Administrative Measure Publication Notice

This Notice is being published by the Financial Intelligence Analysis Unit (FIAU) in terms of Article 13C(2) of the Prevention of Money Laundering Act (PMLA) and in accordance with the policies and procedures on the publication of AML/CFT measures established by the Board of Governors of the FIAU. This Notice provides select information from the FIAU's decision imposing the respective administrative measures and is not a reproduction of the actual decision.

DATE OF IMPOSITION OF THE ADMINISTRATIVE MEASURE:
16 September 2022

RELEVANT FINANCIAL BUSINESS CARRIED OUT:
Corporate Service Provider – Firm/Company

CASE 1:

SUPERVISORY ACTION:
Off-site compliance review carried out in 2020.

DETAILS OF THE ADMINISTRATIVE MEASURES IMPOSED:
Administrative Penalty of €49,129, Reprimand and a Follow-up Directive in terms of Regulation 21 of the Prevention of Money Laundering and Funding of Terrorism Regulations (PMLFTR).

LEGAL PROVISIONS BREACHED:

- Regulation 5(1) of the PMLFTR and Section 3.3 and 8.1 of the Implementing Procedures (IPs),
- Regulation 5(5)(a)(ii) of the PMLFTR and Section 3.5.1, 3.5.1(a), 3.5.3 and 3.5.3(a) of the IPs,
- Regulation 7(1)(c) of the PMLFTR, and
- Regulation 7(1)(d) and 7(2)(a) of the PMLFTR and Section 4.5.2 and 4.5.3 of the IPs.

REASONS LEADING TO THE IMPOSITION OF THE ADMINISTRATIVE MEASURES:

Business Risk Assessment (BRA) - Regulations 5(1) of the PMLFTR and Section 3.3 and 8.1 of the IPs

The compliance review identified serious shortcomings in the Company's BRA methodology applicable at the time of the examination (2020 BRA). Through such shortcomings, the FIAU's Compliance Monitoring Committee (the Committee) determined that the Company failed to draw up an adequate BRA that truly reflects the real threats and vulnerabilities of the business. This consequently affected the nature and level of mitigating measures that are being applied by the Company. Some of the shortcomings noted in the Company's BRA are being illustrated hereunder:

- Despite the Company's BRA having identified Money Laundering and Financing of Terrorism (ML/FT) threats and vulnerabilities, a quantitative approach as part of its assessment and ultimately in its final risk determination was not undertaken.

- The BRA also failed to take into consideration the ML/FT threats originating from the provision of the different types of corporate services offered. This is required as the ML/FT risks and responsibilities arising from offering registered office and company secretarial services are not the same as those arising from directorship services. This was particularly important since the Company had a significant number of customers to which it provided Directorship services. Therefore, it is essential that the BRA assesses these services in isolation and not collectively, so as to be in a position to clearly identify the threats and vulnerabilities of each and every service and subsequently apply adequate and commensurate measures to mitigate the same.

- Despite referring to a reputable source in conducting its jurisdiction risk assessment, the Company was required to ensure that such assessment is in line with local AML/CFT obligations, particularly with Chapter 8 of the IPs. Instead, the Company's BRA allowed instances within which non-reputable jurisdictions were inadequately risk assessed as they were assigned a risk rating below high risk. Despite the Company's statement that such jurisdictions were borderline to being rated as High-Risk, the classification adopted by the Company contradicted the requirement established in Section 8.1 of the IPs in that such jurisdictions were to be rated as High risk, this in view of the heightened risk of ML/FT identifiable with these jurisdictions at the time.

Notwithstanding the above, the Committee positively acknowledged the Company's statement that the Company's subsequent BRAs have taken into account additional guidance issued by the FIAU throughout the years and the recommendations made by the FIAU as part of the 2020 compliance review. Despite the remediation undertaken, the Company's BRA applicable at the time of the examination was inadequate. Hence, the Committee concluded that at the time of the examination, the Company was in **breach of Regulation 5(1) of the PMLFTR and Section 3.3 and 8.1 of the IPs.**

Customer Risk Assessment (CRA) - Regulation 5(5)(a)(ii) of the PMLFTR and Section 3.5.1, 3.5.1(a), 3.5.3 and 3.5.3(a) of the IPs

The compliance examination identified systemic shortcomings pertaining to the Company's Customer Risk Assessment (CRA) methodology. This particularly since all customers reviewed as part of the compliance review were all assigned a low risk rating, despite having elements which should have prompted the Company to assign a different risk rating. Some examples are being relayed hereunder:

- In one file relating to a holding company which was originally incorporated in Panama and subsequently redomiciled to Malta, higher risk elements included the BO of the company being a Panamanian individual (national & resident) who was acting as nominee of and trustee for and on behalf of a Brazilian national beneficiary. The expected yearly turnover was deemed to be €10 million, and the Company was also to provide directorship services to this customer. All of these elements portray higher ML/FT risks, and hence do not justify the low-risk rating attributed by the Company to this customer.

- In another file, the CRA did not account for the higher risk elements emanating from the provision of directorship services to an investment company. Nor did it refer to the higher risk elements in view of the value of investments held (net assets in excess of $5m) in other foreign companies and the type of investments which include the banking sector and the petroleum industry. Particularly, the petroleum industry is commonly associated with a higher risk of bribery and corruption. Hence, such factors should have merited a higher risk rather than the overall low rating assigned by the Company.

- In another three files, all of which formed part of the same group of companies, higher risk elements were not considered in the final CRA rating. This since, the Company was providing directorship services to all three customers, all of which were operating within the gaming sector and also expected transactions with a sister company based in a non-EEA jurisdiction prone to a higher level of ML/FT risk. Hence, these elements should have prompted the Company to risk rate these customers differently and ensure that the ML/FT exposure is adequately identified, and the appropriate measures are taken to mitigate the risks effectively.

In addition, the Company was also found to having failed to carry out a CRA prior to entering into a business relationship with three of its customers.

Finally, while positively acknowledging that the Company's remediation had already started to be implemented in virtue of the enhancements to its CRA system, the FIAU cannot overlook the systematic deficiencies identified within the Company's CRA methodology. Particularly, the Committee noted the Company's lack of consideration to important risk factors including the provision of directorship services and the risks to which certain customers exposed the Company through the services offered. Hence, the Committee determined that the Company has been for a substantial period of time adopting an inadequate CRA methodology, and consequently found the Company to be in **breach of Regulation 5(5)(a)(ii) of the PMLFTR and Section 3.5.1, 3.5.1(a), 3.5.3 and 3.5.3(a) of the IPs**.

Purpose & Intended Nature - Regulation 7(1)(c) of the PMLFTR

The Committee positively acknowledged that for all the files reviewed, throughout the duration of the business relationship (post on boarding), the Company was able to eventually demonstrate its knowledge on the purpose and intended nature of the business relationship. Notwithstanding, the FIAU cannot ignore the fact that in two files, the Company failed to acquire sufficient information on the purpose and intended nature of the business relationship prior to the establishment of the business relationship (at on-boarding). Hence the Company is found in **breach of its legal obligations in terms of Regulation 7(1)(c) of the PMLFTR.**

Transaction Monitoring - Regulation 7(1)(d) and 7(2)(a) of the PMLFTR and Section 4.5.2 and 4.5.3 of the IPs

The Compliance examination also identified serious shortcomings in relation to the Company's obligation to scrutinise transactions undertaken by its customers. For five customer files reviewed, the Company did not comprehensively understand the reasons for certain transactions being undertaken. As an example:

- In one file, the FIAU flagged an inward payment of just under $700,000 received by the customer from a third-party company. The customer is an investment company holding a number of investments in other foreign companies trading in different markets including the petroleum industry. To justify the inward transaction, the Company provided documentation pertaining to a loan agreement. However, neither document provides any rationale as to why the customer was receiving the said amount, the relationship with the said company, the purpose of the loan and any detail to ensure that the activity undertaken by the customer is in line with its expected activity.

- In another file, an outward payment of just over €800,000 undertaken by the Company's customer to its parent entity was noted. The Company explained that such transaction related to a number of invoices and to support such claim provided a number of invoices along with a service agreement entered into between the two parties. However, the Company never questioned why as per the service agreement, services were to be provided by the customer to the parent entity, however the invoices provided illustrate the contrary. Particularly, the invoices provided illustrate services provided by the parent entity to the customer. Therefore, the Committee noted that relying on the service agreement and the invoices provided is thus not possible since such contradiction leads one to question the relevance and reliability of all such documentation. Hence, the Company was required to scrutinize further the said agreement and further ascertain the legitimacy of the services being received by the customer.

- Another file onboarded by the Company in 2018 underwent a change in shareholding merely a month and a half later. The customer was previously owned by an EU based corporate shareholder which transferred all its shares to a non-EEA national. The said share transfer was affected on the same day that the transferee had entered into a 'Call Option' agreement with the transferor. This call option agreement provided the EU based shareholding entity (being the company which sold off the shares) the right to require the non-EEA national (optionor who acquired the shares) to sell, assign and transfer back all the shares onto the Swedish Company, this for the aggregate purchase price significantly lower than the share price. Practically the transfer back to the previous owner could take place for a minimal value of €1.

When questioned on the rationale behind such arrangement, the Company explained that the selling of the Customer's shares was only possible upon the condition that the seller imposed on the buyer through the call option agreement, therefore still not explaining the rationale behind it. The Committee was indeed concerned to note that the Company merely relied on this explanation to explain the motive behind a change in shareholding of its customer. The Company failed to clearly understand the true motive behind the EU shareholding company in that despite transferring its shares, it still maintained the right to get back the shares, within a specified timeframe and for a significantly lower price. The Company was expected to question the rationale behind the change in the customer's majority owner while at the same time, the previous owner retained the right to request the new owner to transfer the shares back. This does lead to possible risks of having merely a paper transfer with beneficial ownership risks not being well catered for.

In view of the failures in relation to the Company's obligation to carry out effective scrutiny of transactions, the Company was deemed to be in **breach of Regulation 7(1)(d) and 7(2)(a) of the PMLFTR and Section 4.5.2 and 4.5.3 of the IPs.**

ADMINISTRATIVE MEASURES TAKEN BY THE FIAU'S COMPLIANCE MONITORING COMMITTEE:

After taking into consideration the abovementioned breaches by the Company, the Committee decided to impose an administrative penalty of forty-nine thousand one hundred and twenty-nine euro (€49,129) with regards to the breaches identified in relation to:

- Regulation 5(1) of the PMLFTR and Section 3.3 and 8.1 of the Implementing Procedures (Ips),
- Regulation 5(5)(a)(ii) of the PMLFTR and Section 3.5.1, 3.5.1(a), 3.5.3 and 3.5.3(a) of the Ips, and
- Regulation 7(1)(d) and 7(2)(a) of the PMLFTR and Section 4.5.2 and 4.5.3 of the Ips.

In addition to the above, the Committee imposed a Reprimand in relation to the breaches identified for the Company's failures in terms of Regulation 7(1)(c) of the PMLFTR.

The Committee positively acknowledged the actions already taken by the Company and the actions planned to be taken in order to remediate the failures identified during the compliance review. Said enhancements include and are not limited to; the implementation of a revised Business Risk Assessment, enhancements to the CRA methodology and transaction monitoring enhancements. The Committee expects the Company to ensure that the remediation, both that which has already been undertaken and that still planned to be undertaken, is effectively implemented. Hence, to ensure that the Company's remediation is adhered to, the Committee also served the Company with a Follow-Up Directive. Through the Directive, the FIAU is requesting the Company to make available a detailed action plan catering for all the breaches identified by the Committee, along with any other relevant enhancements the Company has implemented or plans to implement. The action plan is to include clear reference as to when the actions are to be completed, where applicable to provide supporting evidence, and is to explain the points referred to above.

In determining the appropriate administrative measures to impose, the Committee took into consideration the representations submitted by the Company, together with the remedial actions that the Company had already started to implement. Also, the nature and size of the Company's operations and the overall impact that the AML/CFT shortcomings of the Company had or could have had both on its own operations and on the local jurisdiction in terms of risks. The seriousness of the breaches identified together with their occurrence were also considered by the Committee in determining the administrative measures imposed. The overall good level of cooperation by the Company has also been factored in by the Committee in its final determination.

Finally, the Company has also been duly informed that in the eventuality that it fails to provide the above-mentioned action plan and to make available the requested supporting documentation within the specified deadlines, the Company's default will be communicated to the Committee for its eventual actions. This including the possibility of the imposition of an administrative penalty in terms of the FIAU's powers under Regulation 21 of the PMLFTR.

Key Take aways:

- It is not sufficient for subject persons to merely draw up an inventory of the threats or vulnerabilities in its BRA, however a quantitative understanding of the threats or vulnerabilities are, should also be factored in. Only through such quantitative assessment can subject persons thoroughly understand the extent of the exposure to particular risks, their materiality, and the level of impact should they materialise.

- When establishing their CRA methodologies, subject persons are to ensure that when risk assessing their customers, reference is made to factors that are considered to be of higher ML/FT risk as outlined under by section 3.2 of the IPs. Some of which include and are not limited to:
    - whether the customer or its ownership and control structure involve bearer shares or nominee/ fiduciary shareholders, and
    - the customer is not resident in the subject person's jurisdiction and there is no sound economic and lawful reason for seeking services or products from the subject person.

- When monitoring transactions, subject persons are to ensure that any additional documentation and/or explanations required to substantiate the rationale behind a particular transaction or set of transactions are adequately scrutinized and understood. This to ensure that the activity undertaken is indeed legitimate and in line with the expected activity of the particular customer. Should the additional documentation and or explanations provided by the customer further shed doubts on the rationale of the flagged transaction or set of transactions, subject persons are required to take a proactive approach and further ascertain the legitimacy of the transaction and activity undertaken, this either by requesting for additional documentation and/or explanations or through other means available to the subject person. Finally, based on the available information, should the subject person, know, suspect, or, has reasonable grounds to suspect that either a transaction, including attempted transaction(s), may be related to ML/FT, or a person may have been, is or may be connected with ML/FT or ML/FT has been, is being or may be committed or attempted, the MLRO must file an STR with the FIAU.

CASE 2:

SUPERVISORY ACTION:
Targeted compliance review carried out in 2021.

DETAILS OF THE ADMINISTRATIVE MEASURES IMPOSED:
Administrative Penalty of €12,253 and a Reprimand in terms of Regulation 21 of the Prevention of Money Laundering and Funding of Terrorism Regulations (PMLFTR).

LEGAL PROVISIONS BREACHED:

- Article 30C of the PMLA (Currently Article 30D of the PMLA) and the proviso to Regulation 11(2) of the PMLFTR,
- Regulation 7(1)(c) of the 2008 PMLFTR, and
- Regulation 15(3) of the PMLFTR and Section 6.3 of the IPs of 2017[1].

REASONS LEADING TO THE IMPOSITION OF THE ADMINISTRATIVE MEASURES:

Directive applicable to all subject persons when dealing with natural or legal persons having connections with Iran - Article 30C of the PMLA (Article 30D of the PMLA currently in force) and the proviso to Regulation 11(2) of the PMLFTR

On 17 December 2019, in terms of the FIAU's powers under Article 30C of the PMLA and the proviso to Regulation 11(2) of the PMLFTR, the FIAU issued a directive regarding transactions connected with Iran. The directive required all subject persons to inform the FIAU of every transaction connected with Iran and to only execute transactions connected with Iran if there is no written opposition by the FIAU within five working days from when the aforementioned notification is sent to the FIAU. Where it was not possible to refrain from performing the transaction prior to informing the FIAU, the subject person was expected to inform the FIAU immediately after the transaction was affected.

In one file it was noted that the Company's customer had placed an order of goods to a client located in Iran, this however prior to the imposition of the FIAU's directive on Iran. The goods were however due for delivery following the directive and so was the payment for such order. Despite the Company being fully aware of the economic activity undertaken by its customer with Iran, the Company still failed to inform the FIAU of such transaction. However, the Committee also positively acknowledged the detailed information collected by the Company in explaining the respective transaction. In the taking of its decision as to the administrative measure to impose, the Committee also noted that the ML/FT risks involved in the transactions were not high. However, the Committee cannot disregard the fact that the customer's connection with Iran was still evident following the imposition of the FIAU's directive and that the Company failed to inform the FIAU about such transactions.

In view of the above, the Company was found in **breach of Article 30C of the PMLA (Article 30D of the PMLA currently in force) and the proviso to Regulation 11(2) of the PMLFTR for its failure to abide to FIAU's directive**.

[1] Currently Section 5.5 of the Implementing Procedures last amended in 2021

Purpose & Intended Nature - Regulation 7(1)(c) of the 2008 PMLFTR

The Committee positively acknowledged that for the files reviewed, throughout the duration of the business relationship (post on boarding), the Company was able to demonstrate its good knowledge on the purpose and intended nature of the business relationship and that it had a thorough understanding of its customers and their activities. Notwithstanding, the FIAU cannot ignore the fact that in these files, the Company failed to acquire sufficient information on the purpose and intended nature of the business relationship prior to the establishment of the business relationship (at on-boarding). Hence the Company is found in **breach of its legal obligations in terms of Regulation 7(1)(c) of the 2008 PMLFTR.**

Failure to submit an STR and/or SAR - Regulation 15(3) of the PMLFTR and Section 6.3 of the IPs of 2017

The targeted review identified a serious shortcoming in that on the basis of all the information held at its disposal, the Company failed to submit a suspicious report to the FIAU in view of the suspicion of ML/FT activity undertaken by its customer in one particular file. An illustration of some of the red flags noted which should have prompted the Company to submit and STR/SAR are:

- The complexity of the structure and set up involved, in that the customer's shares were held in a foundation for the benefit of two non-EEA individuals. At the same time the foundation was the shareholder of another Maltese Company holding a non-Maltese gaming license which entered into a shared conduct agreement with a non-EU licensed gaming entity.

- The structure included a number of jurisdictions involved including EU, non-EU and higher risk jurisdictions.

- The structure and modus operandi led to the same non-EEA nationals. Hence, funds were ultimately flowing to the said non-EEA individuals as the said individuals are also the BOs of the foundation within the structure.

- The Maltese Company with a non-Maltese gaming license had a restriction, not allowing the generation of revenue outside the country of the license being issued. The contract with the non-EU licensed gaming entity meant that this was not being honoured. The Company had sufficient information to notice that the customer was created to aid in the circumvention of such a restriction leading to the legitimization of revenue earned from such activity. This legitimization took the form of a number of loans between the parties.

- The customer was incurring expenses emanating from agreements entered into between itself and two non-EEA companies. The services supposedly offered by the non-EEA companies are a replica to the services presumably being offered by the customer itself. Also, despite being provided with invoices for the said services, the amounts of the invoices did not tally with the total expenses incurred. The description provided within the said invoices were also vague and did not provide any clarity as to the services actually provided by the non-EEA companies. Also, some of the services outlined in the invoices are not in line with the details of the services as per the agreements entered into.

- The value of funds involved in the structured transactions, including more than €2 million in loans/ borrowings between the Maltese entity with a non-Maltese gaming license and the customer, and accounting of revenue share of over €2 million between the non-EU licensed gaming company and the customer. Also, dividend payments flowing into the foundation in excess of €1 million and additional expenses incurred by the customer which are for services offered by two non-EEA companies in excess of €1 million.

- The 'transactions' between the entities and the way money was merely accounted for but not truly passing through, given that the customer did not have a bank account. Also, the way as to how the customer was paying for the expenses incurred remains unclear, again in view of it not having a Bank account.

In view of the above, the Company was found in breach for failing to submit a suspicious report to the FIAU in view of the suspicion of ML/FT activity undertaken by its customer in line with **Regulation 15(3) of the PMLFTR and Section 6.3 of the IPs of 2017.**

ADMINISTRATIVE MEASURES TAKEN BY THE FIAU'S COMPLIANCE MONITORING COMMITTEE:

After taking into consideration the abovementioned breaches by the Company, the Committee decided to impose an administrative penalty of twelve thousand two hundred and fifty-three euro (€12,253) with regards to the breaches identified in relation to:

- Regulation 15(3) of the PMLFTR and Section 6.3 of the IPs of 2017

In addition to the above, the Committee imposed a Reprimand in relation to the breach identified pertaining to the directive applicable to all subject persons when dealing with natural or legal persons having connections with Iran under Article 30C of the PMLA (Currently Article 30D of the PMLA) and the proviso to Regulation 11(2) of the PMLFTR. A reprimand was imposed in this case as the amounts passed were of a low amount and although the payment had occurred following the imposition of the Directive of 2019, the placement of the order had taken place prior to the Directive. The Company was also sufficiently knowledgeable on the transaction effected. Thus, it was determined that the ML/FT risks materialising from this transaction were low.

A Reprimand was also imposed in relation to the breaches identified for the Company's failures in terms of Regulation 7(1)(c) of the 2008 PMLFTR.

In determining the appropriate administrative measures to impose, the Committee took into consideration the representations submitted by the Company, together with the remedial actions that the Company had already started to implement. Also, the nature and size of the Company's operations and the overall impact that the AML/CFT shortcomings of the Company had or could have had both on its own operations and on the local jurisdiction in terms of risks. The seriousness of the breaches identified together with their occurrence were also considered by the Committee in determining the administrative measures imposed. The good level of cooperation by the Company throughout the process has also been positively considered.

Key Take aways:

- Subject persons are being reminded of their obligation insofar as non-reputable jurisdictions are concerned. Particularly the proviso of Regulation 11(2) of the PMLFTR makes reference to non-reputable jurisdictions in respect of which an international call for countermeasures has been made. The proviso states that, when undertaking occasional transactions for, or establishing a business relationship with, or acting in the course of a business relationship with a natural or legal person established in a non-reputable jurisdiction in respect of which there has been an international call for counter-measures, prior to the establishment of the business relationship or the undertaking of an occasional transaction, subject persons have to:
    - apply EDD measures; and
    - inform the FIAU of the proposed business relationship, occasional transaction or transaction that is to take place within an already existing business relationship prior to these taking place.

- In deciding suspicious activity, subject persons are to consider all the available information and documentation at its disposal. Caution should be taken in the review of the documentation and information at hand. For instance, in considering loan agreements, one should consider the details included in such agreements, making sure that important information such as the purpose of the loan, the terms of the loan repayment, any interest payments done and other relevant documentation. Red flag indicators are important considerations, and while any one red flag on its own may not be sufficient for suspicion or grounds therefore to be established, numerous red flags should be collectively assessed and not seen in isolation.

- Reference is being made to several guidance made available by the FIAU and other international bodies to aid subject persons to identify suspicion of ML/FT. This so as to remain vigilant regarding the presence of red flags which should lead the subject person to consider submitting a report to the FIAU when illicit activity is suspected:

- **May 2022:** BO Obligations - CSP Thematic Review (including BO concealment red flags): *https://fiaumalta.org/wp-content/uploads/2022/06/1_BO-Thematic-Review.pdf*
- **December 2021:** Intelligence Factsheet on the misuse of corporate vehicles registered in Malta (including red flags): *https://fiaumalta.org/wp-content/uploads/2021/12/FIAUIntelligence-FactSheet_Misuse-of-companies_BOconcealment-2.pdf*
- **November 2021:** Typologies & Red Flags: Indicators of Tax-Related ML: *https://fiaumalta.org/event/typologies-red-flags-indicators-of-tax-related-ml/*
- **June 2019:** FATF - Guidance for a Risk Based Approach (TCSPs) *http://www.fatf-gafi.org/media/fatf/documents/reports/RBA-Trust-Company-Service-Providers.pdf*
- **July 2018:** FATF - Concealment of Beneficial Ownership: *https://www.fatf-gafi.org/publications/methodsandtrends/documents/concealment-beneficial-ownership.html*

TOTAL VALUE OF ADMINISTRATIVE PENALTY FOR THE TWO CASES:

Sixty-one thousand three hundred and eighty-two euro (€61,382).

19 September 2022

APPEAL – On the 14th October 2022, the FIAU was served with a copy of the appeal application filed by the Company before the Court of Appeal (Inferior Jurisdiction) from the decision of the FIAU. By means of the said appeal, the Company is requesting the Court to revoke and cancel the FIAU's decision as hereabove described.

The Company states, *inter alia*, that the FIAU wrongly interpreted the law and/or failed to consider or adequately analyse the information provided by the Company. It also held that the penalty, in its entirety, is disproportionate.

Pending the outcome of the appeal, the decision of the FIAU is not to be considered final and the resulting administrative penalty cannot be considered as due, given that the Court may confirm, vary or reject, in part, the decision of the FIAU. As a result, the FIAU may not take any action to enforce the administrative penalty pending judgement by the Court.

This publication notice shall be updated once the appeal is decided by the Court so as to reflect the outcome of the same.

17 October 2022