

# FINANCIAL CRIME PREVENTION PROGRAMME REPORT | 2019 - 2021



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# GOVERNOR'S STATEMENT

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I am pleased to share the Dubai International Financial Centre's (DIFC) 2021 Financial Crime Prevention Programme report. This report sets out the DIFC's actions, taken since our 2018 report, to reduce the risks of money laundering, the financing of terrorism and proliferation, and to uphold the highest global standards. Both the DIFC and the UAE Government are fully committed to tackling financial crime to safeguard the integrity of the international financial system.

The Financial Action Task Force (FATF) Mutual Evaluation Report of the UAE, published on 30 April 2020 (the 2020 FATF Report), made several positive statements regarding the efforts of the Dubai Financial Services Authority (DFSA) and DIFC Authority's Registrar of Companies (RoC) to prevent abuse of the financial system. The Mutual Evaluation Report included recognition of the DFSA's efforts to:

- develop a detailed understanding of Money Laundering, Terrorism Financing and Proliferation Financing (ML/TF and PF) risks in the areas it supervises, which extends to the individual institution level;
- apply a risk-based approach since 2013 and, having recently further developed that approach, to enhance supervision activity based on ML/TF and PF risk to achieve a more detailed understanding of ML/TF and PF risks in the areas it supervises; and
- apply effective, proportionate, and dissuasive sanctions against both firms and individuals.

The 2020 FATF Report also recognised the efforts of the RoC for its commitment to:

- develop a robust AML review process for non-financial services entities seeking permission to operate in DIFC;

- reinforce the entity application and on-boarding process in relation to nominee arrangements, to capture the existence and associated risk of any such relationship; and
- clarify and apply strict informational requirements around ultimate beneficial ownership arrangements.

Since the publication of the Mutual Evaluation Report, the UAE has taken significant additional steps to align regulatory, supervisory and enforcement frameworks further with the FATF Recommendations. Within the DIFC, the DFSA has continued its proactive and assertive efforts in this regard, encompassing monitoring programmes, thematic reviews, compliance assessments and triggers, which underpin an intensive and sustained cycle of supervision. In so doing, the DFSA has continued to demonstrate the application of effective, meaningful, proportionate, and dissuasive sanctions against both firms and individuals.

The RoC undertook several initiatives to assess and investigate elements critical to preventing non-financial services entities from engaging in financial crime, including enhancing the on-boarding assessment processes for non-financial firms, inspections automation and thematic assessment(s) on key risk areas, strict enforcement of the DIFC Ultimate Beneficial Ownership Regulations (2018), and active participation in the UAE Sub-Committee of Companies Registrars.

We will continue to work with our peer organisations across the UAE and internationally, applying an effective risk-based approach built on a proven methodology for assessing financial crime risks. We will continue to develop our understanding, policies, strategies and activities with the same agility demonstrated since the inception of the DIFC almost two decades ago. The DIFC is committed to playing our part in the UAE by demonstrating high standards in combatting financial crime. We remain resolute in our efforts to work closely with firms and individuals in the Centre to educate them about, and mitigate, financial crime risks.

**ESSA KAZIM**

Governor of the DIFC and Chairman of the DIFC Authority

# INTRODUCTION

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Preventing the misuse or abuse of the financial system is a critical part of the worldwide effort to protect broader society against harms arising from financial crimes and their predicate offences. The UAE has joined over 200 countries in adopting the International Standards on Combatting Money Laundering and the Financing of Terrorism and Proliferation set by the FATF, the global standards setting body founded in 1989 to counter these threats and promote the integrity of the global financial system.

The DIFC is a purpose-built financial free zone in Dubai. It offers a unique and independent legal and regulatory framework to create an environment for growth and economic development in the UAE and wider region. Since the publication of our 2018 Financial Crime Prevention Programme report, international assessors have expressed favourable views about the anti-money laundering efforts of the DIFC and of the DFSA, the independent regulator of financial services conducted in or from the DIFC. This report highlights the progress made by the DIFC in further aligning its regulatory, supervisory and enforcement frameworks with the FATF recommendations over the past three years.

The next two sections of this report are provided by the DFSA and the DIFCA, respectively, describing their work and progress made over the past three years.

# DFSA PROGRESS

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Since the publication of the DFSA's Financial Crime Prevention Programme in 2018, the UAE has undergone a Financial Action Task Force (FATF)-MENAFATF<sup>1</sup> joint mutual evaluation of the of the UAE's level of compliance with the FATF Recommendations, including the effectiveness of the UAE's measures to combat money laundering, terrorist financing and proliferation financing. Leading up to the evaluation, the DFSA made a series of policy amendments to bring our AML/CTF and CPF framework into further alignment with the FATF Recommendations 2021 (as amended).

With the publication of the Mutual Evaluation Report (MER) in April 2020, international assessors shared favourable views recognising the DFSA's efforts in developing a detailed understanding of ML/TF risks in the supervised areas, extending to individuals and institutions; applying and continuously improving a risk-based approach to ML/TF supervision and enforcement; and applying effective, meaningful, proportionate and dissuasive sanctions against both firms and individuals.

Since the publication of the UAE MER, the UAE's national effort to build and demonstrate further progress and alignment with the FATF Recommendations has been relentless. To this end, the DFSA has actively participated in the discussions and policy works of the various national AML/CTF and CPF committees and sub-committees, including the following groups:

- UAE National Anti-Money Laundering and Combatting Financing of Terrorism and Financing of Illegal Organizations Committee (NAMLCFTC);
- the Sub-Committee for National Risk Assessment of Money-Laundering, Terrorism Financing and Illegal Organizations Financing Risks in the United Arab Emirates (UAE NRA Sub-Committee);
- the Sub-Committee for Supervisory Authorities in the United Arab Emirates (Supervisory Authorities Sub-Committee);
- the Sub-Committee for Combatting the Financing of Terrorism and the Financing of Illegal Organizations and the Financing of Proliferation in the United Arab Emirates; and

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1 Middle East and North Africa Financial Action Task Force, a FATF-style regional body.

- the Sub-Committee on Public-Private Partnership to Counter Money Laundering and Terrorism Financing.

The DFSA also contributed to the development of the 2020 - 2022 National Strategy for Combating Money Laundering and Terrorism Financing and the formation of the corresponding National Action Plan. In addition, we participated in several sectoral risk assessments conducted by the UAE National Risk Assessment Sub-Committee. The DFSA's efforts to combat financial crime, carried out under the federal AML/CTF and CPF framework of the UAE and in collaboration with wider stakeholders, include outreach and engagement with our regulated community, other regulators with oversight responsibility for these entities through MOUs and information sharing actions, and the DIFC Registrar of Companies. To demonstrate and reinforce the effectiveness of our efforts, we have continued to engage with our regulated population to help them understand and comply with federal AML/CTF and CPF legislation and the DFSA's own AML Module.

Between 2019 and 2021, the DFSA expanded its permitted financial services activities, introducing new regulatory regimes to accommodate emerging and growing business models. More specifically, with the introduction of the Money Services Regime, the DFSA became the prudential and AML supervisor for newly created money services businesses in the DIFC. In addition, the scope of Financial Institutions under the regulatory remit of the DFSA expanded to include property crowdfunding platforms, venture capital fund managers, employee money purchase scheme operators and scheme administrators. The scope of Designated Non-Financial Businesses and Professions (DNFBPs) under the DFSA's mandate has not changed during the reporting period, and such firms remain subject to the DFSA's supervision, including its AML regulatory framework.

As the digital economy continues to grow in the region, the DFSA plans further public consultations in relation to the market's rapidly expanding interest in virtual assets (VA) and virtual asset service providers (VASPs). In October 2021, the DFSA introduced its Investment Token regime, making it possible for authorised Financial Institutions to provide financial services using cryptographically secured (tokenised) digital representations of assets such as securities or derivative products. This was the DFSA's first step towards regulating service providers in this space.

Regarding other forms of virtual assets, such as digital representations of value that can be used to trade, invest, or make payments, as defined by FATF, the DFSA does not currently authorise such activity beyond investment tokens. Moreover, federal law prohibits their use without proper registration or licensing. The DFSA is currently developing a potential regime for VAs and for licensing VASPs in the DIFC.



As investments and trade in virtual or digital assets increase, efforts to address money laundering and terrorist and proliferation financing risks arising from these activities increasingly highlight significant impediments that supervisors worldwide must confront. These challenges include the following:

- growth in the use of digital assets for cross-border transactions, which highlights the lack of internationally accepted standards for the licensing and use of virtual or digital assets in trade and commerce;
- the use of novel yet largely untested technology supporting their administration;
- the impact of conducting decentralised activities under regulations that presume, and require, centralised providers; and
- the need to ensure the traceability and attribution of transactions while maintaining privacy for consumers acting in good faith.

We are designing controls to mitigate regulatory risks posed by these factors, in cooperation with global regulatory counterparts, and in concert with the federal policymaking efforts for regulating VAs and VASPs in the UAE. The DFSA will consult publicly and collect feedback to incorporate into our VA and VASP-related proposals later this year.



# THE DFSA'S RISK BASED APPROACH TO FINANCIAL CRIME RISK

## THE DFSA'S RISK-BASED APPROACH TO LICENSING/REGISTRATION

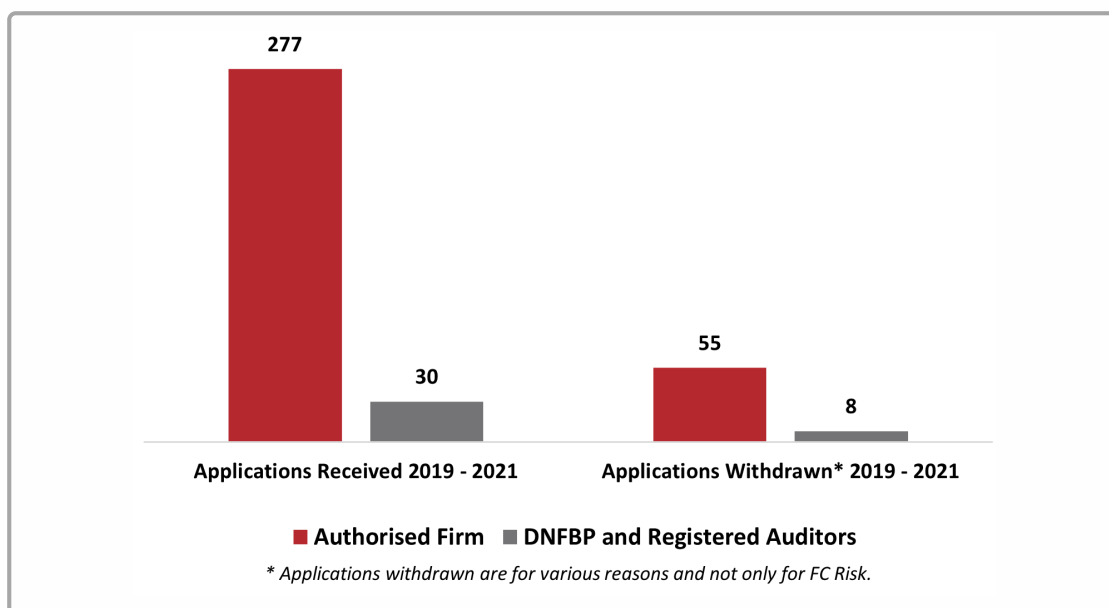
In line with its regulatory mandate, the DFSA continues to review its licensing process to ensure it remains fit for purpose, including that firms onboarded into the DIFC have a sound understanding of AML/CTF requirements and an appropriate control framework in place to address them. In December 2020, the DFSA integrated responsibility for evaluating applications for licensing or registration across its supervisory function to provide adequate resources and to allocate sufficient expertise in our review of all applicants' business models.

All persons conducting financial services or DNFBP activities in the DIFC must obtain a DFSA licence or registration, respectively. The process necessitates an assessment of the financial crime risks associated with a number of key factors, including, but not limited to:

- a. proposed business model;
- b. identification and verification of controllers and beneficial owners;
- c. fitness and propriety checks of senior management, systems and controls; and
- d. evaluations of the quality of risk management processes to mitigate financial crime risk.

At the initial stage of the licensing process, the DFSA undertakes a materiality review of the applicant and its proposed business model to identify the level of risks involved and the amount of authorisation resources required to assess the application. This is a comprehensive review that covers various factors, including the country of origin, complexity of ownership structure, beneficial owners and business models.

Since 2019, the DFSA has received a total of 276 Financial Institution licensing and 25 DNFBP registration applications. A total of 159 Financial Institutions and 20 DNFBP applicants were granted DFSA licences and registration status, respectively. Based on our review, a small percentage of the applications that were withdrawn during this period presented risk profiles that exceeded the DFSA's risk tolerance. Where an application raises material concerns during the initial risk identification stage mentioned above, the DFSA undertakes enhanced due diligence and escalates the matter to senior case managers. Those managers then evaluate the risks presented and take steps to mitigate them both in the pre-application and post-application stages of licensing and registration. Where material concerns remain, even after taking into account an applicant's financial crime prevention programme, the applicant is notified of the DFSA's findings and in most cases opts to withdraw its application.



## THE DFSA'S RISK-BASED APPROACH TO SUPERVISION

The DFSA has applied a risk-based approach since 2013, based on a comprehensive understanding of risk at sectoral, business model and institution-specific level. Since 2019, the DFSA has continued to enhance its risk-based approach to Supervision, which takes into consideration the UAE NRA and other Risk Assessments. Most notably, the DFSA has enhanced its assessment process for Financial Institutions and DNFBPs on inherent risk data points and control data points that feed into the risk profile of the firm. If the risk profile or control levels are not deemed adequate, the matter is escalated to the DFSA's senior management for allocation of resources and continuous supervision, either continuously or until specific issues are resolved or remediated to the satisfaction of the DFSA. The following section sets out the DFSA's risk-based approach across different supervisory areas.

## THE INNOVATION TESTING LICENCE PROGRAMME

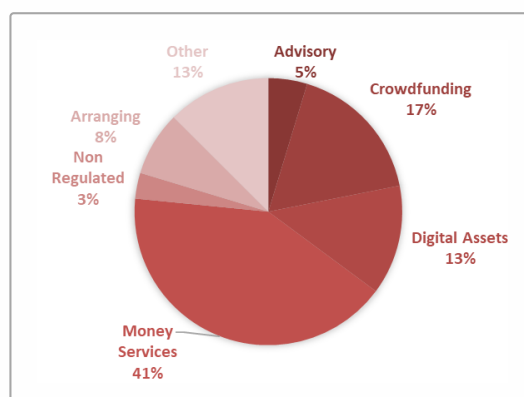
A DFSA Innovation Testing Licence (ITL) is a financial services licence provided to companies that would like to test their innovative solutions in a regulated environment. The ITL is a controlled testing environment that helps foster technology and innovation in financial services in or from the DIFC under careful regulatory scrutiny. Within the ITL, firms are restricted in the amount of business they can undertake in and from the DIFC and are permitted the flexibility of certain waivers and modifications to DFSA's Rules to help them test their innovative products or services without undue regulatory burden. It is important to note that, although certain Rule waivers and modifications are provided, full compliance with DFSA AML Rules is mandatory at all times. The DFSA follows a risk-based approach when licensing and supervising firms within the ITL framework.

## Licensing of ITL

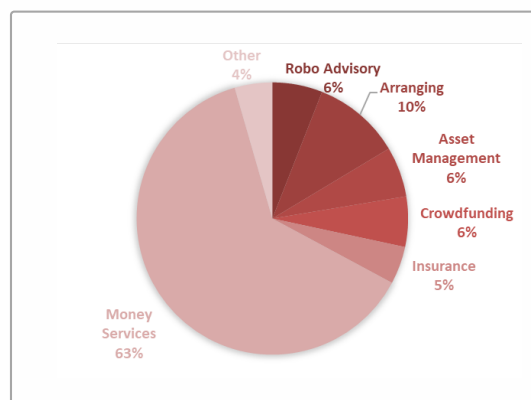
To enable ITL applicants to test their business model and innovative financial products and services, the DFSA provides various waivers and modifications to the DFSA Rules. However, financial crime controls are not waived or modified, and all applicants must, at all times, demonstrate full compliance with the AML/CTF legislative regime that applies in the DIFC. Therefore, all applicants are required to develop and maintain AML/CTF controls commensurate to the financial crime risks and exposures presented by the firm's business model. This includes, amongst other things, establishing appropriate control frameworks reflecting the applicant's customer types and nature of business activities, relevant jurisdictions, counterparties, outsourcing, delivery channels, use of new technologies and value, volume, and complexity of transaction activity.

Since its launch in May 2017, the DFSA has opened seven rounds, or cohorts, for ITL applications. A total of 128 cohort applications were received; of these applications, 67 met the DFSA's eligibility criteria and were accepted into their respective cohorts. Of the 67, 14 were granted an ITL licence and 37 withdrew their application prior to being licensed. The following charts illustrate a breakdown of the applicants' business models and accepted applications.

## ITL applicants by business model



## Accepted ITL applicants by business model



## Supervision of ITL

After granting an ITL licence, the DFSA conducts close and continuous monitoring of licensed ITL firms. This includes regular meetings with senior management including the Compliance and Money Laundering Reporting Officers (MLRO), desk-based reviews of the product or service offerings, and client file review at the commencement of the firm's operations to test its level of compliance with DFSA AML Rules.

The DFSA generally conducts the client file review at the time the firm starts on-boarding its first customers. The aim of this review is to provide quick and efficient feedback on customer on-boarding practices and assess the control levels within the firm. Based on the business model, the DFSA may also conduct a broader financial crime review via a Business AML Risk Assessment to cover transaction monitoring systems.

Any major findings are dealt with through formal Risk Mitigation Plans set by the DFSA. Upon completion, the DFSA conducts follow-up reviews to verify whether identified regulatory issues and/or breaches have been fully rectified to its satisfaction. If an ITL firm fails to rectify the issues during the agreed timeframe, the DFSA, as part of its supervisory oversight, would consider formal action, which may include a suspension of the firm's ITL licence.

## FIRMS LICENSED TO PROVIDE MONEY SERVICES

In April 2020, the DFSA expanded its permitted financial services activities by introducing a comprehensive Money Services regime. Considering the relative newness of the money services regime and the associated risks, the DFSA has decided to accept only established money services entities through the normal authorisation route and to direct all start-up money services business to the ITL programme. This allows the DFSA to monitor start-up entities closely in a controlled environment before allowing them to provide their service

on a larger scale. This approach also helps start-up firms to ensure that their compliance framework will be fit for purpose in keeping pace with any anticipated business growth.

The DFSA updated its risk-based approach to licensing and supervision specifically to address inherent risks from this financial service. This includes, but is not limited to, the following:

- allocation of expert resources from the Financial Crime Prevention team to the ITL licensing and supervisory team;
- assessment of the business model along with the applicant's Business AML Risk Assessment;
- assessment of the proposed AML/CTF and CPF systems and controls;
- assessment of the fitness and propriety of the proposed MLRO. The DFSA also expects the proposed MLRO to be fully conversant with all AML/CTF/CPF legislation that applies to the particular firm in the DIFC; and
- early testing of AML/CTF and CPF systems and controls through testing of implementation of reporting obligations to the FIU, the Executive Office of the Committee for Goods and Materials Subject to Import and Export Control (UAEIEC) and any supervisory specific reporting, desk-based reviews, client file reviews and testing of payments

processing frameworks for transaction monitoring and sanctions screening controls.

## SANCTIONS COMPLIANCE

Sanctions compliance is a key regulatory priority for the DFSA. The DFSA's supervisory framework includes assessment of Targeted Financial Sanctions (TFS) compliance in accordance with the DFSA's Rules, which require Financial Institutions and DNFBPs to maintain adequate systems and controls to demonstrate compliance with all applicable sanctions imposed by the United Nations (UN), the UAE Government and FATF findings.

Since mid-2019, the DFSA has continued with its compliance review process including onsite, offsite and thematic reviews to verify that Relevant Persons comply with sanctions-related obligations that apply in the DIFC.

### TFS onsite reviews

In relation to onsite compliance reviews, the DFSA, in line with its supervisory plan, continued to assess firms' TFS compliance within the sectors it supervises. To date, the DFSA has observed a low number of TFS-related breaches by Relevant Persons. The breaches are generally prevalent in newly authorised firms that may be less familiar with AML regulations, which emphasises the importance of the DFSA's efforts to engage early with them. Common themes observed by the DFSA since mid-2019 include

failures to conduct ongoing sanctions screening of customers and counterparties and inadequate sanctions compliance policies and procedures.

### TFS thematic reviews

In early 2021, the DFSA commenced a review of the sanctions section of the 2020 DFSA AML Return submitted by all Relevant Persons. The purpose of the 2021 TFS thematic review was to assess whether all Relevant Persons complied with the sanctions measures set out under UAE Federal Cabinet Decision No. 74, issued by the UAE Federal Government on 27 October 2020, and to assess the effectiveness of firms' systems and controls. A sample of firms representing a cross-section of the DFSA's regulated population were selected for further follow-up. The DFSA is pleased to observe that selected Relevant Persons had all undertaken regular reviews of their client base to ensure compliance with sanctions notifications and applicable legislation. A key outcome of this review was to update the sanctions section of the DFSA Annual AML Return to assist firms further and improve the quality and consistency of reported data. The final report from the 2021 TFS thematic review will be available on the DFSA's website in 2022.

## Enhancements to the DFSA Annual AML Return

In July 2021, the DFSA enhanced its annual AML Return by expanding the TFS sanctions compliance section. The AML Return is a self-certification framework, whereby Relevant Persons must certify that they have appropriate systems and controls to monitor, on an ongoing basis, relevant resolutions and sanctions issued by UN, UAE and FATF, and applicable sanctions-related legislation that applies in the DIFC. The enhancements captured data points such as terrorist financing- and proliferation financing-designated persons lists (published by the UN and the UAE) that were determined to be false positive matches versus true matches by Financial Institutions and DNFBPs.

## TFS Guidance

In coordination with the UAEIEC, the DFSA circulated TFS Guidance to its regulated community in the DIFC during May and November 2021. The TFS guidance can be accessed via the DFSA's website or directly via the UAEIEC's website.

## Updates to DFSA TFS Inspection Procedures

As part of its risk scoring model applied to Relevant Persons, the DFSA assesses the inherent risk and control framework for several risk groups, including for AML/CTF. Within this specific AML/CTF risk group, there are specific risk elements that include sanctions.

The sanctions risk element is generally expected to be covered by the TFS compliance policies and procedures, and the sanctions screening frameworks, implemented at Financial Institutions and DNFBPs. With the issuance of Cabinet Resolution No 74 of 2020, new TFS Guidance for Financial Institutions and DNFBPs was issued by the UAEIEC and a new reporting mechanism introduced for TFS Potential Matches and Confirmed Matches via the UAE Financial Intelligence Unit's goAML Portal[1] during August 2021. In 2020, the DFSA also updated its TFS inspection procedures to cover the following areas:

- Governance;
- Business AML Risk Assessment in relation to TFS;
- Customer Risk Assessments;
- Monitoring and Controls;
- Sanctions Screening Tools;
- Assessing automatic screening tools;
- Alert Management and Investigation; and
- Reporting Obligations.

## Enhancements to TFS-related Notifications

Relevant Persons are required to notify the DFSA immediately upon becoming aware that they may be carrying on, or be about to carry on, an activity, or holding or about to hold money or other assets, or undertaking or about to undertake any other business for or on behalf of a person, where such carrying on, holding or undertaking constitutes or may constitute a contravention of a relevant sanction or resolution issued by the United Nations Security Council or the UAE Local Terrorist List.

Furthermore, the DFSA expects Relevant Persons to inform the DFSA as soon as possible when they become aware of any sanctions matter concerning them or a member of their Group that could result in adverse reputational consequences. This would generally also include secondary national or regional sanctions issued by entities such as the European Union, the United Kingdom's HM Treasury, or the United States of America's Office of Foreign Assets Control.

## Updates to DFSA TFS Inspection Procedures

In August 2021, the UAEIEC launched a new reporting mechanism for TFS Potential Matches and Confirmed Matches via the goAML<sup>2</sup> Portal. The new TFS reporting

mechanism was communicated to all Relevant Persons. The DFSA also has a dedicated mailbox, monitored by the Financial Crime Prevention Team, that receives all notifications made via goAML.

Upon receipt of notifications, the DFSA has engaged with Relevant Persons to assess the level of their understanding and compliance with the new TFS requirements. It is worth noting that a number of Relevant Persons have also made notifications in relation to secondary sanctions. The DFSA generally uses these notifications to discuss with Relevant Persons their sanctions compliance framework.

## SECTORAL AND THEMATIC REVIEWS

In line with its annual operational work plan, the DFSA undertook certain thematic reviews to understand and assess financial crime risks in DFSA supervised sectors in the DIFC.

### Financial crime risk in the brokerage sector operating in the DIFC

In mid-2020, the DFSA commenced a review that assessed the quality of the AML Business Risk Assessments (ABRA) conducted by each of the sample firms operating in the brokerage sector. The objective of the review was to determine the extent to which selected firms based their AML compliance programmes on their

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<sup>2</sup> The goAML system is an internationally accepted tool developed by the United Nations Office on Drugs and Crime to assist national authorities in their AML and CFT efforts.



ABRAs and to test the linkage between the ABRA and the quality and effectiveness of the firm's systems and controls in place in respect of Customer Risk Assessments and due diligence requirements.

The review including a desk-based assessment of the firm's documentation, virtual meetings and client file reviews for further testing. The review identified various areas of weakness, and the DFSA provided feedback to individual firms to address the shortcomings identified. A Dear SEO letter was sent to all firms that encouraged them to consider the findings in the context of their own operations and determine if process improvements were necessary. The Final Report was published in November 2021 and is available on the DFSA's website. The DFSA intends to conduct an outreach session on the outcomes of this review in 2022.

#### **Follow-up Thematic Review to focus on Trade Finance (TF) Risk and thematic work covering Correspondent Banking and Electronic Fund Transfers systems and controls in the DIFC**

In 2017, the DFSA published the findings of a thematic review on Trade Finance (TF). The thematic review included an assessment of sanctions systems and controls, including the Financial Institutions' involvement in the trade of dual-purpose goods and the facilitation of cross-border transactions. In 2020, the DFSA conducted a follow-up thematic review to focus on TF risks. This thematic review was specifically aimed at

testing firms' responses to the DFSA's earlier 2017 thematic findings and thereby also provided an assessment of the DFSA's supervisory effectiveness, that is, whether our use of thematic work and published good and poor practices help improve compliance standards in this high-risk area.

In addition, during 2020, the DFSA also completed thematic work covering Correspondent Banking and Electronic Fund Transfers systems and controls in place at a sample of Financial Institutions licensed by the DFSA. This included assessing measures in place for managing TFS. Good practice examples observed in the sample included the following:

- use of 'fuzzy logic' for possible name matches, addresses and other identifiers;
- larger firms using dedicated staff at Group centres for name screening and managing possible matches (until satisfactorily discounted);
- concurrent screening by the DIFC based entity;
- use of industry recognised proprietary systems for regular screening; and

The final report for both reviews will be available on the DFSA's website in 2022.

## Financial Crime Risk in the Representative Office Sector operating in the DIFC

In early 2021, the DFSA commenced a review of firms licensed to operate as Representative Offices in the DIFC. Representative offices are authorised to market financial products and services provided by the Group of which they are a part, but otherwise not to engage in financial services in or from the DIFC. The review included a review of the quality and effectiveness of each firm's ABRA together with its policies and procedures covering AML, CTF and sanctions compliance. The findings of this review will be published in 2022.

## OUTREACH EVENTS

The DFSA continues to engage with its regulated community via various outreach sessions and via enhancements to the DFSA's website.

Since 2019, the DFSA's outreach efforts focused on TFS compliance. In addition, the DFSA conducted a number of dedicated sessions for ITL applicants focusing on ML/TF and PF risks and the systems and controls the DFSA expects ITL applicants to put in place. These sessions aimed to enhance the knowledge of ITL applicants on the importance of AML/CTF and CPF controls and compliance.

In early 2021, the DFSA updated its website to make the AML, CTF and Sanctions Compliance section more readily accessible and to update all related guidance notes. The DFSA has also introduced 'Dear MLRO' letters, which are letters aimed at MRLOs to communicate directly with them on relevant issues. For example, these letters have been used to inform MLROs of new guidance at federal level, notices (e.g., High Risk Jurisdictions) and changes to relevant United Nations Security Council resolutions and UAE Terrorist Lists.

In September 2021, following the establishment of the Sub-Committee on Public-Private Partnership for Counter Money Laundering and Terrorism Financing in August 2021, the DFSA hosted a meeting between the UAE Sub-Committee on Public-Private Partnership for Counter Money Laundering and Terrorism Financing and the DIFC-based private sector.



# THE DFSA'S ANNUAL AML RETURN - ANALYSIS

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In July 2013, the DFSA introduced the annual AML Return form (the AML Return), which was subsequently introduced as an online form in July 2017. The AML Return requires Relevant Persons to self-assess compliance and provides the DFSA with key qualitative data. This regulatory filing provides the DFSA with an overall snapshot of the financial crime landscape and risks for all supervised firms in the DIFC at a given time. The information submitted in the AML Return is part of our desk-based risk assessment process conducted prior to an onsite risk assessment visit. Further, the AML Return assists in the selection process and prioritisation of firms for onsite risk assessment visits.

For the reports due by end September 2021, the DFSA received 98% of the AML Return (2021 AML Return) on time. Delays in submitting the AML Return raise concerns, and for this reporting period the DFSA issued a Supervisory Concerns Letter to Relevant Persons who failed to submit by the stated deadline. This resulted in an immediate submission of the 2021 AML Return. The DFSA has zero tolerance for any delayed submissions or reporting and takes immediate, formal steps and actions for non-compliant Relevant Persons. Relevant Persons must ensure their monitoring programs factor in these mandatory deadlines to avoid regulatory action.

The 2021 AML Returns<sup>3</sup> provided the DFSA with an insight into the following areas:

## **Senior management satisfaction with anti-financial crime framework**

The 2021 AML Return provides information on the level of senior management satisfaction that the Relevant Person has adequately assessed its anti-financial crime framework. The review covers the following areas:

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<sup>3</sup> The 2021 AML Return covers the reporting period of 1 August 2020 to 31 July 2021.

## SENIOR MANAGEMENT ASSESSMENT OF ANTI-FINANCIAL CRIME FRAMEWORK



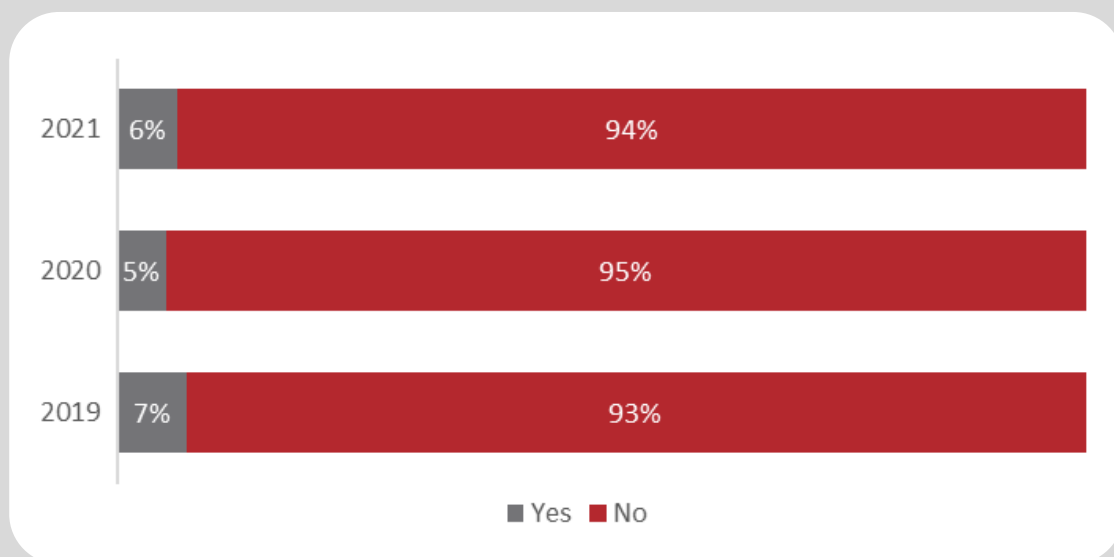
\* The 7% of Relevant Persons where Customer Due Diligence does not apply are Representative Offices.

The AML Return includes elements of self-assessments, including the views of each reporting firm's own senior management about the quality of their firms' anti-financial crime framework. As shown above, the management of virtually all firms assert that they are satisfied. However, these optimistic views generally do not reflect the findings from recent risk assessment visits and thematic reviews that the DFSA has conducted independently of the firms' management. The DFSA reminds senior management to take its findings into account when considering their own-self assessment.

## NEW PRODUCTS OR SERVICES

The annual AML Returns provided the DFSA with data on the development of any new products or services. Since 2019, the DFSA observed that the majority of Relevant Persons who reported the development of new products or services mainly related to new business practices, including new delivery mechanisms, channels and partners. This is a focus area for the DFSA, and we will continue to monitor how it evolves.

## RELEVANT PERSONS REPORT THE DEVELOPMENT OF NEW PRODUCTS OR SERVICES



## TYPES OF CUSTOMERS AND THEIR ACTIVITIES

The annual AML Returns provided the DFSA with data on the number of customers, types of customers and the basis upon which those customers are classified as politically exposed persons (PEPs).

In 2021, Relevant Persons reported 111,178 customer relationships. This is an increase of 40% in the number of customers since 2019. It also worth noting that there has been an 4.5% increase in the number of reporting entities<sup>4</sup>.

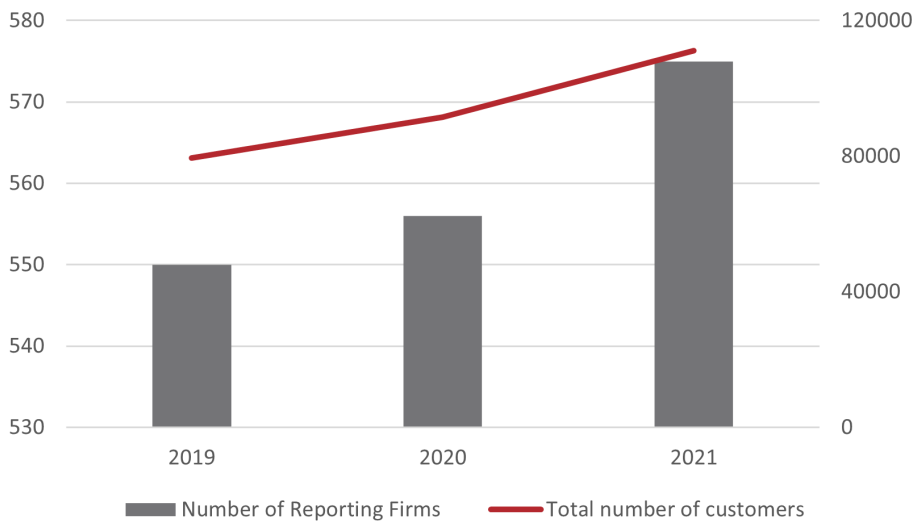
Based on the 2021 AML Return data, customers who were classified as natural persons accounted for 52% of the total customers, reflecting a 24% increase since 2019. Legal persons accounted for 47% of the total customers, and legal arrangements accounted for 1%. Relevant Persons also reported that 33% of their customers who were classified as legal persons and/or legal arrangements were deemed to have complex ownership structures<sup>5</sup>.

The number of customers served continued to rise, from 79 thousand in 2019 to 92 thousand in 2021, demonstrating continued interest in drawing on services from the DIFC even given the impact of the COVID-19 global pandemic. In this regard, the DIFC's standing

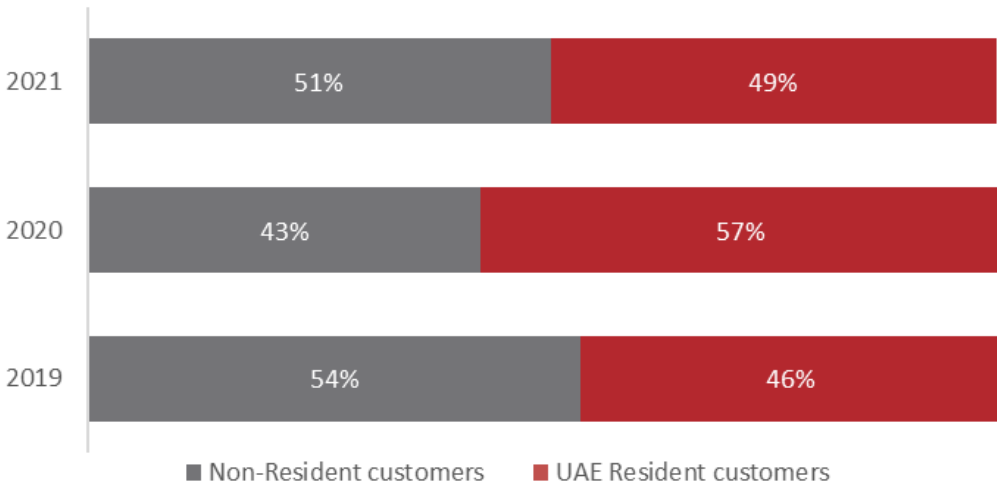
<sup>4</sup> For comparison purposes, this number excludes firms that are licensed to operate Representative Offices since they are prohibited from on-boarding customers.

<sup>5</sup> The DFSA defines complex structures as legal persons or legal arrangements with two or more layers. This was the first time this information had been reported.

as a hub for global finance is evident in the sizeable portion of customers who are non-resident in the UAE: for the period covered by this report, non-resident customers have varied from 54% in 2019 to a low of 43% in 2020. In 2021, non-residents comprised 51% of total customers. The percentage of customers considered to be politically exposed has declined to 11% in 2021 compared to 13% in 2019, which suggests a proportional reduction in exposure to PEPs.

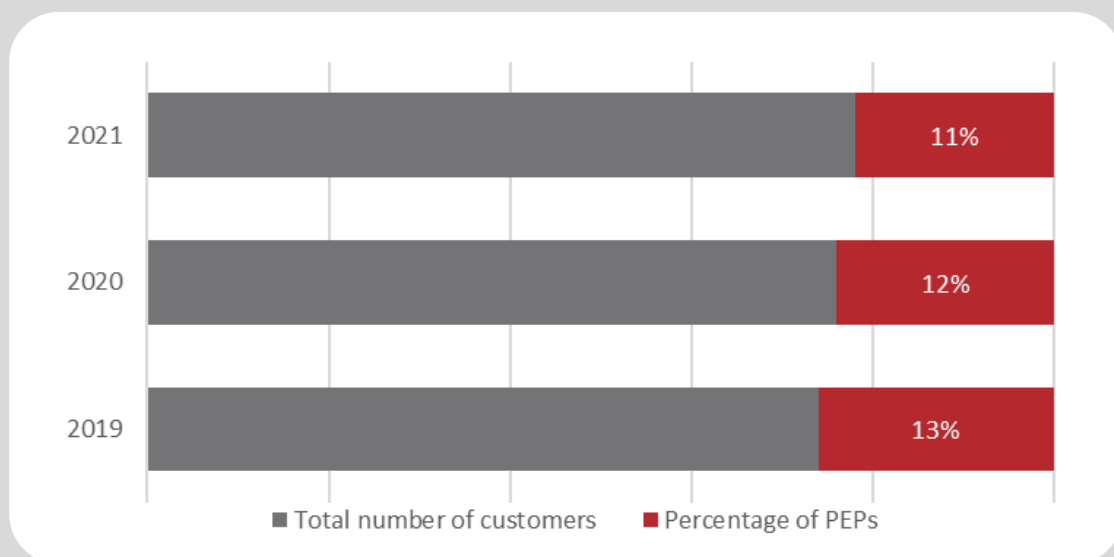


### RELEVANT PERSONS REPORT THE DEVELOPMENT OF NEW PRODUCTS OR SERVICES





## PERCENTAGE OF CUSTOMERS WHO WERE IDENTIFIED AS POLITICALLY EXPOSED PERSONS



## REGISTRATION ON THE FIU'S GOAML PLATFORM

All Relevant Persons are required to register on the UAE Financial Intelligence Unit's goAML platform for the purposes of making suspicious activities reports under Rule 13.3.1(c) of the AML Module of the DFSA Rulebook and federal AML legislation.

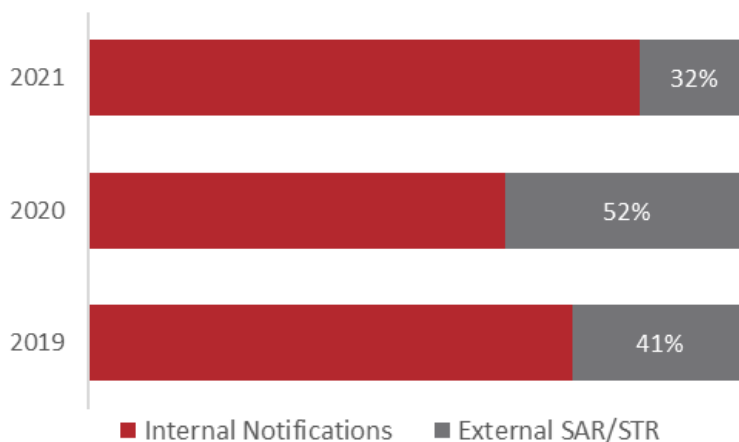
To verify that Relevant Persons are meeting the above obligations, the DFSA requires Relevant Persons to confirm in writing that they have fully completed the registration for access to the platform for the external reporting of SARs. By virtue of that registration, automatic alerts are also enabled by the UAEIEC in relation to individuals or entities listed for sanctions monitoring.

For the reporting period, the DFSA notes that 99% of Relevant Persons have now confirmed full completion of the goAML platform registration process. The remaining 1% have completed the process following the submission of the 2021 AML Return. The DFSA continues to monitor the registration process on a quarterly basis.

## SAR/STR REPORTING

Based on our analysis, the DFSA observes that the number of internal SARs reported increased by 27% from 2019 to 2020, though this decreased in 2021 to 32%. Furthermore, based on our analysis, the majority of all SARs in 2021 originated as a result of internal

monitoring systems, i.e., transaction monitoring/adverse media/screenings followed by internal referral/notification, such as employee referral, compliance review, group compliance, as illustrated in the chart below. This trend both in the increase in the number and the proportion of SARs/STRs generated in 2021 suggests greater sensitivity within firms to “red flags” regarding potentially suspicious transactions.



At the same time, the DFSA also observed that the number of SARs reported to the FIU increased in 2020 but is now back to 2019 levels<sup>6</sup>. When firms generate internal reports of potentially suspicious transactions, supervisors expect firms to evaluate those reports

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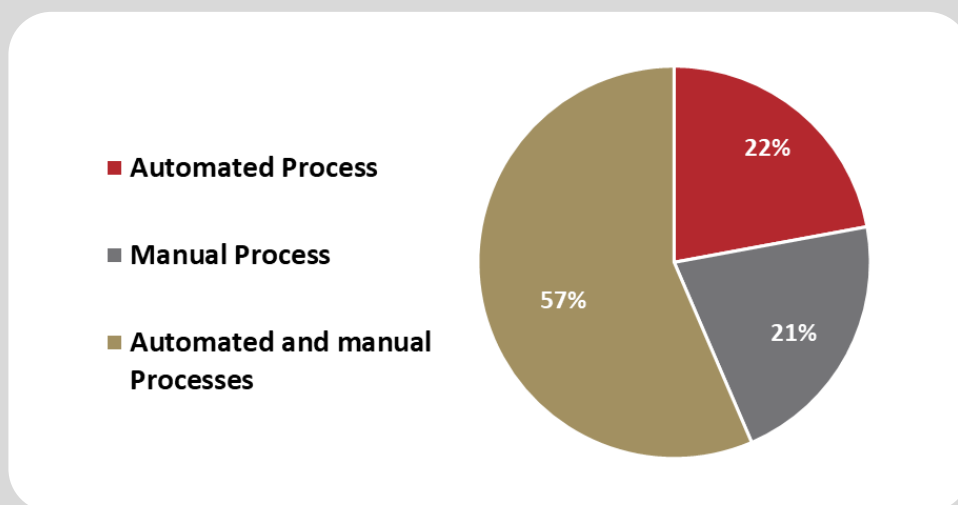
<sup>6</sup> SAR/STR data cover the annual AML Return reporting periods.

carefully to determine whether these transactions represent false positives or, alternatively, leave enough questions unanswered that they should properly be reported to the appropriate authorities. This is a focus area for the DFSA, and we will continue to monitor compliance with the set obligations.

## TARGETED FINANCIAL SANCTIONS (TFS)

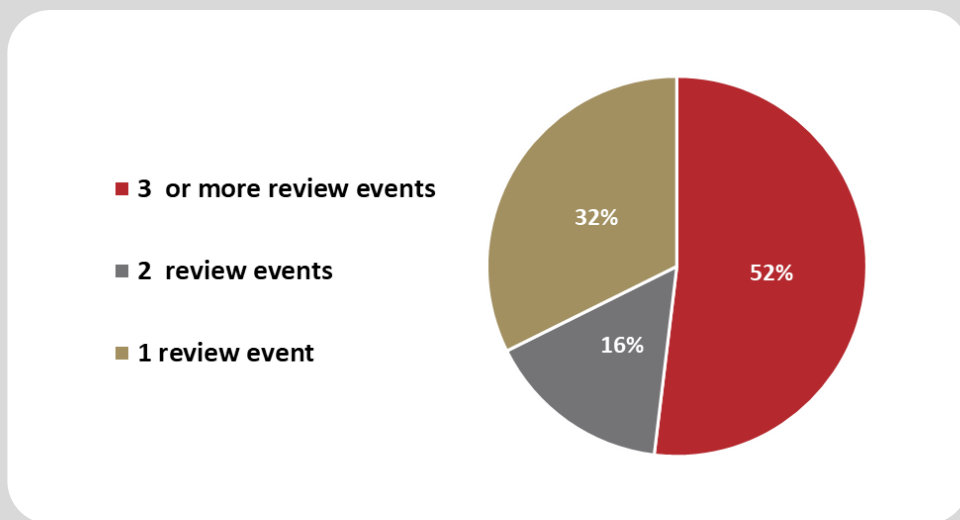
In order to gain further insight into Relevant Persons compliance frameworks, the DFSA enhanced the 2021 AML Return to include data points on the TFS framework. This is the first set of these data points received. Based on our analysis, the TFS compliance level across Relevant Persons is as follows:

### HOW TARGETED FINANCIAL SANCTIONS ARE UNDERTAKEN



Relevant Persons have also provided data in relation to a question added to our regulatory return for the first time in 2021 on how often they screen customer databases, which reveals a number of embedded screening processes that firms employ. For example, firms report practices including overnight batch screening, upon notification by regulatory authority via updated sanctions lists and alerts, specific trigger events and periodic reviews embedded as part of the compliance framework. The aggregated data reveal that more than 50% of Relevant Persons have embedded a combination of three or more of the above-described events in their compliance framework. This is a focus area for the DFSA and we will continue to monitor compliance with the set obligations and the evolution of firms' practices.

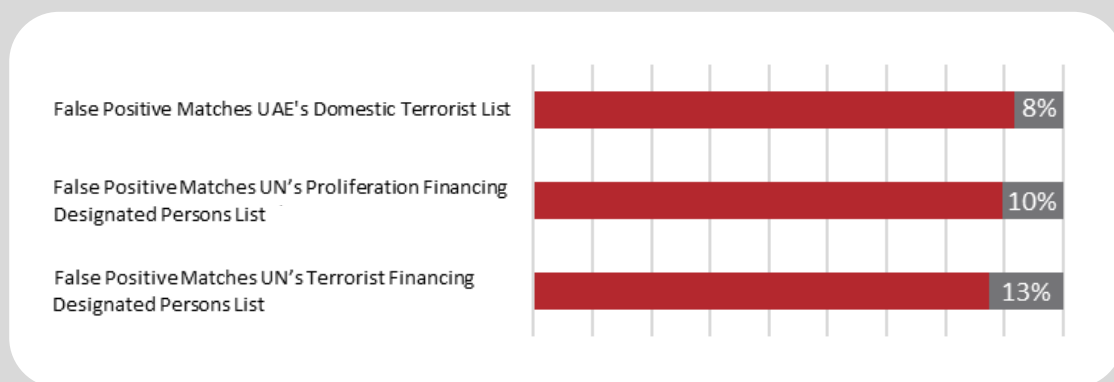
## FREQUENCY OF SCREENING EVENTS AND FINDINGS



Relevant Persons also provided data in relation to a question added for the first time in 2021 on their practices regarding the screening of beneficial owners against the UN Terrorist Financing Designated Persons List, the UN Proliferation Financing Designated Persons List and the UAE list of Designated Terrorist Individuals, Organisations and Groups. The aggregated data revealed that the majority of Relevant Persons screen all beneficial owners against these lists. The small number of Relevant Persons reporting that they do not screen beneficial owners include Representative Offices, which are not permitted to interact with customers, and single-family offices, which tend to be small. The DFSA is engaging with those firms to understand their practices and risks.

In relation to false positive matches, the aggregated data revealed that, during the reporting period, 13% of Relevant Persons had made a false positive match against the UN Terrorist Financing Designated Persons List, 10% against the UN Proliferation Financing Designated Persons List and 8% against the UAE list of Designated Terrorist Individuals, Organisations and Groups.

## FALSE POSTIVE MATCHES



Furthermore, the aggregated data also revealed that, during the reporting period, no Relevant Persons have identified (true) positive matches against the UN Terrorist Financing Designated Persons List, the UN Proliferation Financing Designated Persons List and the UAE Domestic Terrorist Designated Persons List. This finding may not be surprising as the firms based in the DIFC largely focus on wholesale finance rather than activities serving individuals. As 2021 was the first year that the DFSA gathered this statistic from Relevant Persons on potential matches against various designated persons lists, we will monitor trends in reported matches and engage with firms to test their process for determining that matches are false.

# ENFORCEMENT ACTIVITY

During 2020 and 2021, the DFSA continued to prioritise cases that dealt with financial crime risks in line with the DFSA's risk tolerance.

The DFSA has noticed a significant increase in unlicensed financial services activity in the DIFC during the above period. This unlicensed activity poses particular financial crime risks as the activities are not subject to DFSA supervisory oversight. The unlicensed activity included both:

- activity which was carried out by DFSA-regulated firms or firms related to DFSA-regulated firms. These firms are licensed by the DFSA but have engaged in activity beyond the scope of their respective licenses or have been knowingly involved in the unauthorised activity of related unauthorised firms. The DFSA has taken enforcement action against such firms by imposing significant financial penalties on them. The DFSA has also taken action against the individuals involved in the activity by imposing significant financial penalties and restricting them from being involved in financial services in the DIFC; and
- activity which was carried out by firms which are not regulated by the DFSA. The DFSA has commenced a number of investigations and is also following a number of lines of enquiry into such firms and their activities carried on in or from the DIFC.

In addition, the DFSA issued 19 consumer alerts during the above period about scams and other fraudulent activity. The types of scams that came to the attention of the DFSA continued to include advance fee fraud, and scams in which the identities of the DFSA, DIFC and firms within the DIFC and/or their employees were stolen or misused.

The DFSA, in line with its mandate, continued to provide assistance to UAE authorities and other regulators in relation to ongoing matters within their respective jurisdictions.

All DFSA Enforcement action is published on the DFSA's website under Enforcement Decision Notices.

# DIFCA/ROC PROGRESS

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## REGULATORY APPROACH

### REGULATORY MANDATE

On behalf of the DIFC Registrar of Companies (RoC), the Dubai International Financial Centre Authority (DIFCA) has been mandated to monitor non-financial and retail services activities in the DIFC.

The key regulatory responsibilities undertaken by the RoC include enhanced monitoring and enforcement of DIFC Laws and Regulations, as well as the federal AML/CTF laws, and similar financial crime detection and prevention requirements or best practices that are applicable in the DIFC. This is all part of its comprehensive programme that supports a strategic objective of effective regulatory compliance.

### INITIATIVES TO ADDRESS FINANCIAL CRIME RISK

Since 2019, and in line with its mandate from the RoC, the following initiatives were undertaken:

#### ENHANCED THE KNOW YOUR CUSTOMER (KYC) ASSESSMENT PROCESS

A risk-based model and methodology were implemented by digitalising the due diligence process based on specific key criteria. The process requires:

- robust review of every non-financial services company formation applicant. This includes review of UBO information, financials of any relevant and related party to the application, information on source of wealth and funding of the entity by and in addition to UBOs, and any other information deemed necessary to risk rate the application; and
- assessment by the DIFC Relationship Manager that includes qualifying the applicant(s) based on transparency and research regarding the proposed company, providing a view of its potential stability and on its reasons for coming to DIFC.

To enhance effectiveness of the process, the DIFCA AML compliance procedures are reviewed on an annual basis to continuously improve and implement any new requirements, in accordance with latest FATF Recommendations and Reports, market trends, and international best practices.



## **CONDUCTED THEMATIC ASSESSMENT(S) ON KEY RISK AREAS IDENTIFIED**

The outcome of thematic assessments showed where gaps should be mitigated, and further provided a basis on which to support entities' education and understanding of applicable regulations and any implementing requirements imposed by the ROC. The RoC also issued in-depth, user-friendly guidance and self-assessment tools on the DIFC website to correct deficiencies found through the thematic assessments, leading to better, more effective regulation and understanding of the importance of meeting AML/CTF and CPF obligations. The analytics gleaned from the thematic assessments show procedural flaws and patterns that lead to non-compliance and identification of new issues, as well as the opportunity to investigate further the entities creating such risk. In certain cases, this process led to opportunities for supervisory support and in where necessary for disciplinary measures to be applied.

## **ENFORCEMENT OF UBO REGULATION**

The RoC applied enforcement actions in cases of material non-compliance with the DIFC UBO Regulations 2018, by way of significant fines, business activity suspension or removal of operating licences, resulting in full compliance with these Regulations. A total of 816 fines were issued by the ROC in 2021. These fines were primarily for non-compliance with the requirement to maintain a UBO register, but also related to other areas of non-compliance determined through analytics described above, including failure to appoint auditors where required.

## **PARTICIPATION IN NATIONAL SUB-COMMITTEE OF COMPANIES REGISTRARS**

The RoC has been an active participant in this national sub-committee. In this role, the RoC provides feedback and updates on DIFCA developments around effectiveness and compliance to support the UAE efforts.

## **REGULATORY APPROACH IN RELATION TO TRANSPARENCY AND BENEFICIAL OWNERSHIP**

In 2021, the Regulatory Compliance Team was reorganised to implement the Fully Effective Monitoring Mechanism requirement of another financial crime prevention measure, the UAE Economic Substance Regulations. The main objective of the re-structure was to deploy existing and new RoC resources more efficiently, achieving the following:

- effective implementation of planned and ad hoc monitoring updates applicable to DIFCA (inclusive of Economic Substance Regulations, Common Reporting Standard Law and Regulations, etc.);
- enhanced, digitalised monitoring and enforcement methods, such as use of data analytics to identify non-compliance, to enable partially automated compliance supervision, which necessarily results in virtually irrefutable, documented evidence of regulatory effectiveness; and
- identification of practical, impactful methods for training entities and their staff on proper implementation of various compliance requirements.

In its commitment to the transparency and Beneficial Ownership requirements, the RoC took the following actions:

- An entity cannot be incorporated in the DIFC if UBO information is not provided as per the DIFC UBO Regulations (2018). Additionally, the entity is required to maintain a register, produce it upon request, and in any case confirm on an annual basis that its UBO information is up to date;
- DIFC has also assured the availability of UBO information for all its registered entities by tying it to permission to renewing its operating licence if not provided. To date, the RoC has issued over 150 fines in relation to failure to maintain UBO Information;
- DIFC enhanced its on-boarding process in relation to nominee arrangements, to capture the existence and associated risk of any such relationship. Additionally, DIFC companies must disclose their nominee directors soon after entity incorporation or from the date of the change to add the nominee. A similar process is being developed for the inspections process and the annual Confirmation Statement requirements;
- DIFC assesses on an ongoing basis the residual risk of legal persons and arrangements based on various factors such as product delivery channels, geographical exposure of legal and politically exposed persons, sources of income, types of business activities. On an annual basis, DIFC reviews the criteria and draws references from the UAE risk typology report and other international papers, and amends its risk assessment criteria if required;

- as part of business entity licensing and on-boarding, all entities are required to provide comprehensive information and documentation on all key stakeholders (including UBO). An entity cannot be incorporated if the information is not provided or does not appear to be valid. For key stakeholders, supporting documents such as passport copies are required to be certified to confirm authenticity of the document and good standing of the stakeholder; and
- all entities are required to keep UBO and other shareholder information up to date and to regularly confirm that the information contained in its RoC database, which is reflected on the DIFC public register, is valid. If the information has expired, the entity is restricted from renewing its licence until properly updated information is made available.



**FOR GENERAL ENQUIRIES**

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