



Owner	Share	Source
Ms. Y	15%	Ownership of Company C
Ms. Y		BO of Foreign Trust
Mr. X	45%	Ownership of Company E
Mr. X		BO of Foreign Trust
Mr. Z		BO of Foreign Trust

Customer Due Diligence: Purpose and Nature of the Account and Customer's Business

- The purpose of the account and the nature of the customer's business are critical drivers of risk for DPMS and RE sector customers. LFIs should fully understand how their customer makes money and what types of transactions it expect to carry out through the LFI's account.
- As they seek to understand the customer's business, LFIs should collect the information necessary to assess customer risk. This information is also critical to, and closely linked with, the customer risk rating process. LFIs should understand:
  - The jurisdiction(s) in which the customer is based or does business, including both the jurisdictional risk of crime and terrorism but also the regulation in place on the DPMS and real estate sectors;
  - The products and services the customer supplies to its customers;
  - The customer's customer base;
  - The quality of the customer's AML/CFT controls, where they exist.

Customer Due Diligence: Ongoing Monitoring

Ongoing monitoring should be risk-based, so that higher-risk customers receive more frequent and intrusive monitoring.

Ongoing monitoring should include both a review and updating of customer information held by the LFI, and a review of the customer's account activity since the last time the customer profile was updated.

It also should be tailored to the risks identified during the customer risk-rating process and the risks inherent to the customer's structure, sector, or business.

- For legal persons with complex structures, LFIs should be certain that their understanding of the customer's ownership and control structure remains accurate and current.
- For customers that are engaged in high-risk sectors, LFIs should assess whether the customer's business operations have changed in such a way so as to lower or increase their risk.

Other Controls

Mitigating Risk: Suspicious Transaction Reporting and TFS

Suspicious Transaction Reporting

Where possible, LFIs should apply monitoring rules that are reasonably designed to alert on behaviors that are linked to the risks posed by specific customer types, and should consider customer type when investigating the alerts its TM system generates. For example:

- "Burst" activity by a shell company may be more concerning than when it is exhibited by an operating company that pays salaries at the end of the month.
- A dealer in gold bullion may make regular payments to high-risk jurisdictions without causing concern, while the same activity would be unusual for a jeweler that sources materials on the secondary market.

Implementation of TFS

- Legal persons and arrangements pose special challenges for sanctions screening programs, because a legal person or arrangement that is not itself designated on a sanctions list may be owned by someone who is designated.
- LFIs must screen the beneficial owners of all legal person and legal arrangement customers against sanctions lists, and should freeze any accounts or transactions related to a legal person or legal arrangement that is more than 50% owned or controlled by a designated person.

Mitigating Risk: Governance and Training

Training

- Training programs should educate employees about the risks faced by the LFI, including the particular risks associated with sectors and customer types to which the LFI has substantial exposure.
- LFIs should develop dedicated training materials or programs for employees who frequently deal with higher-risk customer types or sectors, whether within the compliance function or the business.

Governance

- Controls should be established within the context of a well-governed AML/CFT program, with clear roles and responsibilities; a qualified compliance officer; and substantive oversight by the Board and senior management.
- Where an LFI has developed a strong customer base in a certain sector, its AML/CFT compliance program should reflect this, and its compliance officer should be knowledgeable about those risks.

Scenarios

The customer is an LP established in the Country A, a common location for offshore company foundation. Its transactions are generally large round-dollar amounts and do not follow a particular pattern. The customer's address is a building that is also the registered office of thousands of other firms and a well-known trust and company service provider.

Risk Assessment

- The customer may be a shell corporation.
- It is founded in a jurisdiction known for corporate secrecy.
- It appears to have been established by a firm that specializes in corporate vehicles.
- Its transactions follow a known illicit pattern but could also be explained by legitimate activity.

Risk-Based Response

- Re-evaluate beneficial ownership information—is it reliable? Sufficient? How can shortcomings be corrected?
- Ask the customer to provide additional information on transactions.
- Set monitoring rules that will alert you when the customer transacts above a certain threshold.

The customer is a gold trader in the Dubai Gold Souk. The customer asserts it does not accept cash payments and is not a DNFBP. Three years into the relationship the customer begins to make large cash deposits. The customer also begins to frequently order outbound wires to beneficiaries in Country B, which is not known to be a gold-producing country.

Risk Assessment

- The customer may have begun accepting cash payments, changing its status as a DNFBP.
- The customer's changed transaction behavior—especially with a country that is not known to produce gold—could be legitimate but requires further investigation.

Risk-Based Response

- Conduct a CDD review for the customer, including asking the customer whether it has changed its policy on cash transactions.
- Inquire regarding the nature of the transactions with Country B. Request and review invoices.

A trust established in the DIFC seeks to establish a bank account. The settlor of the trust is a legal person, and the beneficiaries are all legal arrangements. The trustee is a professional trustee based in Country C, a known tax haven. The customer intends to make only a nominal initial deposit.

Risk Assessment

- The complex nature of the customer structure is not clearly justified by business purpose.
- Country C is known to be associated with tax evasion.
- The purpose of the account—with little initial funding—requires further explanation.

Risk-Based Response

- Consider requiring the customer to submit information on beneficial owners at the 10% threshold.
- Conduct EDD on all beneficial owners.
- Require advanced permission prior to any transactions on the account.

Questions