Financial Action Task Force

Groupe d'action financière

THIRD MUTUAL EVALUATION REPORT
ANTI-MONEY LAUNDERING AND
COMBATING THE FINANCING OF TERRORISM

ICELAND

13 OCTOBER 2006

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PREFACE - information and methodology used for the evaluation of Iceland

1. The evaluation of the anti-money laundering (AML) and combating the financing of terrorism (CFT) regime of Iceland was based on the Forty Recommendations 2003 and the Nine Special Recommendations on Terrorist Financing 2001 of the Financial Action Task Force (FATF), and was prepared using the AML/CFT Methodology 2004[1]. The evaluation was based on the laws, regulations and other materials supplied by Iceland, and information obtained by the evaluation team during its on-site visit to Iceland from 24 April – 5 May 2006, and subsequently. During the on-site the evaluation team met with officials and representatives of all relevant Icelandic government agencies and the private sector. A list of the bodies met is set out in Annex 2 to the mutual evaluation report.

2. The evaluation was conducted by an assessment team, which consisted of members of the FATF Secretariat and FATF experts in criminal law, law enforcement and regulatory issues: Mr. Marijn Y. Ridderikhof, Senior Examining Officer, Central Bank of the Netherlands (financial expert); Mr. Rune Grundekjøn, Special Adviser, Financial Supervisory Authority of Norway (financial expert); Ms. Elena Cocchi, Legal Advisor, Ufficio Italiano dei Cambi (UIC), Italy (legal expert); Mr. William Malone, Proceeds of Crime Branch, Royal Canadian Mounted Police (law enforcement expert); and Mr. Kevin Vandergrift, FATF Secretariat. The experts reviewed the institutional framework, the relevant AML/CFT laws, regulations, guidelines and other requirements, and the regulatory and other systems in place to deter money laundering (ML) and the financing of terrorism (FT) through financial institutions and Designated Non-Financial Businesses and Professions (DNFBPs), as well as examining the capacity, the implementation and the effectiveness of all these systems.

3. This report provides a summary of the AML/CFT measures in place in Iceland as at the date of the on-site visit or immediately thereafter. It describes and analyses those measures, sets out Iceland's levels of compliance with the FATF 40+9 Recommendations (see Table 1), and provides recommendations on how certain aspects of the system could be strengthened (see Table 2).

[1] As updated in June 2006.

EXECUTIVE SUMMARY

1. Background Information

1. This report provides a summary of the AML/CFT measures in place in Iceland as of May 2006 (the date of the on-site visit). The report describes and analyses those measures and provides recommendations on how certain aspects of the system could be strengthened. It also sets out Iceland's levels of compliance with the FATF 40 + 9 Recommendations. (See attached table on the Ratings of Compliance with the FATF Recommendations).

2. Overall, Iceland's legal requirements in place to combat money laundering and terrorist financing are generally comprehensive; however, the evaluation team had concerns about the system's effectiveness. The penalties for money laundering appear low, and the number of ML prosecutions and convictions has decreased. The terrorist financing offence is generally broad, although it does not fully cover the financing of acts listed in the Terrorist Financing Convention. While Iceland has generally adequate provisional and confiscation measures, they could be enhanced to be more effective; Iceland also needs to adopt a comprehensive mechanism to freeze assets in the context of S/RES/1373. The financial intelligence unit (FIU) operates as part of the Economic Crime Unit within the National Commissioner of Police and performs the basic function of receiving, processing and disseminating suspicious transaction reports (STRs). However, at the time of the on-site visit the evaluation team concluded that the FIU was not effective, due mainly to insufficient structural independence and inadequate resources. A new regulation (of July 2006) strengthening the FIU's structure, when fully implemented, should improve the situation. Measures for international co-operation are generally comprehensive, although there are concerns about dual criminality, and there is currently no ability to share seized assets with other governments.

3. At the time of the on-site visit (24 April—5 May), the Icelandic authorities were in the process of adopting legislation to implement the 3rd EU ML Directive; the legislation was passed by the parliament on 2 June and came into force in 22 June 2006. While the new legislation expands upon previous AML requirements from 1993 and 1999, it should be noted that the effectiveness of the new measures cannot yet be measured. While the new legislation includes stronger CDD measures, more comprehensive measures are needed, especially as regards beneficial ownership. Record-keeping measures are comprehensive. The scope of the suspicious transaction reporting requirements is generally sufficient, with the clear obligation to report STRs related to terrorist financing included in the new Act; however, there were some concerns regarding the effectiveness of the system.

4. The supervisory powers including the power to issue sanctions are generally broad; however, Iceland should strengthen administrative sanctions for directors and managers of financial institutions. At the time of the on-site visit, there were concerns about the overall effectiveness of the supervisory system—there had not been enough attention paid to AML/CFT matters. Since then, the Financial Supervisory Authority (FSA) has since hired an additional resource to specialise in AML/CFT issues, as planned. The same AML/CFT requirements now apply to all designated non-financial businesses and professions (DNFBPs) in Iceland.

5. Icelandic authorities indicate that the general crime rate in Iceland is low, due generally to the small and close-knit population (approximately 300,000) and geographic isolation. But the situation may be changing with growing globalisation in all fields, and authorities report an increased influence of foreign criminal groups. The number of narcotics cases has more than doubled between 2000 and 2004. The FIU considers that narcotics smuggling and trading together with various kinds of economic crimes including tax evasion continue to be the most significant sources of illegal proceeds in Iceland. The Icelandic bank notes (the Icelandic krona—ISK[2]) are not traded abroad, and many STRs are tied to the

[2] At the time of the on-site visit, the exchange rates were as follows: 1 ISK = 0.011 EUR or 0.014 USD; 1 EUR = 91 ISK; 1 USD = 72 ISK.

purchase of foreign currency. Authorities suspect that the exchanges may be of illegal funds intended for purchasing narcotics, and in several cases such indications have led to the capture and prosecution of drug smugglers. There are some indications that a growing number of criminal operators may be avoiding regulated operations in Iceland by using cash carriers to transfer funds for laundering or other illegal activity abroad. Authorities report that the financing of terrorism has not so far been a problem in Iceland.

6. Over the last decade, there has been a significant increase in the size of the Icelandic financial sector. In 2005, financial services became the largest contributor to GDP. Iceland joined the European Economic Area (EEA) on 1 January 1994. The current financial sector includes three commercial banks, 24 savings banks, and various credit undertakings such as credit card companies, leasing companies, and investment banks, as well as securities companies and brokerage firms, and life insurance companies. These entities are all licensed and supervised by the Financial Supervisory Authority (FSA), and covered by the AML/CFT legislation. Known money remittance activity takes place directly through banks, through Western Union and MoneyGram, which operate out of Icelandic banks, and through a domestic branch of a foreign bank (Forex). Known foreign exchange also takes place through Icelandic banks as well as one domestic business. This domestic business is not supervised.

7. The DNFBP sector includes 203 authorised real estate dealers, approximately 360 practicing lawyers, approximately 300 authorised public auditors, and an unknown number of retail dealers in precious metals and stones (there is only one wholesale dealer). All of these sectors are covered under the new Act No. 64/2006 on measures against money laundering and terrorist financing, of 22 June 2006. Casinos, including internet casinos, are prohibited in Iceland.

2. Legal System and Related Institutional Measures

8. Money laundering is criminalised through Section 264 of the General Penal Code and as "any action by which anyone accepts or acquires for itself or others, gain from an offence criminalised in the Penal Code, as well as stores or moves such gain, assists in the delivery thereof or does in other comparable manner support securing for others the gain of such an offence. The preparatory works clarify that this includes concealing, converting, and disguising. Participation in an organised criminal group or racketeering is not separately criminalised; and ancillary offences do not appear otherwise to cover adequately "participation" in the profit-generating crimes of organised criminal groups. Arms trafficking, insider trading and market manipulation are not money laundering predicates.

9. It is not clear whether the money laundering offence may apply to the person who also commits the predicate offence (i.e., self–laundering). Legal practice has been based on the principle that it is not possible to convict the same individual for the further exploitation of the gains of a criminal act, and in particular an offence of an economic nature, *following* a conviction of that individual for the original offence. However, Icelandic authorities believe that it is possible under the current legislation to convict someone at the same time of both of the predicate offence and money laundering, although no judicial rulings have been passed resolving this point finally.

10. The ancillary offences of attempt, aiding and abetting, facilitating and counselling the commission of the money laundering offence are adequately covered in the Penal Code. However, conspiracy is not fully covered.

11. The offence applies to those who intentionally or negligently engage money laundering. Under the basic concepts of Icelandic law, intention can be inferred from objective factual circumstances. Knowledge, according to the explanations provided, encompasses direct intention, probable intent, and also wilful blindness and *dolus eventualis.* Criminal liability of legal persons exists for money laundering related to corruption, but otherwise is too narrow.

12. Penalties of a maximum of two years apply for the basic money laundering offence; four years for aggravated offences. In cases involving narcotics trafficking, a penalty of up to 12 years is available.

Penalties appear to be too low, especially in comparison with penalties for similar types of offences (e.g. enrichment offences (6 years)) and do not seem to be effective, proportionate and dissuasive.

13. In general, it appears that the offence is not effectively implemented. There have been a limited number of prosecutions and convictions; these numbers have sharply decreased since 2000, despite a corresponding increase in reported narcotics trafficking, STRs filed, and the large expansion of the financial sector which would appear to offer additional opportunities for money laundering. Actual penalties applied have been low, even in cases involving narcotics trafficking where much higher penalties are available.

14. The terrorist financing offence is generally comprehensive and is defined in Section 100 (b) by penalising anyone who contributes funds or grants other financial support, procures or gathers funds or making funds available to individuals or groups who have the purpose of committing "terrorist acts" as defined in Section 100 (a). However, Iceland should broaden its definition of terrorist act to include all those activities referred to by Article 2 (1)(a) and (b) of the CFT Convention. Penalties of up to 10 years apply; criminal penalties also apply to legal persons. It was also a concern that the legislation does not specifically cover the financing of a terrorist act. There has not yet been any terrorist financing prosecution.

15. A general provision on confiscation is contained in Section 69 of the Penal Code, which covers proceeds from and instrumentalities used in or intended for use in any criminal offence, including the money laundering offence. Prosecutors and police have broad authority to seize assets, objects or documents accordance with Section 78 of the Code of Criminal Procedure. While the framework provides investigators and prosecutors with basic confiscation and provisional measures, the main issue is framework's effectiveness. The burden of proof turns out to be too high for prosecutors, since it appears that in practice they have to prove, beyond any reasonable doubt, that the accused has knowledge of the specific criminal origin of the proceeds. Provisions on confiscation should also be strengthened especially when the offender is not in possession of the assets, which are held by a third party.

16. Public Announcements which implement Act No. 5/1969 "Concerning the implementation of decisions taken by the United Nations Security Council." aim to implement S/RES/1267(1999) and S/RES/1373(2001) and successor resolutions. The Announcements make it an offence to release funds to individual terrorists and groups or to provide them with other form of support. A more direct freezing obligation has been introduced by Sec. 16(a) of the Act 87/1998 on financial supervision (as amended in 2003). As a practical matter, the only lists that can be enforced are those from the UN 1267 designation committee. Iceland does not have effective laws and procedures to give effect to freezing designations in the context of S/RES/1373; a domestic mechanism should be implemented to be able to designate terrorists at a national level as well as to give effect to designations and requests for freezing assets from other countries. Iceland should also issue additional guidance to the financial sector and adopt procedures for evaluating de-listing requests, for releasing funds or other assets of persons or entities erroneously subject to the freezing and for authorising access to frozen resources pursuant to S/RES/1452(2002).

17. The Icelandic FIU is a unit within the Economic Crime Unit at the National Commissioner of the Icelandic Police (Ríkislögreglustjórinn). The FIU has sufficient access to a wide range of financial, administrative, and law enforcement information. The FIU also appears to have a good network of informal relationships within the police and the banking sector. However, the evalution team had concerns regarding the FIU's effectiveness, which appears to be hampered by insufficient independence and resources (one dedicated staff). There was no pro-active analysis of STRs, periodic reports including statistics or AML/CFT trends/typologies, nor written guidelines or standardised STR forms, although the FIU plans to address these issues since the passage of new AML/CFT legislation in June 2006. Finally, it was not clear that the FIU has shown adequate results: while authorities indicated that STRs are forwarded to the national and local police when relevant, the number of ML prosecutions has dramatically decreased during a period of increased drug crimes, STRs filed, and a vast increase in the financial sector.

18. Major ML investigations and prosecutions are generally conducted by the Economic Crime Unit, which is headed by a public prosecutor and comprised of 14 police officers, another prosecutor and 3 police attorneys. The Director of Public Prosecution's office also prosecutes ML related to serious narcotics and other serious offences. These units would also investigate and prosecute terrorist financing cases, although no such cases have yet arisen. Authorities have a broad and sufficient range of access to customer identification information and any other relevant documents from financial institutions or other persons during the course of an investigation or prosecution.

19. There are no current statistics available concerning the number of ongoing ML investigations. The number of prosecutions has decreased since 2000, when there were 5 cases which included 12 indictments, to zero, one or two cases in each year after that. Icelandic authorities should take a more proactive approach to investigating and prosecuting money laundering and should also receive more specific ML/FT training to deal with these types of matters.

20. A new Customs Act No. 88/2005 (which entered into force in January 2006) requires arriving and departing passengers to declare amounts of cash which they have in their possession exceeding an amount equal to EUR 15,000. However, the system does not cover the majority of issues in SR.IX. In addition, the evaluation team did not view that the current system for detecting and preventing cross border movements of currency or bearer negotiable instruments related to money laundering or terrorist financing is effective. No currency declaration has been made.

3. Preventive Measures - Financial Institutions

21. The Act on Measures to counteract Money Laundering, No. 80/1993 (as updated in 1999) (hereafter "the MLA 1999") covers the full range of financial institutions listed in the FATF Recommendations. New legislation aimed at implementing the 3rd EU Money Laundering Directive and updating the AML/CFT regime, Act. No. 64/2006 on Measures against Money Laundering and Terrorist Financing (hereafter "AML/CFT Act 2006"), came into force on 22 June 2006. The legislation also covers a broad range of financial institutions, but is more specific than the previous legislation. The legislation extends the AML/CFT requirements to the full range of designated non-financial businesses and professions, as described below. This summary will refer to the new legislation, since the requirements are broader, although it should be noted that the effectiveness of the new requirements cannot yet be assessed.

22. Anonymous accounts and accounts in fictitious names are not permitted under Icelandic law. CDD is required when commencing business relationships, for occasional transactions of EUR 15,000 or more, for foreign exchange transactions of EUR 1,000 or more, when there is a suspicion of money laundering or terrorist financing, although not yet for wire transfers in circumstances covered by Special Recommendation VII. With regard to legal persons, the new legislation requires identification of "beneficial owners", defined as the "natural persons who ultimately own or control a legal person through direct or indirect ownership of more than a 25% share in the legal person or control more than 25% of the voting rights…" However, there is no general requirement to identify beneficial owners for all customers. Financial institutions are not required to determine actively if the customer is acting on behalf of someone else. In addition, exemptions from CDD appear overly broad. There are no general requirements to apply CDD measures other than ongoing due diligence to existing customers on the basis of materiality and risk.

23. Iceland has not yet implemented any provision regarding the establishment and maintenance of a customer relationship with politically exposed persons (PEPs). Article 12 of the new legislation covers most aspects of PEPs; however, these provisions will only enter into force on 1 January 2007. While the requirements in the new legislation regarding correspondent relationships are generally broad and based on the requirements of Recommendation 7, there are some significant deficiencies. They do not apply to relationships in other countries within the European Economic Area (EEA); there is not a requirement to ascertain that the respondent institution's AML/CFT controls are adequate and effective. Iceland has implement requirements for non-face to face transactions in the old and new legislation when establishing business relationships.

24. Article 16 of the AML/CFT Act 2006 introduces provisions on the use of third parties and introduced business; however, some provisions are unenforceable, in case of a third party outside Iceland, since the obligations are placed on the third party to provide information upon request.

25. Financial secrecy laws do not inhibit the full implementation of the FATF Recommendations.

26. Icelandic legislation generally requires financial institutions to pay attention to all complex, unusual transactions and transactions which have no apparent economic or lawful purpose, make written findings of these examinations and make them available to competent authorities. Financial institutions must also pay special attention to transactions and customers from states or geographical regions which do not follow international AML/CFT standards. However, there are no provisions dealing with the possibility to apply appropriate counter-measures where a country continues not to apply or insufficiently applies the Recommendations.

27. The Regulation for the new AML/CFT legislation was issued on 27 June 2006. It further details article 17 of the law and indicates that any suspicion that a transaction can be traced to money laundering or terrorist financing, shall be reported to the Economic Crime Unit of the National Commissioner of Police (which houses the FIU.) The obligation in relation to money laundering applied under the old legislation. The obligation applies regardless of amount and regardless of whether they involve tax matters. Attempted transactions are not specifically covered in the law, although in practice financial institutions report them. The legislation provides an adequate "safe harbor" for good faith reporting, and penalises unauthorised "tipping off."

28. Competent authorities have not established guidelines to assist financial institutions to implement and comply with STR requirements, and while the number of the number of STRs has increased from 112 in 2000 to 283 in 2005, the evaluation teams had concerns about the effectiveness of the STR system. While there is acknowledgment of STRs received, there is no substantive general feedback such as statistics on the number of disclosures and results, information on techniques, methods and trends, or sanitised case examples.

29. Financial institutions are required to maintain internal controls and written rules to combat money laundering and terrorist financing. However, the law does not specify that their procedures should cover, *inter alia*, CDD, record retention, the detection of unusual and suspicious transactions and the reporting obligation. The new legislation also clarifies that persons under the obligation to report shall nominate a person at the managerial level to be generally responsible for notification and practices supporting implementation of the Act; however, there is no requirement that the AML compliance officer and other appropriate staff have timely access to CDD, transaction, and other relevant information.

30. There is a general requirement in the financial institutions legislation to maintain an internal audit function; however, the requirement does not apply to the three securities brokerages currently operating, and the requirements do not specify an independent audit function to test compliance (including sample testing) with AML/CFT procedures, policies and controls. Financial institutions must provide training to combat ML and FT and comply with the Act. Financial institutions are also required to put in place screening procedures to ensure high standards when hiring employees.

31. The new AML/CFT Act 2006 also requires Icelandic institutions to ensure that their branches and subsidiaries outside the EEA take equivalent measures regarding CDD or as similar as the legislation of the state in question will permit. These requirements do not apply to AML/CFT requirements other than CDD.

32. It is not possible to establish a shell bank in Iceland. According to Article 13 of the AML/CFT Act 2006 ("Correspondent banking business with shell banks"), credit institutions are prohibited from entering into correspondent relationships with shell banks or with institutions that allow their facilities to be used by shell banks.

33. The FSA is the designated competent authority to license and supervise a wide range of financial institutions, according to Act No. 161/2002 on Financial Undertaking, including: commercial and savings banks, insurance companies, insurance brokers, securities companies and brokerage, mutual funds, stock exchanges and other regulated markets, an pension funds. Known money remittance takes place through Icelandic banks and a local subsidiary of a foreign bank. Money exchange activities must be licensed; foreign exchange takes place through banks as well as one domestic entity, which is not supervised. At the time of the on-site visit, the FSA had 35 employees, although no dedicated AML/CFT resources. In general, the FSA should give more attention to AML/CFT matters; Icelandic authorities are already taking steps to do this and since the on-site visit have hired one person to focus on AML/CFT issues. While this is a positive development, it is not year clear if this will be sufficient.

34. For supervised entities, the FSA has comprehensive inspection and surveillance powers and access to information, which are not predicated on the need to obtain a court order. Financial institutions are obliged to furnish all information that the FSA may require. On-site inspections can include the review of policies, procedures, books and records and sample testing.

35. Criminal sanctions are available for violations of provisions of the AML/CFT Act 2006. The FSA also has the authority to apply a range of administrative sanctions including warnings, insisting on corrective action, daily fines, and more severe financial penalties. However, there are no administrative penalties which can be imposed against directors and controlling owners of financial institutions directly for AML/CFT breaches, only indirectly by not meeting fit and proper criteria. Available sanctions for other senior management appear more limited. The available sanctions do not include the possibility to directly bar persons from the sector, unless they are convicted of an offence. In addition, sanctions do not include the general possibility to restrict or revoke a license for AML/CFT violations.

36. The requirements for fitness and properness of directors of institutions subject to the Core Principles are generally comprehensive. However, while fit and proper tests apply for directors and board members, they do not apply to other senior management.

37. According to Article 8 of the Act on Foreign Exchange, natural and legal persons providing currency exchanging services must be licensed by the Central Bank. There is no general requirement for money or value transfer services to be licensed or registered, nor have the other main requirements of SR VI been implemented. Although money exchange and remittance businesses that operate outside of banks are subject to the provisions of the revised AML/CFT Act, these entities are not subject to any system for monitoring and ensuring compliance with the AML/CFT requirements.

38. No specific AML or AML/CFT inspections have been conducted. The FSA indicated that it has inspected AML provisions as part of the general inspections process; FSA has conducted 50 on-site inspections from July 2003 to June 2004, and 41 on-site inspections from July 2004 to June 2005. However, there was no break down in terms of which financial institutions were covered or which ones also involved AML issues.

4. Preventive Measures – Designated Non-Financial Businesses and Professions (DNFBPs)

39. The Money Laundering Act of 1993 (as updated in 1999) also applied to real estate dealers and dealers in precious metals and stones. The new AML/CFT Act 2006, which came into force on 22 June 2006, covers a broader scope of DNFBPs in items, including attorneys, auditors, real estate dealers, and trust and company service providers, when they engage in the range of activities and the thresholds listed in the FATF Recommendations for these sectors, and dealers in any high-value items over EUR 15,000.

40. These DNFBPs are “reporting entities” and have the same obligations as financial institutions and activities described in the Act, and as such have the same strengths and deficiencies as previously described for financial institutions. However, the provisions have just begun applying to the full range of DNFBPs, and therefore their effectiveness cannot yet be assessed. A key area of concern in order to ensure effective implementation is the lack of adequate monitoring of DNFBPs. Icelandic authorities have not designed any authority to have the responsibility for the AML/CFT regulatory and supervisory

regime for DNFBPs. Adequate AML/CFT guidelines and guidance will also need to be provided to assist the various sectors to comply with their new obligations.

41. Icelandic authorities have applied AML requirements to other non-financial businesses and professions since the MLA was amended in 1999 and expand upon these in the new AML/CFT Act 2006, which also covers: shipping brokerage (i.e., the buying and selling of ships), licensed lotteries and raffles, and natural or legal persons who, in the course of their work, perform the various activities where lawyers are covered (i.e., buying and selling real estate, managing client money, etc.) The law provides as examples tax consultants or other external consultants.

5. Legal Persons and Arrangements & Non-Profit Organisations

42. The vast majority of legal persons in Iceland are Private Limited Companies (approximately 24,600), followed by Public Limited Companies or "hlutafélag" (approximately 950). There are also branches of foreign companies, and partnerships. These are generally registered in a national Register of Enterprises located at the Tax Directorate. Information on business names, addresses and directors are registered and available to the public. Similarly, information on several types of foundations is also recorded and made available to the public. Trusts cannot be formed under Icelandic law.

43. While the registration system allows for some information on control to be recorded and made readily available regarding these legal persons and arrangements, access to beneficial ownership does not appear to be adequately available in a timely fashion. Directors and shareholders may be nominees. Access appears more limited in the case of foreign entities.

44. Iceland has not yet reviewed the adequacy of domestic laws and regulations that relate to non-profit organisations (NPOs) for the purpose of identifying the features and types NPOs that are at risk of being misused for terrorist financing by virtue of their activities or characteristics. Authorities report that generally there are two types of entities that fit into the category of "NPO" as defined by FATF: commercial foundations and non-commercial foundations. Both of these types of entities must be registered, and therefore some kinds of information on their structures, purpose and managers are recorded and made available to the public. They must also keep accurate accounting records and generally file annual accounts. However, the other elements of SR.VIII have not yet been implemented.

6. National and International Co-operation

45. Iceland has a generally comprehensive system for national and international co-operation. Domestic co-operation is enhanced by the small size of the government and informal networks of co-operation which appear effective among all relevant AML/CFT authorities. Iceland has ratified the 1988 Vienna Convention and the 1999 Terrorist Financing Convention. Iceland has signed the 2000 Palermo Convention but not yet ratified it; preparations to ratify and implement it are underway.

46. Icelandic authorities are able to provide a wide range of mutual legal assistance; measures apply equally for ML and FT requests. In order to gather evidence for use in criminal proceedings in another state, the provisions in the Code of Criminal Procedure shall be applied in the same way as in comparable domestic proceedings. This would thus include the production, search and seizure of information, documents, or evidence (including financial records) from financial institutions, or other natural or legal persons; the taking of evidence or statements from persons, and the identification, freezing, seizure, or confiscation of assets laundered or intended to be laundered. Requests are sent to the Ministry of Justice except in the case of Nordic countries, where communication flows directly through the National Police Directorates.

47. The mutual legal assistance legislation requires dual criminality (except for most requests from Nordic countries), and it is therefore not clear that non-coercive measures could be applied in the cases where there is not dual criminality. Iceland has no legal or practical impediment to rendering assistance where both countries criminalise the conduct underlying the offence.

48. The general requirements for enforcing foreign criminal judgements are found in the International Co-operation on Enforcement of Criminal Judgements Act 56/93, as amended in 1997, which implements the 1970 Council of Europe Convention on the International Validity of Criminal Judgements. However, foreign judgments cannot be executed if the person is not domiciled in Iceland. Iceland has not considered an asset forfeiture fund or authorising the sharing of confiscated assets with other countries when confiscation is directly or indirectly a result of co-ordinated law enforcement action.

49. Act 13/1984 on Extradition of Criminals and other Assistance in Criminal Proceedings allows for extradition if the concerned offence is equivalent in substance to a crime punishable under Icelandic law with imprisonment of one year or more, which therefore includes both money laundering and terrorist financing. The legislation prohibits the extradition of Icelandic nationals, except under certain circumstances to Nordic countries. For Icelandic nationals, a special request must be made to the Icelandic authorities to institute proceedings domestic proceedings, and if this is received, then the same procedural rules apply to the case as would apply to comparable cases in Iceland. Extradition also requires dual criminality; however, Iceland has no legal or practical impediment to rendering assistance in extradition requests where both countries criminalise the conduct underlying the offence. The limitations on the scope of "acts of terrorism" as defined in Iceland also present some concerns about Iceland's ability to effectively provide assistance in cases involving the financing of acts not defined as terrorist acts in Iceland.

50. In general law enforcement, the FIU, and supervisors can engage in a wide range of international co-operation. Icelandic authorities attempt to render assistance to foreign authorities as expeditiously as possible; however, given the complete lack of statistical data, the evaluation team was not able to determine that the mechanisms for international cooperation are fully effective.

1. GENERAL

1.1 General Information on Iceland

1. Iceland is located in the North Atlantic between Norway, Scotland and Greenland, with a land area of some 103 thousand square kilometers, a coastline of 4,970 kilometres and a 200-nautical-mile exclusive zone (EEZ) in the surrounding waters. Iceland enjoys a warmer climate than its northerly location would indicate because a part of the Gulf Stream flows around the southern and western coasts of the country. Iceland is mostly mountainous and of volcanic origin, with the highest peak reaching 2110 metres. The population is approximately 300,000; about 63% of the population lives in the capital city of Reykjavik and its surrounding municipalities.

2. The Icelandic economy is the smallest within the Organisation for Economic Cooperation and Development (OECD), generating GDP of EUR 10.2 billion euros in 2004. The small economy has not inhibited economic growth and prosperity, which has been built largely on Iceland's comparative advantages in abundant marine and land based natural resources, as well as human capital. The location and geology of Iceland determine its main resources which are fish, and hydro and geothermal energy. Iceland is the 12th largest fishing nation in the world, exporting nearly all its catch as domestic demand is relatively small. In recent years the percentage of fish and marine products in the total export of manufactured goods has declined with growing exports from aluminium smelting and medical and pharmaceutical production. Iceland's natural environment represents another major resource, reflected in large and growing tourist industry. After privatisation of the 3 largest banks which formerly were state-owned, financial services have greatly expanded at home and abroad and in 2005 they contributed more to GNP than the fish and marine products industry. Iceland's unemployment rate was estimated at 2.1 % for 2005.

3. With the Act of Union 1918, Iceland became a sovereign state in a monarchical union with Denmark. In 1944, Iceland terminated this union with Denmark and the Republic of Iceland was established. Iceland has a parliamentary democracy with a tradition of political stability. The parliament operates in one chamber and has 63 members elected for the period of four years. The head of government is the prime minister; there are formally fourteen ministries administrated by 12 ministers. The president of the republic, a mainly representative and ceremonial post, is the head of state and is elected for a term of four years by a direct vote of the electorate. Iceland has a Supreme Court and eight district courts; justices are appointed for life by the Minister of Justice). Iceland joined the EFTA (European Free Trade Association) in 1970 and the European Economic Area (EEA) on 1 January 1994.

4. Public Administration in Iceland is in two tiers: government and local authorities. The number of local authorities has in the last decade been decreasing through mergers and is 98 at the end of 2005. The public administration is relatively slim (approximately 400 in the ministries) and pathways of communications between officials and between them and the public usually short.

5. As in other Nordic states, the legislative tradition is that all law proposals are accompanied with explanations which later are one of the tools used to interpret the legislation. The legal text itself may therefore be shorter and perhaps not descriptive in detail. This does not however apply to laws originating in the EU as the European Court of Justice or respectively the EFTA Court has the final word in their interpretation.

6. The office of the Ombudsman was established in 1988 by Act No. 82/1988. The Ombudsman is elected by Parliament and reports to Parliament annually, but in other respects he is autonomous. His role is to supervise state and municipal administration and investigate administrative cases either on his own initiative or upon complaint. The Ombudsman also keeps under observation whether laws conflict with the Constitution or suffer from other faults, including whether they are in conformity with international instruments to which Iceland is a party.

7. According to the findings of the Transparency International (TI) Corruption Perceptions Index (CPI), which is a survey measuring the level of perceived corruption in the public service, Iceland ranked first out of 159 countries studied in terms of absence of corruption in 2005. According to article 109 in the GPC both passive and active bribery is an offence regarding Icelandic and foreign officials. Iceland was the first OECD country to ratify the OECD Convention on Combating Bribery of Foreign Public Officials in International Business Transactions. The Icelandic legislation was reviewed under Phase 1 in October 1999 and an on-site visit for a Phase 2 exam took place in 2002. Iceland is also a member of GRECO (Group of States Against Corruption). The GRECO evaluation reports on Iceland give more detailed information on the Icelandic system in relation to corruption. (see Evaluation Report on Iceland adopted by GRECO July 2004 and Addendum to the Compliance Report on Iceland adopted by GRECO December 2005 - www.greco.coe.int). Iceland has not signed the United Nations Convention against Corruption.

1.2 General Situation of Money Laundering and Financing of Terrorism

8. Icelandic authorities indicate that the general crime rate in Iceland is relatively low, and the reasons for this are probably small and close-knit population and geographic isolation. But the situation may be changing with growing globalisation in all fields and ever improving communications to other countries, Iceland becoming an airline communications hub in the North Atlantic.

9. Statistics for the past few years show that the yearly numbers of offences committed have remained broadly constant. However narcotics-related offences are on the increase—about 19% of penal cases were related to narcotics in 2004, compared with 10% in 1997, and the number of narcotics cases has more than doubled between 2000 and 2004. In 2004, there were 86,987 offences recorded in police dossiers, of which 64,070 (just over 75%) were traffic offences; when excluding these traffic violations, enrichment offences (fraud, embezzlement, receiving stolen goods) amounted to approximately 45% of offences. The annual rate of homicide in Iceland in 1998 – 2004 was one per 100,000 inhabitants and the annual rate of robbery for the same period was 13 per 100,000 inhabitants. The FIU considers that narcotics smuggling and trading together with various kinds of economic crimes including tax evasion continues to be the most significant sources of illegal proceeds in Iceland.

10. Statistics are not available regarding economic loss or damage from the offences committed but reported offences in each category were as follows:

Year:	**2000**	**2001**	**2002**	**2003**	**2004**	**Total**	**% (excluding automobile)**
Offences against public order	133	126	118	241	216	834	0.71%
Forgery	455	398	513	340	328	2,034	1.74%
Sexual offences	228	282	324	359	277	1,470	1.26%
Assault	1,508	1,455	330	1,304	1,199	5,796	4.95%
Enrichment offences	10,482	10,522	11,330	10,041	9,716	52,091	44.51%
Vandalism	4,182	4,463	4,141	3,883	3,536	20,205	17.26%
Unlawful use of property	427	388	566	412	463	2,256	1.93%
Narcotics offences	781	911	994	1,285	1,671	5,642	4.82%
Alcohol offences	2,665	2,230	1,984	2,009	1,553	10,441	8.92%
Automobile/Traffic violations	66,814	66,570	73,573	64,510	64,070	335,537	
All other offences	3,233	2,625	3,439	3,763	3,204	16,264	13.90%
TOTAL	90,908	89,970	97,312	88,147	86,233	452,570	
TOTAL not including automobile/traffic offences						117,033	

* See Ch. XXVI of the Penal Code. Enrichment offences include theft, embezzlement, fraudulent settlement, extortion, and receiving stolen goods.

11. The illegal proceeds mostly derive from domestic offences but the importation of narcotics is tied in many ways to international organised crime. Iceland authorities also report that several attempts by the organisation "Hells Angels" to gain hold in Iceland have been thwarted by the police so far. These motorcycle clubs are already established in other Nordic countries and in Canada and generally believed to be associated with narcotics, prostitution and violent crimes.

12. Although the number of STRs has been increasing in recent years (for example, 55 in 1999, 125 in 2001, and 301 in 2004), the FIU concludes that the money laundering situation has not changed noticeably in the last four years. New and strengthened measures such as the planned purchase and operation of new electronic surveillance equipment may make such estimates more reliable. The amounts involved in the suspected ML—as indicated by the total monetary amount reported in the STRs—were: ISK 394 million ISK in 2004 and ISK 596 million ISK in 2005.

13. The Icelandic bank notes are not traded abroad, and many of the STRs are tied to the purchase of foreign bank notes in banks or money exchange offices. Authorities suspect that the exchanges may be of illegal funds intended for purchasing narcotics, and in several cases such indications have led to the capture and prosecution of drug smugglers. These cases were pursued and punished under the predicate narcotics crimes, since the laundering activity is considered to be part of and "co-punished" with the predicate offence, and self-laundering is not separately punishable.

14. There are some indications that a growing number of criminal operators may be avoiding regulated operations in Iceland by using cash carriers to transfer funds for laundering or other illegal activity abroad. Persons carrying large amounts of cash in foreign currency without being able to give satisfactory explanations have occasionally been caught by customs supervisors or airport police. Countermeasures are being considered, such as a review of confiscation rules and closer coordination between the FIU and the Directorate of Tax Investigations.

15. There are cases where financing of terrorism may be involved and which are now under investigation by the relevant police unit under the National Commissioner of Police. However, Icelandic authorities do not consider that this has been a significant problem in Iceland.

1.3 Overview of the Financial Sector and DNFBP

a. Overview of Iceland's financial sector

16. Over the last decade, there has been a significant increase in the size of the Icelandic financial sector. Direct foreign investment "has grown by over 40% per year on average over the past ten years".[3] In addition to this, "Iceland's financial services sector has experienced tremendous growth in recent years, catalysed by deregulation in the 1990's and, in particular, privatisation in 2002 of two commercial banks.[4] There are four commercial banks in Iceland; the three largest account for 88% of total consolidated assets for 2005. Approximately 60% of assets are held by foreign subsidiaries, most of them located in northern Europe.[5] A fourth commercial bank serves as the banking institution for the 24 savings banks in Iceland. Together, commercial and savings banks amounted to approximately 93% of assets at the end of 1994.[6]

17. As 1 January 2006, the number of financial institutions subject to supervision by the FSA is indicated below. These activities are all included in the Icelandic Money Laundering Act (MLA). A description of their institutions' activities according the FATF definition of "financial institution" is

[3] Source: The Central Bank of Iceland "The Economy of Iceland 2005."

[4] Ibid.

[5] Nordic Banking Structures: Report. Available at : http://www.norges-bank.no/ finansiell_stabilitet/nordic_banking_structures.pdf

[6] Economy of Iceland 2005. Published by the Central Bank of Iceland.

contained in the subsequent chart. Known money remittance activity in Iceland takes place directly through banks, through Western Union (which operates only through 35 branches of an Icelandic bank (Landsbankinn)), and through MoneyGram, (which operates from an Icelandic bank (Icebank) as well as through Forex). Forex is licensed as a foreign subsidiary of a Swedish bank and primarily conducts foreign exchange activities. Known foreign exchange also takes place through Icelandic banks as well as one domestic business. Foreign exchange licences are issued by the Central Bank of Iceland.

Institution	Number
Commercial banks	4
Savings banks	24
Credit undertakings:	10
Credit card companies	2
Leasing companies	2
Investment banks	5
Other credit undertakings	2
The Housing Financing Fund*	1
The New Business Venture Fund**	1
Securities companies	7
Securities brokerage	3
Life insurance companies	4
Insurance intermediaries:	
Licensed brokers	8
Authorised insurance agents (such as banks and other intermediaries) that act on behalf of insurance companies	Unknown
Management companies of UCITS	6

b. Overview of designated non-financial businesses and professions (DNFBPs)

18. ***Casinos:*** Casinos are not allowed in Iceland and gambling in general is forbidden according to the General Penal Code. There are however exemptions for a related activity as the Ministry of Justice can permit small scale raffles and lotteries for charities[7]. Exemptions have also been granted to several humanitarian and cultural organisations, i.e. to operate lotteries, football pools and gaming machines. Internet casinos would be illegal in Iceland; however if originators of such activity were domiciled in Iceland or their activity especially focused on the Icelandic market this would however be possible.

19. ***Real estate dealers:*** In January 2006 there were 203 authorised real estate dealers in Iceland. The profession is regulated by law, with the current legislation being from the year 2004.[8] The detailed process of trading in Real Estate is also stipulated in other legislation from 2002.[9]

20. ***Dealers in precious metals and stones:*** Dealing in precious metals and stones is not a regulated activity in Iceland. Local jewellery handicrafts have covered their needs for raw materials and semi-completed products with purchases from European suppliers. Their final production or imported jewellery is generally below value limits. There is only one Icelandic wholesaler in this field with a small turnover. There is no mining of precious stones or metals in the country.

21. ***Legal profession:*** In January 2006, there were 359 independent practicing lawyers or "attorneys at Law" employing 93 associates in Iceland. The legal profession is regulated with a Lawyers Act[10] which provides rules for admission to the profession. Membership in the Icelandic Bar Association is compulsory for practicing lawyers, and they are considered public servants although they are not employed by the state. The Association is by law required to supervise the attorneys' adherence to the legal and ethical rules regulating the legal profession, and in this capacity has issued a professional Code

[7] Act on Lotteries No. 6/1926

[8] Act on the sale of Real Estate, Undertakings and Ships

[9] Act on trade in Real Estate.

[10] Act on Lawyers No. 77/1998

of Conduct (*Codex Ethicus*). Attorneys can be disciplined or even disbarred for breaches of conduct. Sentences may also include the cancellation of the permit to practice law.

22. ***State authorised public auditors:*** The profession of State Authorised Public Auditors or "Chartered Accountants" has a similar status as the legal profession. Membership to their professional Association is not compulsory, but most accountants however belong to it. The present legislation[11] is based on Directive 84/253/EEC, but work has already started to rewrite it in accordance with new acquis from the EU. Recent years have seen the trend of globalisation in this field, with international auditing companies establishing offices and affiliated units in Iceland. This has lead to the adoption of similar work rules in these companies as used by their parent companies worldwide. There are approximately 300 people in this field.

23. ***Notaries:*** In Iceland notaries are officials within the office of a district sheriff, who are empowered to certify documents etc. They have no tasks of relevance in money laundering or financing of terrorism context and are for that reason not covered by the AML/CFT Act.

24. ***Trust and company service providers:*** A separate category of trust and/or company service providers does not exist currently in Iceland. Persons conducing company formation services are doing so from the offices of law and accounting firms.

[11] Act on accountants No.18/1997 with amendments April 10th, 2003

1.4 Overview of Commercial Laws and Mechanisms Governing Legal Persons and Arrangements

25. Most of the large companies in Iceland are **Public Limited Companies or "hlutafélag" (hf)**. *(approximately 950 in January 2006).* The Act regulating these[12] is based on the relevant EU directives. Minimum share capital is ISK 500,000. Twenty-six of these are traded on the Icelandic Stock Market as of January 2006. For those companies listed on the stock market, special disclosure rules apply.

26. **Private Limited Company or "einkahlutafélag (ehf.):** *(approximately 24,600)* is a smaller and somewhat simpler form than the Public LC. The Act regulating these is also based on the relevant EU directives. Minimum share capital is ISK 90,000.

27. **A co-operative company or "samvinnufélag" (svf.)** is a legal entity which has united producers of farm products, fish etc., in marketing their produce and purchasing their supplies. Their purpose is to further the interests of the members by economic activities in which the members take part as customers or suppliers or by contributing their labours or making use of the services of the association in some other manner. The number of these entities has decreased in recent years to about 82 in January 2006.

28. **Branches of foreign companies** *(approximately 53).* These are foreign entities operating in some form of business in Iceland. They are required to register if their activity falls within the scope of the taxation regulations in Iceland.

29. The companies with limited liability (hf, ehf, co-ops) and branches of foreign companies are registered in the Register of Enterprises at the Tax Directorate, Ministry of Finance. That register is open to the public along with its information on directors, board members, and annual financial statements. For those companies listed on the stock market, special disclosure rules also apply.

30. **Private individuals** *(approximately 11,200)* are people who are engaged in some kind of independent business. They are especially registered with the tax authorities (using their national identification number) and for the purpose of VAT, pension fund liabilities, etc. In recent years, the number registered under this arrangement has for taxation reasons decreased with a corresponding increase in the number of Private Limited Companies.

31. **Partnerships** *(approximately 2,350)* are a registered form for economic activity. For general partnerships, the owners carry unlimited liability for the partnership and share the profits between themselves. For limited partnerships, at least one partner has limited liability. Partnerships are registered with the local sheriff's office if they wish to operate under a special name or logo.

32. **Commercial and non-commercial foundations** are the main types of non-profit organisations that can be used for fundraising. Foundations are legal persons, have a founding charter and/or memorandum of association, are established for a particular purpose, and have fund/capital requirements and a board of directors. Commercial foundations (44) must register at the Tax Directorate in the Ministry of Finance. Non-commercial foundations (671) do not have a direct obligation to register with the Tax Directorate; however, they generally do so in order to obtain an organisation number, which is required to open a bank account. Non-commercial foundations need to apply to and be approved by the Ministry of Justice.

33. Public collections of funds also need a permit from the relevant district chief of police according to a special legislation on public collections. The legislation is now being reviewed with MLA requirements in mind. The operation of several of the non-profit organisations/charities depends on such public collections.

[12]Act on Public Limited Companies No. 2/1995

34. **Trusts** cannot be set up under Icelandic law.

1.5 Overview of Strategy to Prevent Money Laundering and Terrorist Financing

a. AML/CFT Strategies and priorities

35. The Government of Iceland has in recent years been strengthening the police. In 2005, the number of policemen was 671 and 80 reservists. The number of inhabitants per an active policeman in 2005 was 434. The Police School has also been strengthened in order to enable it to offer all policemen continuing education and training during their whole career on the force.

36. Iceland authorities also indicate that the establishment of the Financial Supervisory Authority has also strengthened the supervision of the financial sector. At the time of the on-site visit the FSA was in the process of increasing its staff especially in order to tighten the supervision on AML/CFT activities. In this regard, an additional person began work in June 2006 to deal solely with AML/CFT issues, and tasks include the development of guidelines.

37. Co-operation and co-ordination between relevant law enforcement agencies dealing with different forms of economic crime in Iceland including ML has been given increased attention and this applies also to co-operation with neighbouring states. Iceland takes an active role in ongoing work within the European Economic Area, the Schengen Council, Council of Europe, UN and OECD to enhance co-operation and increase the surveillance effectiveness in the field.

b. The institutional framework for combating money laundering and terrorist financing

(i) Ministries and inter-ministerial bodies

38. ***The Ministry of Industry and Commerce*** is responsible for legislation concerning financial services. It is also responsible for the legislation on measures against money laundering and administrative regulations and guidelines pertaining to that legislation. The Financial Supervisory Authority comes under the general authority of the Ministry.

39. ***The Ministry of Justice*** and Ecclesiastical Affairs is responsible for the General Penal Code, including the general provisions concerning the money laundering offence and terrorist financing offences. It is also responsible for legislation in the field of civil and criminal procedures, and for regulating the Legal profession, Real Estate Dealers and gaming activity. The National Commissioner of Police, the Prosecutor General and the Courts come under the general authority of the Ministry.

40. ***The Ministry of Finance*** is responsible for tax and customs legislation, as well as preventive measures on tax evasion, smuggling, etc. It is also responsible for regulating public accountants. The Ministry's *Tax Directorate* also issues business numbers, which in practice are required for opening accounts at banks and non-bank financial institutions in Iceland. The Tax Directorate also hosts several corporate registers, the information of which is generally open to the public: the Register of Enterprises (public and private limited companies, foreign companies), Co-operatives Registry, and the Registry of Commercial Foundations.

41. ***National Statistics Office*** of Iceland has a status as a Ministry. It maintains a register of all persons resident in Iceland[13]. This information is publicly available and the police have online access to all the registers. In addition all residents are issued an identification number, which in practice a condition for opening accounts at banks and non-bank financial institutions in Iceland.

[13] That registry will move under the Ministry of Justice during 2006.

42. **A *AML/CFT Consultation Committee*** was originally composed of representatives from the ministries and agencies as well as representatives of the types of financial institutions covered by the MLA Act. Since the autumn of 2005 it is composed of representatives from the Ministries, the Financial Supervisory Authority, the Central Bank, the FIU, and the Bankers and Security Dealers Association of Iceland (BSA).

(ii) Criminal justice and operational agencies

43. ***The National Commissioner of Police*** falls under the Minister of Justice and is in charge of police in Iceland. The role of the Commissioner is to perform various supervisory and administrative functions in fields related to country-wide law enforcement and international co-operation through Interpol and Europol. The Commissioner is also in charge of national security and civil protection matters, which shortens the lines of communication in CFT cases. Prosecution of economic crimes rests with the National Commissioner of Police. ***District police chiefs (sheriffs)*** investigate and prosecute the less serious crimes and misdemeanours (the vast majority of offences).

44. There are five specific divisions under the Commissioner, one of which is the ***Economic Crime Unit***. This division, which is headed by a public prosecutor, is comprised of 14 police officers, one prosecutor and 3 police attorneys, which is an increase by 10 since 1998. The unit also houses the ***Financial Intelligence Unit*** and has divided its work and staff correspondingly. A few large economic fraud cases have recently absorbed greatly the resources of the division, but authorities indicate that a reorganisation is now underway making it possible to allocate more resources to AML/CFT problems and more proactive work in the field.

45. ***The Director of Public Prosecutions (DPP)*** is the highest holder of prosecution authority. His role is to ensure that legally prescribed sanctions are applied against persons who have committed criminal violations, and to supervise the exercise of prosecution authority by district chiefs of police. The DPP's Office prosecutes the more serious offences defined in the Criminal Code, including offences committed in an official capacity, and it also has the exclusive jurisdiction to prosecute all offences before the Supreme Court. Although the DPP formally reports to the Minister of Justice, the office has by law a special independent status intended to secure its independence similar to the status of judges.

46. The Constitution provides that the ***judiciary*** wield judicial power. There are eight courts of the lower instance in Iceland, each with a prescribed geographical jurisdiction. These have jurisdiction in private and criminal cases, and they issue remand orders and other orders necessary in the context of criminal investigation. They also render bankruptcy orders and resolve disputes arising in enforcement of judgments by the magistrates. The resolutions of the lower courts can be referred to the Supreme Court of Iceland, which is a court of appeals serving all Iceland. Criminal judgments can be referred to the Supreme Court subject to certain conditions, and in private cases appeal is subject to certain requirements concerning minimum interests. There is an independent Courts Council which is responsible for the detailed administration of the district courts.

47. ***The Customs Service*** operates under the Ministry of Finance, operates customs controls of foreign passenger and goods traffic, and can commence investigations for possible Custom offences. However, the Customs authorities have limited enforcement powers, and in practice hand over all cases to the police after an initial investigation. The Customs authorities have not had a significant role in investigating money laundering, but may do so in the future when attention of the authorities turns more to trade based money laundering.

(iii) Financial sector bodies—government

48. ***The Financial Supervisory Authority*** was established in 1999 by the merger of the Bank Inspectorate of the Central Bank and the Insurance Supervisory Authority.

49. The ***Central Bank*** has a changed status since the second FATF evaluation of Iceland. It now has the legal status of an independent body governed by public law. The main objective of the Central Bank

is to now to be in charge of monetary policy implementation in Iceland by promoting price stability. The Central Bank also undertakes standard central bank tasks, such as maintaining external reserves and promoting an efficient and safe financial system. It is also responsible for issuing notes and coinage and exchange rate matters. The Central Bank does not have any supervisory powers or similar responsibilities with regard to the Anti-Money Laundering Act.

(iv) Financial sector bodies—associations

50. The ***Bankers and Securities Dealers Association of Iceland (BSA)*** was formed by a merger of the Icelandic Bankers Association (IBA), the Association of Securities Firms (ASF) and the Association of other Credit Institutions (ACI). It is also closely associated with the Icelandic Savings Banks Association which has a member on the Board of SBV (BSDI). There is a close co-operation between BSA and the Ministries, and it is represented on the AML/CFT Consultation Committee. The Association maintains contact on both a regular and informal basis with government agencies regarding development in money laundering and it has an information role towards its members.

51. ***The Association of Icelandic Insurance Companies (SIT)*** is the trade association of insurance companies in Iceland. Its objectives are to promote the general interests of the insurance industry and to provide information and education on insurance and insurance activity.

52. ***The Icelandic Bar Association*** comprises lawyers holding the title "lögmaður" (attorney at law), those authorised to practice law conducted in Iceland. The membership is mandatory. By law, the association is required to supervise the attorneys' adherence to the legal and ethical rules regulating the legal profession. The association has in that capacity adopted a professional Code of Conduct (*Codex Ethicus*). Separate from the Bar is a ***Disciplinary Board***, which handles complaints lodged against attorneys.

53. ***The Institute of State Authorised Public Auditors*** is the only professional body of auditors. Its purpose is to strengthen the co-operation between Icelandic state authorised public auditors and to maintain and improve the reputation of the Icelandic audit profession. It is also responsible for professional ethics and issuing of auditing guidelines.

54. ***The Association of Dealers in Real Estate*** enfolds State Authorised Real estate Dealers in Real Estate, businesses and ships. Membership in the Association is mandatory by law. In order to qualify as an authorised dealer in Real Estate, the individual must fulfil several requirements regarding education, insurance cover and not having been sentenced in a penal case. Connected with the association is a special tribunal, which can issue sanctions and disciplinary measures in complaints pertaining to the performance of a dealer, including temporary cancellation of work authorisation. The Ministry of Justice has, however, the final administrative decision is such cases.

c. Approach concerning risk

55. The new AML/CFT legislation, which entered into force on 22 June 2006 incorporates, the issue of risk into preventative measures for financial institutions and DNFBPs. Article 2 indicates that the "Financial Supervisory Authority may decide that parties falling within the scope of…[the Act] and engaging in financial activities on an occasional or very limited basis, and where there is little risk of money laundering or terrorist financing, should be exempt from the provisions of the act." However, no parties or sectors have so far been exempted on this basis. Article 7 also allows covered persons to implement the CDD provisions on the act on a risk-sensitive basis, where the extent of information gathering and other measures pursuant to this Act in respect of each customer are based on an assessment of the risk of money laundering and terrorist financing. Persons must establish rules on the conduct of risk assessment, which must be approved by the FSA in the case of financial institutions, and by the police, for other persons covered by the Act.

d. Progress since the last mutual evaluation

56. Since the last evaluation, the legislative changes which were then in the pipeline have been passed as legislative Acts, e.g. the expansion of the scope of preventative measures to also cover *inter alia* money remittance and exchange. The establishment of the Financial Supervisory Authority has strengthened the supervision in the financial sector and the Financial Intelligence Unit has been operated within the division of economic crime activity at the National Commissioner of Police. New articles 100a. 100b and 100c in the General Penal Code create financing of terrorism offences.

57. Legislation aiming to implement the Third Anti-Money Laundering Directive (2005/60/EC) of EU passed the Icelandic parliament and came into force on 22 June 2006. Iceland authorities indicate that the submittance of STRs has improved, and the MLA awareness in the financial sector and DNFBPs has increased. With the entry into force of legislation implementing the 3rd EU Directive, an administrative regulation will be published by the Minister of Justice regarding the operation of FIU within the National Commissioner of Police's economic crimes' division. The intention is to strengthen the FIU. The Ministry of Justice issued Regulations on the handling of notifications of alleged money laundering on 12 July 2006, and they took effect on 19 July 2006. These regulations include provisions on the recording, treatment and deletion of notifications of alleged money laundering.

e. Deficiencies identified and recommendations in the second mutual evaluation (February 1999):

58. The 1999 mutual evaluation suggested a number of other improvements to the Icelandic system:

1) *Changes in the criminal code to make the ML offence more effective.* Specifically:
- Widen the offence to include the concepts of *conversion* or *transfer* as per the Vienna Convention. (These were also recommendations from the first mutual evaluation report.)
- To prove an offence under Art. 264 of the GPC, the prosecution must prove that the accused has actual knowledge of the illegal origin of the proceeds, and must prove the link between the proceeds and the predicate offence. This is a very high burden of proof and this should be reviewed.
- Consider increasing the maximum penalties for basic ML (2 years).

2) *Changes to improve the regime for confiscation and provisional measures:* Confiscation provisions require the prosecution to prove on the normal criminal standard of proof that assets sought to be confiscated derived from the commission of the predicate offence for which the accused has been found guilty. This is a heavy burden, and the following should be considered:
- After a conviction, subject all the property of the defendant to confiscation unless he can prove that the property was lawfully obtained;
- Reduce the standard of proof required by the prosecution;
- Provisions should apply to the value of property transfers to third parties (e.g. to close relatives, associates, or companies controlled by the defending where value was transferred by gift.);
- Oblige the court to order the confiscation of the total proceed of crime unless it is clearly unreasonable to do so;
- Provide specific powers of enforcement of confiscation orders, whether they are proceeds or value based;
- Allow seizure of freezing powers also to be used against assets held by third parties.

Icelandic authorities reported that these suggestions, while not yet implemented, are awaiting the conclusions from a comprehensive review of the Penal Code by a special committee

3) *The FIU should increase its resources.* Iceland reported that the Economic Crime Unit, which houses the FIU, has increased its staff resources by 10 people since 1998. However, there have not been any additional resources dedicated to the FIU functions.

4) The number of STRs has remained modest and the results are unevenly distributed. Some further steps need to be taken by the government to ensure a comprehensive and consistent set of guidance notes. The number of STRs has increased significantly; STRs have been submitted by a range of financial institutions. However, the results of the STRs have been minimal: there have been very

few cases that resulted from STRs, the FIU has not done any proactive analysis of STRs, nor issued any reports with statistics, trends, indicators, or other guidance on or results from STRs.

2. Legal System and Related Institutional Measures

Laws and Regulations

2.1 Criminalisation of Money Laundering (R.1 & 2)

2.1.1 Description and Analysis

Recommendation 1

Definition and scope of the offence

59. Section 264 the Icelandic General Penal Code was introduced in 1997 in order to implement the 1988 Vienna Convention and enlarge the scope of the money laundering offence beyond the proceeds of narcotic trafficking crimes. Section 264 defines money laundering as any action by which anyone accepts or acquires for itself or others, gain from an offence criminalised in the Penal Code, as well as stores or moves such gain, assists in the delivery thereof or does in other comparable manner support securing for others the gain of such an offence.

60. Iceland has ratified the Vienna Convention; however, the definition of the money laundering offence has not been amended in accordance with the specific requirements of the Vienna Convention. In the current wording, neither conversion or transfer nor concealment or disguise is explicitly covered. While section 264 criminalises the act of "moving", this is not synonymous with "transferring" with the meaning of converting as adopted by the Convention, which is meant not to physical movement but primarily a transfer which also includes any transformation in the nature of funds/assets.

61. According to preparatory works accompanying this provision, the clause "in other comparable manner support securing for others the gain of such an offence" should be interpreted by courts as covering any assistance in converting gain with the purpose of concealing its illegal origin. As examples, it is mentioned that the penal provision would cover the conduct of concealing, sending or transferring such proceeds between bank accounts or converting them, pledging them, or investing them. Therefore, conversion and concealment are explicitly mentioned as some of the most common laundering techniques to pay attention to. Preparatory works are often used in Nordic countries for better specifying the scope of legal provisions fall into the sources of law. Although not directly enforceable, courts interpret and apply the laws in accordance with these documents. It is a long-standing legal tradition in Iceland that these preparatory/explanatory works are meant to complement and interpret statutory provisions and are approved by the Parliament along with the law itself. However, it should be noted that, in the limited number of money laundering cases which have led to a conviction, concealing has been considered almost exclusively in the meaning of hiding the location of the illegal proceeds, without any mention of layering techniques through financial transactions.

62. It should also be noted that the Money Laundering Act no. 80/1993 (as amended in 1999) includes, for the purposes of the preventative measures of the act, a definition of money laundering. However, this definition is slightly different and includes the word "conceal."

63. As far as *possession or use of property derived from a predicate offence* is concerned, this *actus reus* of the money laundering crime may be inferred from the concepts of acceptance and storage as stated in section 264. Another two provisions in the Penal Code complement the money laundering offence. Section 254 and Section 263 criminalise the intentional and the inadvertent retaining of valuables unlawfully acquired with an intent of pecuniary gain or a fraudulent intent (e.g. due to theft, embezzlement or fraud) as well as the assistance in retaining and the participation in the gain derived from such an enrichment offence. With respect to the money laundering crime, the *actus reus* of the

offence is of a more passive nature in this case - i.e. receiving and retaining - and the predicate offences are restricted to the enrichment offences listed in Section 254.

64. The provision on money laundering does not specify whether it extends to assets, which are not the direct proceeds of crime. However, pursuant to the case law – case n. *S-1635/2003* - the money laundering crime is conceived as encompassing any type of property, provided that it can be identified as direct proceeds of the predicate offence or as surrogates or income from such assets.

65. Nevertheless, section 264 also indicates that when the gain is of a minor character and no aggravating factors occur, a lawsuit shall not be brought before the court, unless so required by public interest. No further explanations are contained in the law, nor were the Icelandic authorities able to provide additional clarifications on what is deemed to be proceeds of a "minor" character because of the lack of any pertinent case law. It was clarified, however, that it would fall under court's competence to establish that amount on a case by case basis; there is no objective threshold in the legal provisions for determining what constitutes an offence of "minor character", which may not be prosecuted.

66. It is not required that a person be convicted of a predicate offence when proving that a property is the proceeds of crime, only evidence that assets are derived from a criminal acquisition is sufficient. This does not require proof, *inter alia*, of the exact circumstances of the crime. Prosecuting authorities clarified that in order to issue an indictment, it is sufficient to demonstrate that property can be considered, on reasonable grounds, the proceeds from a criminal activity. In spite of that, police investigators indicated that they should be able to prove some link between the predicate offence and the illegal gain beyond any reasonable doubts in order to build a money laundering case which can lead to a successful indictment and prosecution.

Predicate offences

67. Predicate offences for money laundering include all of those listed in the Penal Code as well as drug offences according to the reference contained in section 264, par. 4 to a *lex specialis*, the Narcotics Act n. 65/74. In addition, several other laws refer back to section 264 of the penal code, making offences in those laws also predicate offences for money laundering: the Alcoholic Beverages Act n. 75/98, section 27; the Medicinal (or Pharmaceuticals) Products Act n. 93/94, section 48, and the Customs Act n. 88/2005, section 171. Accordingly, unlicensed importation, selling and production of alcoholics and medicinal products as well as smuggling are predicate offences for money laundering.

68. According to the Penal Code, offences related to the securities market may be sanctioned by means of the fraud provisions (sections 248-254) if all the requirements for the fraud offence (e.g. fraudulent intent) are met. However, specific offences like insider trading and market manipulation are contained in the Act on Trade in Securities n. 33/03, so that they cannot separately constitute predicate offences for money laundering outside of the offences in sections 248-254. Arms trafficking related offences are also not included in the Penal Code and, accordingly, are not predicate offences for money laundering.

69. Participation in an organised criminal group and racketeering are not specific criminal offences, except in the case the organisation aims at the commission of terrorist acts or terrorist financing. This is one of the matters under consideration by the Criminal Law Committee, which was established in 1997 to advise the Ministry of Justice on matters involving criminal law and to undertake a revision of criminal legislation. Nor is the agreement among two or more people to commit any serious crime (conspiracy) – including the laundering of illegal proceeds– a specific criminal offence. In the view of Icelandic authorities, the general provisions of the Penal Code on attempt and participation are very broad and so far deemed as adequate to cover also this type of crime because they extend to even remote acts of attempt and preparation. Despite this, it is not clear that these ancillary offences fully cover all forms of conspiracy and therefore participation in the activities of organised criminal groups as required by Article 5(1)a(i) and 5(1)b of the Palermo Convention.

70. The money laundering offence applies to predicate crimes committed abroad. According to Sec. 4 of the Penal Code, the laundering of proceeds may be prosecuted on the basis of the Icelandic criminal law irrespective of the fact that they were generated by a predicate offence committed abroad and irrespective of who perpetrated it.

71. It is not clear whether the money laundering offence may apply to the person who also commits the predicate offence (i.e., self–laundering). No judicial rulings have been passed resolving this point finally. Icelandic judicial practice and academic writing on law has been based on the principle that it is not possible to convict the same individual for the further exploitation of the gains of a criminal act, and in particular an offence of an economic nature, *following* a conviction of that individual for the original offence. Section 77 of the GPC details the sentencing provisions when someone is convicted of two or more offences at the same time. Icelandic courts may conclude that under such circumstances, the offences are to be dealt with collectively in the sense that the punishment imposed for the original offence (i.e., "co-punishment") is regarded as adequate. Section 77 also allows for an increase in the penalty by up to one half. Iceland authorities indicate that the right course of action is to allow it to be put to the test when the occasion arises whether there is reason, taking into account the nature and seriousness of a money-laundering offence and Iceland's international undertakings in this area, to convict an individual for both the original offence and for the laundering of the gains derived. Since self-laundering could potentially be covered under current law, the evaluation team could not conclude that fundamental principles of domestic law are currently preventing it from being an offence.

Ancillary offences (conspiracy, attempt, aiding and abetting, facilitating, counselling the commission)

72. Attempt to commit any offence is defined and sanctioned by Sec. 20 (1) of the Penal Code. On the basis of this provision a lower penalty may be applied than for a completed offence, whereas penalty may be cancelled if the attempt could not have led to a completion of the crime because of inadequacy of the objective element of the offence. In the opinion of the evaluators this should not represent any actual challenge to prosecutions. According to the application of this provision by the courts, even remote acts of preparation and planning are sufficient to meet the prescribed requirement, provided that intent to carry out a particular crime can be proven.

73. Complicity and participation are covered on the basis of a general provision contained in Section 22 of the Penal Code, applicable to any offence. Paragraph 1 of this section reads as follows: "Any person who in word or deed provides aid in the commission of a punishable act defined in this Code, or takes, by persuasion, exhortation or otherwise, a part in committing such act, shall be punished as provided for in the provision applying to the offence." Pursuant to this provision and to Section 264, the latter explicitly covering the conduct of "assisting in the delivery of illegally obtained proceeds or contributing in other manner to secure them for others", aiding and abetting, facilitating and counselling the commission of the money laundering offence are adequately covered. If the offence is not completed, attempted contribution can also be punished.

74. As indicated above, conspiracy to commit money laundering is not fully addressed. In order to punish this conduct courts have insofar applied, in a combined manner, provisions on attempt and participation. However, no case law has been provided on this.

Additional elements

75. In general Section 264 of the Penal Code only applies to proceeds deriving from actions that constituted crime in the country where they were committed. However, pursuant to Section 6, Icelandic criminal jurisdiction is conferred over a wide range of offences committed abroad even if they are not punishable in the other country. Such cases refer to offences against the independence of the Republic of Iceland, its security, constitution or public authorities or against the interests of Icelandic citizens if committed outside the criminal jurisdiction of other states under international law as well as to offences envisaged in several Conventions to which Iceland is a party. If proceeds were produced as a result of these activities, the money laundering provision is applicable as well.

Recommendation 2

76. Sec. 264 applies to natural persons that intentionally and negligently engage in the laundering of illegal proceeds. As for the *mens rea* in the case of intentional offence, prosecutors need to demonstrate that the accused knew the criminal origin of the proceeds beyond any reasonable doubt. Knowledge, according to the explanations provided, encompasses direct intention, probable intent, and also wilful blindness and *dolus eventualis*. By the latter approach, situations where a person ignored risk after suspicion was aroused or consciously accepted the risk that his/her behaviour might lead to the commission of a crime, should be prosecuted.

77. The prosecution does not have to bear the burden of demonstrating actual knowledge of the illicit nature of the proceeds. The principle of the free evaluation of evidence allows the courts to infer the knowledge of the accused of the illegal origin of the proceeds from any objective factual circumstance resulting from the information gathered.

78. One issue of concern is that it seems that there is no legal mechanism to alleviate the burden of proof, so that knowledge of the specific criminal origin of the proceeds beyond any reasonable doubt seems extremely difficult to be proved. Statistics on prosecutions and convictions confirm that, as from year 2000 to April 2006 there have been only 14 money laundering cases prosecuted and sentenced. The only exception to this strict approach lies in the possibility of prosecution by a standard of negligence, but in this case only a fine or a minimum term of imprisonment – up to 6 months - can be imposed.

79. Act 144/98 on Criminal Liability of Legal Persons concerning Bribery amended Section 19 of the Penal Code and introduced the availability of corporate criminal liability in certain limited cases (i.e., in relation to bribery). This provision indicates that, if specified by Law, a legal person shall be ordered to pay a fine (a monetary penal sanction). The definition of legal person is broad and encompasses any entity, which is not a natural person, capable of enjoying rights and carrying duties under Icelandic Law. The term includes companies, public associations, enterprises, foundations, administrative authorities and institutions in general (Section. 19b). Section 19c indicates that a legal person can only be held criminally liable if its officers, employees or other physical person acting on his behalf, committed a criminal or unlawful act in the course of its business. Penalties would apply to the legal entity even if the identity of the natural person has not been ascertained. Furthermore, whether a criminal or unlawful act has been committed in the course of activities deemed to be comparable to the business of private entities, criminal liability also extends to administrative authorities.

80. The Act 144/98 also amended the Penal Code in several sections to specify for which crimes the legal entities may be fined: a) active bribery in the public sector (Section 109) and in the private sector (Section 264a, par.2) in the course of professional duties; b) money laundering, but only when the predicate offence is one out of these two corruption offences; and c) for terrorism (Sec. 100a), terrorist financing (Section 100b) and for any kind of support to terrorism (Sec. 100c), when these crimes are committed within its business or in its interest. Thus, while corporate criminal liability does apply for money laundering in a few cases, overall its scope is very narrow since it does not apply beyond money laundering relating to bribery.

81. Criminal responsibility of a legal entity does not preclude the possibility of holding concurrently liable any individual involved in the commission of the same offence. No civil or administrative liability regime is in place for the case where a legal person is convicted for money laundering. Nevertheless, in the limited situations where criminal liability of the legal entity for money laundering applies, parallel administrative or civil proceedings – e.g. claims for damages - are not precluded. The imposition of additional civil or administrative sanctions is possible, but it is carefully assessed when the court is deciding upon the total penalty, pursuant to the principle of proportionality. It is, however, unlikely that these additional sanctions are imposed through a parallel civil or administrative procedure separated from the criminal proceeding.

82. In this context, the only measure foreseen by Icelandic legislation is the withdrawal of licenses, in cases where a licence or authorisation is necessary for doing business, while there is no possibility, for instance, of imposing administrative pecuniary sanctions or the replacement of the board of management.

Sanctions

83. According to Sec. 264 of the Penal Code, the basic money laundering offence is sanctioned by a fine or imprisonment for a maximum of two years. In case of a reiterated offence or a more serious offence – when aggravating factors occur – a penalty of up to four years imprisonment can be imposed. In case of gain resulting from a drug offence, according to the reference to Section 173a made in par. 4 of Sec. 264 of the Penal Code, detention for up to 12 years can be ordered. On the other hand, if the penalty prescribed for the main offence does not exceed imprisonment for up to one year, the penalty for money laundering may be cancelled. This provision is consistent per se, but the main difficulty lies in the low level of penalties for money laundering.

84. Penalties appear to be low with respect to both international standards and the domestic provisions for other economic crimes, namely "enrichment offences", for example embezzlement or fraud (up to 6 years imprisonment). Likewise, penalties for negligent money laundering do not provide a significant disincentive since they are of a minor relevance (fines or imprisonment up to 6 months).

85. As indicated earlier, two other provisions in the Penal Code (section 254 and section 263) criminalise the intentional and the inadvertent retaining of valuables unlawfully acquired by means of an enrichment offence as listed in section 254 as well as the assistance in retaining and the participation in the gain derived from such a predicate crime. While for the latter (section 263) penalties are the same as for negligent money laundering, for the former (section 254) the term of imprisonment is twice as the one for money laundering (up to 4 years instead of 2).

86. The amount of fines that can be imposed is not specified in the law. According to Sec. 51 of the Penal Code, when deciding the amount of a fine, a court shall have regard for an offender's income and property and other factors affecting his/her ability to pay, so that the amount of the monetary sanction is determined by the court on a case by case basis according to the established principles.

87. In addition, Sec. 68 of the Penal Code provides legal basis for banning any person convicted of an offence to pursue an occupation for which an official licence, authorisation, appointment or examination is required, or even for depriving the same person of the related right, for up to five years or for life when he/she is no longer considered worthy of pursuing the occupation or enjoying this right.

Recommendation 32[14] (Statistics): money laundering investigation/prosecution data

88. There are generally no statistics on money laundering investigations. Statistics were provided on money laundering prosecutions and convictions, but there is not a comprehensive system in place for recording these data and making them easily accessible. From year 2000 to 2006 there have been 14 convictions for money laundering, but in the last two years neither convictions nor on-going cases were reported. Most of the cases and defendant pertained to a major drug investigation in 2000, when 11 out of 12 persons were convicted of laundering drug proceeds.

	2000	**2001**	**2002**	**2003**	**2004**	**2005**	**2006**	**Total**
Number of cases	5	0	1	1	2	0	0	9
Number of indicted persons	12	0	1	2	3	0	0	18
Number of convictions	11	0	1	1	1	0	0	14
Number of acquitted	2	0	0	1	2	0	0	5

[14] See Section 7.1 for the compliance rating for this Recommendation.

89. The following details were provided regarding the convictions:

2000	Sentence
receiving profit from drug trafficking of ISK 8.5 million. also convicted of import and sale of large amount of illegal drugs	9 years imprisonment
laundering ISK 8.5 million in drug proceeds, unlawfully retaining stolen objects and possession of illegal drugs.	16 months imprisonment
laundering ISK 8.5 million in drug proceeds	10 months; suspended for three years subject to no new offence being committed
laundering 780,000 in drug proceeds	4 months; suspended for two years subject to no new offence being committed
laundering NLG 36,500 in drug proceeds	4 months; suspended for two years subject to no new offence being committed
laundering ISK 6.15 million and buying and distribution of illegal drugs	15 months imprisonment
laundering ISK 361,434 of drug profit and possession of drugs	ISK 200,000 fine
laundering ISK 12 million of drug profit	18 months
laundering NLG 120,000 of drug profit	6 months; 4 months suspended for 3 years subject to no new offence being committed
laundering ISK 5 million of drug profit	4 months; suspended for two years subject to no new offence being committed
laundering ISK 36,500 of drug profit	no penalty decided (on account of age, health and connection with other defendants)
2002	**Sentence**
laundering ISK 956,500 and EUR 300 of drug profit; participating in drug trafficking	2 years; suspended for 3 years subject to no new offence being committed
2003	**Sentence**
laundering ISK 26 million from embezzlement and market manipulation	3 months imprisonment; suspended for 2 years subject to no new offence committed
2004	**Sentence**
laundering ISK 31.4 million from embezzlement	3 months imprisonment

90. According to the data provided, out of 14 convictions, 12 pertained to narcotic offences while the other two concerned embezzlement and, in one case, market manipulation as well. The global penalties ordered ranged from 9 years – in this case also including the penalty for importing and sale of illegal drugs – to a few months imprisonment with enforcement of penalty – fully or partly - suspended for two or three years for half of the cases. Only a fine of approximately 55% of the amount of the illegal proceeds was imposed in one instance.

91. Overall, it does not appear that the money laundering offence is being effectively applied. There is a limited use of the money laundering offence; nearly all money laundering prosecutions have been limited to drug money laundering cases. Sanctions available for money laundering do not appear effective, proportionate, and dissuasive—actual penalties applied have been low, even in cases involving narcotics trafficking where a penalty of up to 12 years is available.

2.1.2 Recommendations and Comments

92. Iceland should fully cover all the necessary predicate offences for money laundering, and conspiracy should be fully criminalised. The authorities should review domestic laws, and if necessary, adjust them to ensure that self-laundering is fully criminalised.

93. The authorities should consider lowering the standard of proof to demonstrate the *mens rea* in the money laundering offence by allowing prosecutors and lower courts to adopt a full range of mental element including every degree of knowledge. A "*should have known*" parameter may also be explicitly applied in cases when laundering is committed through a professional activity, like for instance, banking or accountancy.

94. There are a limited number of prosecutions and convictions since the broader provision on money laundering was adopted in the 1997. Specific training on money laundering investigations jointly with clear guidance by prosecutors on evidence requirements under Sec. 264 should be delivered to officials from law enforcement authorities.

95. Iceland should also raise the criminal penalties for money laundering, to be in line with those of other profit-generating offences in Iceland, which would further the use of the money laundering offence. Criminal liability of legal persons for money laundering offence should be expanded and extended to any predicate offence.

2.1.3 Compliance with Recommendations 1 & 2

	Rating	Summary of factors underlying rating[15]
R.1	**LC**	• Arms trafficking insider trading and market manipulation are not crimes in the Penal Code. Therefore, these actions cannot constitute predicate offences for money laundering. • Participation in an organised criminal group or racketeering is not separately criminalised and not a ML predicate offence; ancillary offences do not appear otherwise to cover adequately "participation" in the profit-generating crimes of organised criminal groups—conspiracy is not fully covered. • It is unclear whether self-laundering is adequately criminalised. • The offence is not effectively implemented, as witnessed by the limited number of indictments and convictions.
R.2	**PC**	• Penalties appears to be too low, especially in comparison with penalties for similar types of offences (e.g. enrichment offences (6 years)) and do not seem to be effective, proportionate and dissuasive. • Actual penalties applied have been low, even in cases involving narcotics trafficking where a penalty of up to 12 years is available. • Criminal liability of legal persons is very narrow. • The offence is not effectively implemented, as witnessed by the limited number of indictments and convictions

[15] These factors are only required to be set out when the rating is less than Compliant.

2.2 Criminalisation of Terrorist Financing (SR.II)

2.2.1 Description and Analysis

Special Recommendation II

96. Terrorist financing and general support to terrorism are criminalised by Sec. 100(b) and 100(c) respectively, that were introduced in the Penal Code, along with Sec. 100(a), by Act 99/2002. This Act primarily aimed to implement S/RES/1371(2001) and fulfil the obligations set out in the International Convention for the Suppression of Terrorist Bombings of 15 December 1997 and the International Convention for the Suppression of the Financing of Terrorism of 9 December 1999.

97. Pursuant to Sec. 100(b) "Anyone who directly or indirectly supports a person, an association or a group committing or having the purpose of committing acts of terrorism as per Sec. 100(a) by contributing funds or granting other financial support, procuring or gathering funds or making funds available in another manner shall be subject to imprisonment for up to 10 years." This definition of the terrorist financing offence is generally broad and does not require that the funds have actually been used for the purpose of carrying out a terrorist act. For prosecution purposes, it is sufficient to demonstrate that funds are collected or provided for the maintenance and operational expenses or more broadly for the benefit of either an individual terrorist or a terrorist organisation. Explanatory notes referring to this provision highlight the fact that terrorist activity need not be the organisation's sole purpose.

98. Despite this, the terrorist financing offence is not fully consistent with the wording of the CFT Convention, which defines terrorists acts as "(a) An act which constitutes an offence within the scope of and as defined in one of the treaties listed in the annex; or (b) Any other act intended to cause death or serious bodily injury to a civilian, or to any other person not taking an active part in the hostilities in a situation of armed conflict, when the purpose of such act, by its nature or context, is to intimidate a population, or to compel a government or an international organization to do or to abstain from doing any act" (Article 2 (1)(a) and (b)).

99. Sec. 100(a) of the Penal Code defines "acts of terrorism" as one of the specified violent offences when a) committed with the purpose of causing considerable fear to the public or to compel a government or an international organisation to do or to abstain from doing any act and b) can damage a State or an international establishment.

100. The primary issue lies in the definition of "acts of terrorism". Sec. 6 of the Penal Code indicates that all of the offences contained in all the various anti-terrorist Conventions and Protocols listed in the Annex of the CFT Convention are criminal acts in Iceland. However, Sec. 100(a) of the Penal Code separately defines "acts of terrorism" by specifying a list of violent offences. The specified acts refer back to offences contained in other sections of the Penal Code and include most offences that would be offences in the anti-terrorism Conventions and Protocols (indeed this was the intention), such as homicide, physical assault, deprivation of freedom, upsetting traffic safety, disturbing public transport, causing gross damage to property, hijacking aircraft, and arson. However, these acts do not fully cover all the offences contained in all of the Conventions and Protocols. For example, the Convention on the Physical Protection of Nuclear Material includes theft or robbery of nuclear material, and embezzlement or fraudulent obtaining of nuclear material. While these would be criminal acts in Iceland—since Sec. 6 specifies that all acts listed in the Conventions are offences—they are not separately designated as "acts of terrorism" pursuant to Sec 100(a); therefore, financing these acts would not constitute a criminal offence of FT in Iceland.

101. Another difficulty arises from the purpose elements required. Article 2 (1) (a) and (b) of the CFT Convention lists two separate categories of offences as terrorist acts (i.e., those in the Annex or any other offence intended to intimidate/coerce, etc.). However, the Icelandic law requires that both of these elements are met—i.e., that they be one of the specified offences *and* that they be conducted for the purpose of intimidating/coercing the government, etc. Further, Sec. 100(a) requires the condition that the

act "in light of its nature or having regard for circumstances it is committed can damage a State or an international establishment. This represents a restrictive clause which introduces a certain degree of vagueness and discretion in the legal provision, which may substantially challenge the prosecution of the terrorism and terrorist financing offences by imposing an additional burden of proof.

102. The funding of a terrorist act directly – without transferring funds to any terrorist individual or organisation – is not specifically addressed by Sec. 100(b). The legal construction of this article requires evidence of a receiver of the funds. This situation would be covered by applying the provisions on complicity to terrorism (with a penalty of 10 years imprisonment) according to Sec. 22 (on complicity) vis-à-vis Sec. 100(a) of the Penal Code – or, in case the terrorist act is committed by the same person who also funded it, by prosecuting the accused for terrorism only. Authorities indicate that the "complicity" approach would be followed in cases where the evidence shows that the *mens rea* was more likely to be part of the financing of a particular act of terrorism, and hence Sec. 22 vis-à-vis 100 (a) would be used. When such an intention cannot be ascertained, the person would be prosecuted under Sec. 100(b). This approach is not fully in line with the Interpretative Note to SR II, which specifies that using ancillary offences to terrorism is not adequate for the purposes of criminalising terrorist financing. Since no prosecution or investigation for terrorist financing has yet occurred in Iceland, no case law is available.

103. The law itself does not define the term "funds," but according to the clarifications provided it would encompass any valuable, since the original Icelandic term is very broad and may refer to assets of every kind, whether tangible or intangible, movable or immovable, however acquired, and legal document and instrument in any form, including electronic or digital, whether from a legitimate or illegitimate source.

104. Sec. 100(c) complements the provision on terrorist financing by punishing with imprisonment for up to 6 years any other kind of support, provided by any means, to an association or a group having committed or with the aim of committing one or more violations of Sec. 100(a) or Sec. 100(b).

105. The ancillary conduct that should be criminalised according to the TF Convention is appropriately addressed through the general provision on complicity as well as through Sec. 100(c). The attempt to commit terrorist financing is covered by Sec. 20 of the Penal Code, which is applicable to any offence.

106. Like any other crime in the Penal Code, terrorist financing (as defined) can constitute predicate offence for money laundering. Furthermore, if the terrorist individual or organisation is located outside Icelandic jurisdiction or the terrorist act occurred abroad, the financier can be prosecuted on the ground of Sec. 100(b). The legal basis for that is set out by Sec. 6 points 16 and 17 of the Penal Code, which envisage a specific provision on the terrorist offences as outlined in the Convention for the Suppression of Terrorist Bombings as well as the TF Convention. In such cases penalties have to be imposed according to Icelandic legislation even if the offence has been committed abroad and irrespective of the identity of the offender.

107. Terrorist financing is an offence which implies a knowledge element, which can be inferred from factual circumstances on the ground of the established principle of free evaluation of evidence by the court.

108. Criminal liability of legal persons committing crimes against Sec.100(a), (b), (c) of the Penal Code is provided by Act 144/98 and does not preclude parallel civil or administrative proceedings.

109. Penalty for perpetrating terrorism acts as defined by Sec. 100(a) is imprisonment for life whereas terrorist financing is sanctioned with detention for up to 10 years. Therefore, the available sanctions appear proportionate and dissuasive.

110. It is difficult to assess effectiveness of the provisions on terrorism and terrorist financing since no case law exists with this respect. It is also impossible to judge effectiveness based on ongoing investigations, as no suspicious transaction related to these phenomena has yet been sent to the FIU.

2.2.2 Recommendations and Comments

111. Iceland should review its legislation to ensure that the financing of terrorist acts directly is included in the FT offence. Iceland should also broaden its definition of terrorist act to include all those activities referred to by Article 2 (1)(a) and (b) of the CFT Convention. Iceland should also remove the purpose elements—i.e., the need to demonstrate that the act occurred for the purpose of intimidating/coercing of a government, etc, and the need that the act also to be able to damage a State or international establishment in order for acts under the Convention to be valid FT offences.

2.2.3 Compliance with Special Recommendation II

	Rating	Summary of factors underlying rating
SR.II	**LC**	• Financing of a terrorist act directly is not specifically covered by Sec. 100(b), although it appears most cases would be covered by other provisions. • The definition of "acts of terrorism" does not fully cover all those activities Article 2, par.1 of the CFT Convention; the financing of acts not specifically designated as terrorist acts in the Penal Code (but within the Annexes of the Convention) would not be criminal acts in Iceland. • The need to show that the act was committed for the purpose of intimidation/coercion, and the need to show that the act could damage a state or international establishment further limits the scope of FT offences and their effectiveness.

2.3 Confiscation, freezing and seizing of proceeds of crime (R.3)

2.3.1 Description and Analysis

Recommendation 3

Confiscation of proceeds and instrumentalities

112. The provisions on confiscation cover proceeds from all offences, objects used or intended to be used in or produced by a criminal offence and seizure of objects or other assets. Confiscation in Iceland is a non-mandatory penalty which can be ordered by a court when requested in the prosecutor's indictment (Sec. 116 of the Code of Criminal Procedure, Act n. 19/1991). It does not affect the determination of a penalty in a criminal case.

113. A general provision on confiscation is contained in Sec. 69 of the Penal Code, which covers proceeds and instrumentalities used in any criminal offence, including the money laundering offence. Objects created through an offence or used for its commission may be confiscated, except if they are in the ownership of a person not involved in the commission of the offence. However, if these assets are acquired by third parties after the crime has been committed, prosecuting authorities can apply for a confiscation order, provided their knowledge of the criminal origin of the assets can be proven. With this respect the Icelandic Code of Criminal Procedure does not allow for any alleviation of the burden of proof in cases when there is a gift made, or inadequate value given, in exchange for the property, or the asset is acquired by a spouse, nominee or corporate owner.

114. Objects that are deemed to be intended for a criminal purpose may also be confiscated to prevent the continuation of the offence, as for instance in the case of things whose selling, manufacturing or possess is generally forbidden (narcotics, counterfeited money) or are dangerous in nature (arms). Sec. 69 also provides for the confiscation of objects or proceeds of crime to which no party has a lawful claim. Properties of organisation criminal in nature can be forfeited provided the requirements of Sec. 69 are met, since it is not necessary that a crime has actually been committed.

115. The meaning of the term object, according to the Icelandic language, is broad enough to encompass money, goods and any other movable and immovable asset.

116. Confiscation applies to direct and indirect proceeds - i.e. the monetary amount corresponding to such proceeds - of any offence. Whether the exact value of the proceeds, meant to encompass all economic benefits from the offence, cannot be proved, courts may assess the amount thereof and are allowed for issuing a value confiscation order. Such an order is based on an estimated value, believed to be equivalent to the profit of the sale of the confiscated property.

117. As a main rule proceeds of crime cannot be confiscated without a criminal conviction of the perpetrator, although in certain cases this is not necessary before an application for a confiscation order: evidence that a crime has been committed is deemed to be sufficient, even if the perpetrator has not been identified. Except for this, the prosecutor generally needs to prove that the assets sought to be confiscated derived from the commission of the offence for which the accused has been found guilty on the basis of the normal criminal standard of proof, i.e. beyond any reasonable doubt. Evidence of the amount of criminal proceeds is not required since the court can assess it as previously described. The Icelandic legal system does not allow for a civil forfeiture.

118. The mentioned provisions apply equally to all property, regardless of whether it is held by the criminal defendant or by a third party, even though the burden of proof lies entirely on prosecutors according to established case law; there are no situations where this burden can be lowered or reversed. The question of shifting the burden of proof in some confiscation cases - for instance where a person is convicted for serious offences, or when the concerned property is owned by spouses or nominees - is

nevertheless under consideration within the AML Consultation Committee. In fact, this was a recommendation made in the second FATF mutual evaluation report on Iceland, in 1998.

119. Confiscated properties confer to the State Treasury, even though third parties who have suffered a loss from the offence shall have priority to the proceeds when compensation cannot be obtained by other means.

Provisional measures

120. At any time during an investigation, prosecutors and police can seize assets in accordance with Sec. 78 of the Code of Criminal Procedure. Any objects or documents that – on reasonable grounds - may be assumed to be of evidential value in criminal proceedings, that have been obtained by criminal means or that may become subject to confiscation can be seized. This includes any movable asset, like for instance bank, financial or commercial records. A court order is not needed to seize the property; usually, a well founded suspicion that a crime has been committed is sufficient to have the provisional measure approved by the court. The application for seizing can be made *ex parte* or without given prior notice; notice will not be given unless it is certain the assets could not be removed. Although seizure is a temporary measure, once executed it can stay in effect until necessary without any time limit.

121. Even though Sec. 78 of the Code of Criminal Procedure refers to different words than those used in the confiscation provision of the Penal Code (Sec. 69), in the original Icelandic text the terms have the same scope. The result is that all proceeds and instrumentalities of crime can be seized and forfeited. Property of seized funds and assets remains to the original owner; however, possession and control is assigned to the police which collect properties and maintain them in a special compound.

122. Beside a general provision according to which seized property shall be registered and securely stored, there is no specific regulation in place on the management of property which has been seized or confiscated.

123. The Code of Criminal Procedure (Sec. 85) contains another provisional measure; it allows an investigator or prosecutor to bar a suspect from disposing of his property in value in order to obtain security for a fine, compensation, legal costs, or confiscation, if the property is deemed to be in danger of being secreted, lost or significantly reduced in value. This "arrest" does not require that an investigation has started, but the person has to be reasonably suspected of an offence. There also have to be reasonable grounds to impose these restrictions at a very early stage. In practice, there is the need to demonstrate a reasonable cause to anticipate the disposition or removal of property. This measure may also be applied at a later stage of the proceeding with the aim to secure a payment.

124. This type of restraining order is an administrative measure which operates in similarly way to freezing orders. In practice it is used only for immovable properties. The order is issued against a suspect and registered in a public registry by a "maghistrati" (notary public) and does not require an intervention by a judicial authority. Civil law rules apply; the lien on assets is publicly registered and cannot be disregarded. Therefore, the person subject to it would in practice not be able to sell the property to third parties; nor would third parties be able to claim good faith. Additionally, criminal responsibility for fraudulent setting may be charged to the seller according to Sec. 250 of the Penal Code.

Powers to identify and trace property

125. Law enforcement authorities generally have adequate powers for identifying and tracing property that may become subject to confiscation, from the very early stages of the criminal proceeding. Nevertheless, except for the case where a suspicious transaction is reported to the FIU, investigative authorities need a production order by the court to obtain customer and transactions documents and records from financial institutions.

126. For the purpose of an investigation, police authorities may be authorised by judges to record telephone conversations or images, to monitor other sounds and signals as well as to take photos, without

knowledge of the person concerned. An affirmative decision by a court, with this respect, usually depends on two factors: the high relevance of the information to be acquired with these means for the investigation; and the seriousness of the alleged offence (penalty should be provided for not less than 8 years imprisonment, or important public/private interests require the measure to be taken). Once authorised, the measure can stay in effect for a limited lapse of time as decided by the court.

127. As for search powers, any premises of a suspect, including places for storage and ships, may be searched for the purpose of arresting him, to investigate the scene of a crime, or to obtain evidence to be seized. Search may also take place regardless of any suspicion when the person has been arrested in a certain place or when there are reasonable grounds that he/she is staying there or that items and evidence may be found there. Unless there is a danger of evidence being prejudiced, the search can be executed by police investigators only upon a judge's decision.

128. Statistics on property frozen, seized and confiscated, related to money laundering and underlying offences were not kept. Any other data or information was not available on this issue.

3.2.3 Recommendations and Comments

129. While the framework provides investigators and prosecutors with basic confiscation and provisional measures, the main issue is framework's effectiveness. The burden of proof appears to be too high for prosecutors, since they must prove—beyond a reasonable doubt—that proceeds resulted from the specific crime for which the accused has been convicted. Provisions on confiscation should be strengthened especially when the offender is not in possession of the assets, which are held by a third party.

130. Authorities should consider measures that require confiscation of property held by a perpetrator convicted of a serious offence generating profit, unless the offender can prove that the property was legally obtained (reversal of burden of proof). This would be particularly significant in confiscation cases relating to drug trafficking or other serious crimes or situations where properties are held by third parties.

131. Beyond this, authorities may also consider reducing the burden of proof when executing a forfeiture order after conviction, e.g. by adopting "a balance of probabilities approach" or other standard lower than the criminal standard.

132. Notwithstanding the fact that the previous mutual evaluation report pointed out the need to thoroughly review the Icelandic confiscation regime, identified shortcomings have not yet been addressed. Icelandic authorities should give higher priority to confiscation of criminal property.

133. The lack of any quantitative data makes it impossible for examiners to form an opinion about the amount of illegal money recovered through confiscation.

2.3.3 Compliance with Recommendation 3

	Rating	Summary of factors underlying rating
R.3	**LC**	• The high burden of proof lying on prosecutors inhibits effective implementation of the confiscation provisions. • The lack of any data or other information on results does not allow the examiners to be satisfied that the confiscation provisions are effective. • There are some indications in the whole system that confiscation of criminal property is treated as a low priority issue.

2.4 Freezing of funds used for terrorist financing (SR.III)

2.4.1 Description and Analysis

Special Recommendation III

Laws and procedure for freezing funds under S/RES/1267/1999 and S/RES/1373/2001

134. Legislative measures adopted to fight terrorism in pursuance of S/Res/1373(2001) include Public Announcement 867/2001, enacted on the basis of Act 5/1969; Act 99/2002 which enacted into the Penal Code the substantive part of the Resolution by introducing Sec. 100(a), (b) and (c); Act 15/2003 amending Law 87/1998 on Official Supervision of Financial Operations.

135. Act 5/1969 Concerning the implementation of decisions taken by the United Nation Security Council authorises the government to take measures (through a "Notice" or "Public Announcement, depending on the translation) necessary to implement UN Security Council decisions. Violations of the Act or instructions issued pursuant to are subject to a fine or imprisonment of up to two years, unless heavier penalties apply under other legislation (Sec. 2).

136. Using this legislation, Icelandic government gave effect to S/RES/1267(1999) by enactment of a first Public Announcement issued by the Ministry of Foreign Affairs, which was later replaced by Public Announcement 349/2002 (of 29 April 2002). The Announcement forbids Icelandic citizens and legal entities, foreigners who live in Iceland and foreign entities engaged in activities in Iceland to supply any weapons or technical and military assistance as well as to make any funds available to the benefit of the Taliban and Al-Qaida affiliates as named in the Annex to the Notice. It also provides penalties for any breaching of the provisions contained therein by reference to Sec. 2 of the Act 5/1969. The latter imposes fines or imprisonment up to 2 years, if no heavier penalties are provided in other laws. The Annex then lists the persons and entities designated by the United Nations.

137. Although they have been sometimes indicated as a temporary measure, Public Announcements are legislative act which may stay in effect indefinitely.

138. With the aim of implementing S/RES/1373(2001), Public Announcement 867/2001 (of 14 November 2001) applies to the same range of subjects as stated in Announcement 349/2002. The subjects "may not raise funds or acquire other assets for the purpose of financing terrorist activity, "which is punishable according to Chapters XVIII, XXIII, and XXIV of the Penal Code"[16] (Item 1). Neither may they supply funds or other assets, in their safekeeping which "belong to persons who commit or attempt to commit the offences cited in Item 1, or which belong to persons who have participated in such offences or who have facilitated such offences by other measures. The same applies to funds or other assets belonging to legal entities that are owned by such persons, and funds and other assets belonging to persons who work on their behalf. It also prohibits establishing accounts, administering property, or providing any kind of direct or indirect service involving financial resources or other assets. The Announcement also obliges natural and legal persons who are authorised to provide financial services to the public to report suspicious transactions that might be linked to terrorist activities to the National Commissioner of the Police.

139. A more direct freezing obligation (which could apply to persons designated in the context of either S/RES/1267 of S/RES/1373), and a mechanism to enforce it by means of the FSA supervisory structure, has been introduced by Sec. 16(a) of the Act 87/1998 on financial supervision, as amended in 2003. According to that provision, parties which are under the supervision of the Financial Supervisory Authority (FSA) - cf. Article 2 of Law No 87/1998 - are obliged to freeze funds or assets of persons and legal entities included in the lists transmitted by the FSA: "In accordance with international obligations

[16] These chapters refer, respectively, to acts causing danger to the public, manslaughter and bodily injuries, and offences against personal freedom.

or conventions to which Iceland is a party, the FSA shall issue notices listing certain individuals and legal entities; regulated entities must check specifically as to whether they have established business connections with these parties and are obliged to prevent any financial transfer, such as the delivery of funds, withdrawals, transfers, asset registration or other dealings, thus preventing those parties listed in notices from the Authority from receiving any payment or being able to make us of funds by other means." The FSA is also required to notify the National Commissioner of Police if freezing has not been conducted in the correct manner and funds will be seized by the police pursuant to Sec. 78 of the Code of Criminal Procedure.

140. Iceland does not have effective laws and procedures to give effect to freezing designations in the context of S/RES/1373. While the Announcements creates a basic legal framework give effect to S/RES/1373, the Announcement's definition of terrorism and all subsequent obligations are limited to certain violent acts in the Penal Code. It therefore does not fully cover all persons who commit or attempt to commit terrorist acts. While it covers entities that are owned by terrorists etc, it does not specifically cover funds of entities that are *controlled* directly or indirectly by such persons, although, this may be partly covered by the category of funds or other assets "belonging to persons who work on their behalf." Nor does it cover funds or other assets derived or generated from funds or other assets owned or controlled directly or indirectly by designated persons, terrorists, those who finance terrorist, or terrorist organisations.

141. Furthermore, while the more direct obligation to freeze funds contained Sec 16(a) of the revised Law 87/1998 could apply to designations in the context of either S/RES/1267 or S/RES/1373, the law and corresponding structure to enforce it applies only to entities supervised by the FSA. Therefore, it appears that there is not a mechanism to enforce the freezing obligation for designations in the context of S/RES/1373, if any were made, for entities that are not supervised by FSA. In addition, this provision allows only for the FSA to forward lists pursuant to international obligations. As a practical matter, as described below, the only lists that can be enforced are those from the 1267 designation committee.

Communication to financial institutions and procedures

142. The procedure starts at the Ministry of Foreign Affairs which receives, in accordance with international obligations or agreements, lists which contain names of persons or legal entities suspected of being linked to terrorism. Any list received is forwarded to the Financial Supervisory Authority (FSA). The UN lists are also published in the Icelandic Official Gazette. The FSA immediately sends out the lists to financial institutions and other parties subject to its surveillance and also maintains them on its own web-site along with some instructions on obligations.

143. There is not a national mechanism to designate persons in the context of S/RES/1373. The Ministry of Foreign Affairs does not review or screen the lists received, and no distinction has been made about the content of the obligations for financial institutions, so that the duty to freeze funds and assets apply to any persons included in any list forwarded. Neither the Ministry nor any other authority plays a role in the designation process at domestic level; no national terrorists have been designated.

144. The UN and EC lists are also published on the FSA website along with a summary of the legal requirements. It is stated that in order to freeze funds there is no need to have them previously seized; however, neither Art. 16(a), regulation nor guidance provide more specific instructions as to the freezing mechanism. So, for example, it is not required that the action take place without delay and without prior notice to the persons involved.

145. At the time of the on-site visit, no guidance had been provided to the financial sector on the reporting obligation about suspicious transactions that may be linked to terrorist financing. However, the FSA were planning to release such guidance once the new AML/CFT Act was approved by Parliament. After the on-site visit, this new law was enacted and came into force on 22 June 2006. Authorities later reported that the FSA was in the process of developing an MOU with the Ministry of Foreign Affairs relating to this issue.

146. To date the FSA has notified the financial sector about several EU lists, mainly those imposing restrictive measure on Burma/Myanmar and Zimbabwe and the lists approved by the 1267 Taliban and Al-Qaida Sanctions Committee. It was however not clarified to the evaluation team how the EU lists are actually implemented. The lists include:

- Council Decision 2003/461/CFSP, implementing Common Position 2003/297/CFSP on Burma/Myanmar;
- Council Decision 2004/161/CFSP renewing restrictive measures against Zimbabwe;
- Council Decision 2004/423/CFSP renewing restrictive measures against Burma/Myanmar.

147. The evaluation team noted that these Council Decisions were not related to FT. Apart from these EC decisions, Iceland has not yet received any requests to examine and give effect to actions initiated under the freezing mechanisms of other jurisdictions; however there is not a comprehensive mechanism in place to examine and give effect to such actions. Iceland does not take part in the EU mechanism for screening, amending and updating any list of person and entities suspected to be connected with terrorism. While authorities indicated that there was a clear legal basis for enforcing freezing orders originating from the UN Security Council, this was less clear for those actions indicated under freezing mechanisms of other jurisdictions.

148. In any other case outside the designation in a list, where a person may be suspected of having committed or taken part to terrorist acts, financing or supporting terrorism, the provisions of the Code of Criminal Procedure on seizure and confiscation apply.

149. There are no formal procedures at national level for evaluating de-listing requests, for releasing funds or other assets of persons or entities erroneously subject to the freezing and for authorising access to frozen resources when deemed necessary for basic expenses, the payment of certain types of fees, etc pursuant to S/RES/1452(2002). Nevertheless whether the FSA receives a notification from the Ministry of Foreign Affairs regarding de-listed persons or entities, the FSA forwards that notification to supervised financial institutions. To date no cases of funds or assets freezing have occurred, but as a matter of fact financial institutions would unfreeze the concerned property only if a formal notification from the National Commissioner of the Police or from the FSA would be received. As a general rule, all administrative decisions can be challenged before a court according to Art. 60 of the Constitution. However, there is no specific provision or procedure enabling a person or entity to challenge a freezing decision with a view to having it reviewed by a court—it is assumed that the entity frozen will use the same legal mechanisms that any citizen has at its disposal to challenge governmental decisions. . Nor are there specific measures to protect the rights of bona fide third parties consistent with Article 8 of the CFT Convention.

Sanctions for non-compliance and monitoring mechanism

150. Both Public Announcement 349/2002 and 867/2001 provide for penalty of fines or detention for up to 2 years for any breach of freezing and reporting duties as set out by the announcements.

151. Supervisory powers and duties assigned to the FSA pursuant to Article 9(1) of the Act on Official Supervision of Financial Operations, may extend to CFT requirements as well, including the duty to freeze. Therefore, parties subject to the supervision of the FSA are obliged to grant it access to accounts, minutes, documents and any other information in their possession as deemed necessary. However, the FSA has not performed any specific off-site or on-site monitoring of compliance with CFT obligations so far.

2.4.2 Recommendations and Comments

152. As a priority issue Iceland should establish a central authority at national level to examine, integrate and update the received lists of persons and entities suspected to be linked to international terrorism before sending them to the financial sector. More broadly, a domestic mechanism to enact S/RES/1373(2001) should be implemented to be able to designate terrorists at a national level as well as

to give effect to designations and requests for freezing assets from other countries. Likewise, Iceland should adopt procedures for evaluating de-listing requests, for releasing funds or other assets of persons or entities erroneously subject to the freezing and for authorising access to frozen resources pursuant to S/RES/1452(2002). Subsequent to the on-site visit, the evaluation team was informed that the AML/CFT Consultation Committee is contemplating remedies for these areas, and that the Ministry of Foreign affairs was also looking into these issues including the EU, lists from other countries, and de-listing issues.

153. Authorities should also release practical guidance to the financial institutions concerning their responsibilities under the freezing regime as well as for the reporting of suspicious transactions that may be linked to terrorist financing. The team received assurances from representatives of the FSA that such guidance will be issued now that the AML/CFT Act 2006 has been adopted by the Parliament and has entered into force.

154. Whereas the prohibition in dealing with or providing assets to terrorists is generally comprehensive under Act 5/1969 and the Public Announcements, the direct obligation to freeze funds of persons and entities designated in the context of S/RES/1373 applies only to financial institutions supervised by FSA. This should be broadened to apply to all financial institutions and DNFBPs.

2.4.3 Compliance with Special Recommendation III

	Rating	Summary of factors underlying rating
SR.III	**NC**	• Overall, Iceland does not have effective laws and procedures to give effect to freezing designations in the context of S/RES/1373. • There is not a national mechanism to designate persons in the context of S/RES/1373, nor a comprehensive mechanism in place to examine and give effect to actions initiated under the freezing mechanisms of other jurisdictions. • The Public Announcement's definition of terrorism and all subsequent obligations are limited to certain violent acts in the Penal Code, which do not fully cover all persons who commit or attempt to commit terrorist acts. • There is not a mechanism to enforce the freezing obligation for designations in the context of S/RES/1373, if any were made, for entities that are not supervised by FSA, such as money exchange and money transfer and non-financial business and professionals. • The freezing obligation in Law 87/1998 allows only for the FSA to forward lists pursuant to international obligations. As a practical matter, the only lists that can be enforced are those from the 1267 designation committee. • The Announcement implementing S/RES/1373 does not cover fully freezing funds associated with terrorism, etc; nor does it not specifically cover funds of entities that are *controlled directly or indirectly* by such persons, nor funds or other assets derived or generated from funds or other assets owned or controlled directly or indirectly by designated persons, terrorists, those who finance terrorist, or terrorist organisations. • It is not required that action take place without delay and without prior notice to the persons involved. • There are no formal procedures at national level for evaluating de-listing requests, for releasing funds or other assets of persons or entities erroneously subject to the freezing and for authorising access to frozen resources when deemed necessary for basic expenses, the payment of certain types of fees, etc pursuant to S/RES/1452(2002). • No specific measures to protect the rights of bona fide third parties consistent with Article 8 of the CFT Convention. • Even though the freezing obligation is already in place for financial institutions concerning persons and entities on the lists distributed by the

		FSA, no practical indications have been released to clarify related duties and responsibilities.

Authorities

2.5 The Financial Intelligence Unit and its functions (R.26, 30 & 32)

2.5.1 Description and Analysis

155. The Icelandic Financial Intelligence Unit (FIU) is a unit within the Economic Crime Unit (Ríkislögreglustjórinn) at the National Commissioner of the Icelandic Police. As of the time of the on-site visit, there was no Icelandic law or regulation which explicitly created the FIU; the FIU function was derived from Article 7 of the Act on Measures to Counteract Money Laundering, No. 80/1993, as amended by Act No. 38/1999 which states, " … [An individual or legal entity referred to in Article 1 is obliged to]1) have any transactions suspected of being traceable to a violation [as referred to in Article 2]1) carefully examined, and shall notify [the National Commissioner of Police]1) of any transaction considered to be so related. Upon the request […]1) of police investigating cases of money laundering, any information deemed necessary on account of [such notification]1) shall be provided."

156. Since the on-site visit, some further structure for the FIU is provided for in a new Regulation 626/2006 of 12 July 2006 (issued pursuant to the new AML/CFT Act of 22 June 2006). It defines a specific "Money Laundering Office" as "the unit within the Economic Crime Unit within the National Commissioner of Police where notifications of suspicious practices are received and examined."

157. When the FIU was initially formed, all suspicious transaction reports (STRs) were forwarded by the various reporting entities, identified in Article 1 of the Act on Measures to Counteract Money Laundering to the Department of Public Prosecutions (DPP) for further dissemination to law enforcement. This practice of sending STRs was noted in the Second FATF Mutual Evaluation of Iceland in February 1999. However, since that time the practice has changed and the DPP no longer handles or receives the STRs from the reporting entities. The STRs are now forwarded directly to the FIU which processes and analyses the information for any underlying criminal activity. Pursuant to its analysis, the FIU may also request additional information from the reporting entity (as per Article 7 of the Act on Measures to Counteract Money Laundering, No. 80/1993 and amended in 1999) and disseminate these reports as required.

158. The general procedure for receiving and disseminating STRs is as follows. Normally STRs begin with an informal inquiry from the financial institution as to whether or not to file. If there was any doubt about the transaction it would lead to a formal STR, which would be registered in the FIU database. At this point the FIU might request the sender for additional information, and also checks for information in other databases (described in greater detail below). Then a decision is made as to whether to move forward with the case or to simply keep the STR registered for intelligence purposes. If the former is decided, the STR is sent to local investigating police (each police chief would then decide if there would be an investigation) or to others in the Economic Crime Unit to open a formal investigation. Depending on the course of the investigation, that Unit would then decide whether to pursue formal charges. However, there were no statistics to indicate how often or how many STRs were referred either to either local police or the Economic Crime Unit.

159. Since the on-site visit, this process of receiving and recording STRs has been further clarified in the new Regulation 626/2006 of 12 July 2006. Article 7 indicates that investigations shall be carried out on the basis of notifications received, and as appropriate, the gathering of information; these shall be the basis of the decision as to what the FIU shall do with the STR—delete the STR, record it in a special database, open a formal investigation, or block the transaction.) When a transaction is blocked, this investigation should be carried out quickly.

160. Authorities also indicated that the FIU has a contact officer in each police district in order to ensure that all information which might be of interest is exchanged. From time to time regional meetings are held with these officers to update on money laundering issues and discuss information needed for the work of the FIU. The FIU also has a telephone service where anyone covered by the Money Laundering

Act can phone to discuss whether or not to send a STR without having to reveal information on the customer's identity.

Guidelines on the manner and form of reporting

161. The FIU appears to have a very good rapport and working relationship with the various banking institutions in the country. The FIU has met with representatives of the financial institutions and provided them with informal "verbal" guidance regarding their reporting obligations pursuant to the Act on Measures to Counteract Money Laundering, No. 80/1993. However, the FIU has not yet issued any written guidelines to either the financial institutions or to the Designated Non-Financial Business Professions (DNFBPs) within the country. Furthermore, the FIU has not set out a standardised reporting format which can be used by the reporting entities to file an STR. At the present time the form of an STR is left up to the entity sending the report.

162. This absence of standardisation also holds true vis-à-vis the reporting process of filing an STR itself. A typical reporting scenario is as follows: a bank contacts the FIU by phone and advises them that an STR is forthcoming. The bank will then choose one of the following methods to send it: (1) a letter, (2) courier, (3) an e-mail or (4) a fax, or a combination thereof. Upon receipt of the STR the National Commissioner of Police, i.e. FIU is then required pursuant to Article 8 of the MLA 1999 to, "… *confirm in writing the receipt of notifications pursuant to Article 7... The Commissioner shall send notice without delay if no reason is seen to prevent the transaction."* The same provisions are included in Article 19 of the new AML/CFT Act 2006. During the assessment team's meeting with representatives of the National Commissioner of Police and the FIU they stated that the reason that a "standardised" reporting process had not yet been developed was due to the fact that they relied a great deal on the personal relationships which they had fostered with banking personnel. The FIU added that when reporting entities are looking for clarification and guidance they are simply told to refer to the law. On the other side of this were representatives of the banking sector who stated that they would certainly prefer a "standardised format" for the reporting of STRs. In this regard, a new provision is included in Article 3 of the Regulation 550/2006 for the new AML/CFT Act. It specifically authorises the Economic Crime Unit to provide instructions on form and content of such reports and issue a special form for this purpose. The new Regulation 626/2006 "On the handling of Notifications of alleged money laundering" also indicates that the Notifications of suspicious transactions shell be sent in the form of letters or fax messages, or in electronic or digital form" (Article 5).

163. According to representatives of the financial sector, the FIU has generally been very accessible by telephone to answer any questions. The FIU has also been prompt in providing written confirmation of STRs received, as required by Article 7 of the Act. However, banking sector also indicated that "feedback" regarding the status of filed STRs, i.e. investigations, charges, seizures, etc. has been more limited. The private sector would also welcome a time limit placed on the FIU for reporting back to the financial institutions regarding suspicious transactions. This view is based on situations whereby banks had identified suspicious transactions, filed a report and were required to wait for the FIU to get back to them with a determination of whether or not a transaction should be allowed to proceed. In cases where an FIU response was delayed, (more than two days), the financial institutions were placed in the precarious position of having to determine whether or not a transaction should be allowed to continue or not. There was no statistical data available that illustrated the number of transactions which had been halted or permitted to continue.

Access to information

164. Upon receiving STRs the FIU has the ability to access numerous databases both directly or indirectly, e.g. information on police intelligence, criminal records, passports, vehicles, driver's license, companies and enterprises. They also have access to the Schengen system, the Egmont Source Web, Interpol and Europol. It is also planned to provide the FIU access to the World-Check database. Access to the aforementioned databases assists the FIU in analyzing any suspicious transaction reports that they receive. If further information is required from a financial institution that has filed an STR, the FIU has the ability to make additional inquiries with the reporting institution and obtain the necessary information.

165. In the view of the assessment team, the FIU does not appear to have any impediments, vis-à-vis their ability to access the information it needs to meet its mandate. If an STR is filed, there is no requirement for the FIU to obtain a judicial authorisation to acquire additional information from the reporting institution. Article 7 of the Act on Measures to Counteract Money Laundering ("MLA 1999") states that the FIU may obtain all information related to an STR from a reporting entity by way of a written letter. A similar obligation to provide all requested information is laid out in Article 4 of Regulation 550/2006 (for the new AML/CFT Act) of 27 June 2006. Information provided includes a description of the basis for the suspicion, information concerning the suspects and third parties involved (if any), account data (if any), data on the movements on the account, data on the nature and size of the transaction, whether the transaction has actually been carried out, to whom the funds are to be transferred and the origin of the funds.

166. However, in the absence of an STR, both the FIU and law enforcement must obtain a production order from a court pursuant to Article 89 of the Code of Criminal Procedure, No. 19/1991 to acquire the information from a financial institution.

167. According to Icelandic law enforcement and the FIU, there has been no reported case of a court refusing to grant judicial authorisation, i.e. production orders for information that was needed for investigative purposes. Representatives of the financial sector echoed this sentiment by adding that they have received a number of production orders from law enforcement for various records and documents and they have fully complied with the requests. The statistics regarding the exact number of production orders executed was not available.

Dissemination of information

168. The FIU is itself part of the law enforcement system and can disseminate all financial information received pursuant to the law. This information can be shared with other domestic competent authorities without much difficulty. However, the FIU, as part of the Egmont Group, must respect the *Principles for Information Exchange* (June 2001) and the *Best Practices for the Exchange of Information* adopted by the Egmont Group. Specifically, the principles indicate that, "… information exchanged between FIUs may be used only for the specific purpose for which the information was sought or provided. The requesting FIU may not transfer information shared by a disclosing FIU to a third party, nor make use of the information in an administrative, investigative, prosecutorial, or judicial purpose without the prior consent of the FIU that disclosed the information."

169. The FIU stated that they have analysed a significant number of STRs and disseminated them to various police agencies throughout Iceland for further investigation. The statistics from 2004 and 2005 revealed that, according to the reporting entities, many of these STRs involved suspected narcotics and fraud. (See the chart following paragraph 193.) The status of the STRs disseminated to other police agencies is not known because there are no available statistics or other information regarding the number of active investigations; arrests, seizures, confiscations, etc. Authorities indicated that many of the STRs disseminated to other police agencies were of investigative value, although there were no statistics available.

Independence and autonomy

170. The FIU is a part of the Icelandic law enforcement system; however, it faces some significant challenges that inhibit its ability to function as an effective FIU. The primary areas of concern are that the FIU does not have sufficient structure or an appropriate level of financial and human resources. At the present time the head of the Economic Crime Unit decides on the level of financial resources that the FIU will receive. The funding that the FIU does receive is balanced against other policing priorities and, as a result, the FIU does not get the resources it needs because of budget pressures elsewhere in the organisation. This affects the FIU's ability to plan for the long-term and address areas such as the hiring of additional personnel, the purchasing of equipment, as well as the provision of training for FIU personnel.

171. The FIU currently has one person who monitors the STRs that are submitted; he conducts database checks and analysis and then disseminates them as necessary. In the event that he requires additional analytical assistance, the FIU can call upon analytical resources from within the Economic Crime Unit on an ad hoc basis. The converse of this arrangement also holds true, i.e. the FIU resource may be called away for "other duties" outside the scope and mandate of his work in the FIU. Given this situation, it is the assessment team's view that the FIU does not have sufficient operational independence and autonomy to ensure that it is free from undue influence or interference regarding its ability to effectively carry out all FIU functions. This situation should be improved when the new regulation 626/2006 of 12 July 2006 is fully implemented (see paragraph 185).

172. There were no statistics available to determine the number of situations where FIU resources were drawn away to fulfil "other" operational policing duties. To mitigate this risk to the FIU, the head of the Economic Crime Unit is asking for three (3) additional staff to complement the existing resource that is currently there.

Storage and protection of information

173. The FIU is housed within the Headquarters of The National Commissioner of Icelandic Police in Reykjavik. The person working in the FIU and several others in the Economic Crime Unit have direct access to the information in the database. There are several pieces of legislation which ensure that the information is protected and handled properly.

174. Articles 4, 5, 6, 7 and 13 of the Regulation on Management of Personal Information by the Police, No. 322 dated; 9 April 2001 with amendment no. 926/2004 with articles dealing with security and internal control, the processing of personal information, the sharing of personal information, the use of shared personal information, and access to personal information and its deletion.

175. In this last regard article 13 indicates that "In the event recorded personal information is no longer necessary for police work due to its age or for other reasons, it shall be deleted." In discussions with the FIU at the time of the on-site visit there was no clear policy regarding the deletion of STRs or special criteria regarding when STRs are deleted. Normally STRs begin with an informal inquiry from the financial institution as to whether or not to file. The team was informed that, if there was any doubt about the transaction in question it would lead to a formal STR which would be filed and not deleted thereafter. When an informal enquiry is received regarding a possible suspicious transaction it is taken under consideration, and if the FIU concludes that there is no need to file an STR, all information regarding the enquiry would be deleted. The FIU estimated that less than 10% of the STRs are received in this way, not registered and the information deleted from the FIU database. However, there were no precise statistics available to verify if this had any impact on the FIU's effectiveness.

176. The rules on processing and deleting STR information have been further clarified in the new Regulation 626/2006 of 12 July 2006. (see paragraph 159). In addition, Article 14 indicates that if an investigation under Article 7 "eliminates all suspicion of a connection with illegal activities, then all information recorded in the database regarding the case shall be deleted." It further states that in all other ceases, the information shall be deleted no later than seven years after it was recorded in the database, except where new information has been recorded or a police investigation has been initiated against individuals or legal persons who are the subject of the notification. In the cases of blocking a transaction, Article 10 requires that the FIU investigate.

177. Provisions on protecting STR information are further detailed in Regulation 626/2006. It specifies that notifications of suspicious commercial transactions shall be recorded in a separate database. Only staff of the Economic Crime Unit who are engaged in the reception and investigation of notifications may have read and write access to the database. Access to the database shall be granted in writing by the head of the Economic Crime Department (Articles 5 and 6). Article 3 also specifies that "all police employees who are involved in investigations under these regulations shall be bound under the Police

Act and the Civil Servants' Rights and Obligations act not to disclose matters of which they become aware of as a result of notifications and their investigation."

178. Article 22 of the Police Act No.90/1996 also indicates that: "Policemen and other police workers shall be subject to a confidentiality obligation regarding matters of which they become aware in or through their work and which should remain secret in terms of lawful public or private interests… The confidentiality obligation shall remain in force even after the individual's employment ends."

179. Under article 18 of the Government Employees Act No. 70/1996, "Each employee is obliged to observe confidentiality in regard to matters of which he gains knowledge in his work and shall be regarded as confidential according to law, the instructions of superiors or by the nature of the matter. The obligation of confidentiality remains even if the employee concerned leaves his employ."

180. Finally, Article 136 of the General Penal Code has a term of imprisonment up to one year for any civil servant who reveals anything which is to be treated as a secret and of which he/she has learned in the course of his/her work or which pertains to his/her office or function. The same penalty applies to a person having left official service and who thereafter tells of or abuses knowledge he/she has obtained in his/her position and which is to be kept secret.

181. In terms of physical security of information, the evaluation team had several concerns. At the present time the database is backed-up; however, this is currently a manual process using a USB mass storage device (i.e., "memory stick"). Consideration should be given to having the system automatically back-up the information at regular intervals with the back-up information being stored off site. The FIU could use their membership in the Egmont Group and consult with the IT Working Group to enhance their IT system and examine new software applications which may facilitate their analytical capacity and effectiveness.

Reports

182. The FIU has not yet released any reports, statistics, trends analysis and/or typologies concerning their activities. During the assessment team's discussions with the FIU and Economic Crime Unit staff, they acknowledged that they have not been able to do tasks such as reports or other proactive work on STRs due to the limited resources at its disposal, i.e. one person working full time on FIU functions.

183. However, the FIU will have obligations in this area in the future pursuant to new requirements in Regulation 626/2006 of 12 July 2006. Article 13 requires the "Money Laundering Office" to keep and publish each year, information on the number of notifications of suspicious commercial transactions it receives, how notifications are followed up, the number of cases investigations, the number of individuals prosecuted or sentenced for money laundering or the financing of terrorism, and the value of categories of assets embargoed or seized under the Code of Criminal Procedure or confiscated under the General Penal Code. The Money Laundering Office shall release to the reporting parties the latest information on methods used in money laundering and the financing of terrorist activities, and on how to identify transactions covered by the new AML/CFT Act.

FIU structure, resources, integrity standards and training.[17]

184. The FIU is a part of the Economic Crime Unit of the National Police. Beyond this, there is no formal structure defining or distinguishing the FIU roles and functions. There is generally one dedicated person conducting FIU tasks of receiving and processing STRs; however, this person could be drawn away for other policing tasks, and he can also be assisted by additional staff of the Economic Crime Unit when warranted. Icelandic authorities indicated that there are also a prosecutor, a lawyer and two (2) police officers who often work with the FIU. However, this assistance with its analytical and investigative functions is not provided to the FIU on a full time basis. Authorities were not able to

[17] As related to Recommendation 30; see Section 7.1 for the compliance rating for this Recommendation.

indicate precisely how much or how often this assistance has been provided, but it estimates that assistance was provided on approximately 20% of the STRs that had been received.

185. Some further legal structure is provided for in a new Regulation 626/2006 of 12 July 2006. It defines a specific "Money Laundering Office" as "the unit within the Economic Crime Unit within the National Commissioner of Police where notifications of suspicious practices are received and examined."

186. The number of dedicated staff is not sufficient: The FIU remains a "one person entity" which inhibits its ability to function in an effective manner. Whereas the number of staff dedicated to the Economic Crime Unit has increased by 10 since the Second FATF Mutual Evaluation of Iceland in February of 1999, there has been no increase in the level of resources dedicated to the FIU since that time. As a result, while STRs are processed without a backlog and investigated, other key "pro-active" FIU functions such as STR analysis, ML/FT typologies and publications, and issuing guidance and reporting forms are not carried out.

187. Furthermore, the FIU does not have a sufficient budget or budgetary control to effectively perform its functions. This restricts the unit's ability to make long-term strategic plans, to hire additional resources, to fund training and to buy analytical equipment and software. The FIU's ability to function effectively is directly tied the budgetary constraints / pressures that the National Commissioner of the Icelandic Police may experience.

188. The staffs of the FIU and of the Economic Crime Unit have been hired in accordance with the selection criteria and the professional standards outlined in Article 38 of the Police Act No. 90, 13th June, 1996. Articles 22 of the Police Act and Article 6 of the Police Code of Ethics outline the obligation of "confidentiality" and the maintenance of a high level of integrity that must be observed by all officers.

189. In the opinion of the assessment team, the skill level of FIU personnel regarding ML and FT issues should be addressed. This is based on the observation that AML/CFT training is inadequate, and there is no mechanism in place to ensure that the person(s) within the FIU remain current in their knowledge and experience.

190. It is the assessment team's view that the FIU has the requisite knowledge concerning the predicate offences and the obligations of financial institutions to report suspicious transactions related to these occurrences. However, there appears to be very little formal training provided to FIU personnel, both upon engagement as well as on an ongoing basis. This was confirmed by the FIU and officers from the Commissioner of Icelandic Police who stated that there are no specialized courses in Iceland which are specifically dedicated to AML and CFT related matters. The only AML training they receive is subsumed within an Economic Crime Course which is given at the Icelandic Police College. Furthermore, the last time anyone from the FIU and/or the Economic Crime Unit participated in AML/CFT training outside the country was in 1999.

191. To address this training gap, authorities indicated that the FIU officer is planning to take part in AML/CFT training seminars in the future. The Public Prosecutor for Serious Economic Crime mentioned that arrangements are made for in-house training in "fields of interest". The assessment team was unable to determine if any of the training that is provided is related to AML/CFT analytical or investigative techniques.

Recommendation 32[18] (Statistics)

192. The FIU provided a breakdown of STRs based on financial institution, DNFBPs, as well as other businesses. (See paragraphs 347 and 348 for complete statistics.) According to the information provided, all STRs which have been received have been analyzed and many have been disseminated to various law enforcement agencies for further investigative action. However, it appears that when an STR is disseminated, it is done so on an informal basis with no discernable framework or structure in place.

[18] See Section 7.1 for the compliance rating for this Recommendation.

193. The FIU provided statistics for 2004 and 2005 that demonstrate that the vast majority of STRs that they have received are related to suspected narcotics cases. This also corresponds to the sharp increase of drug related offences over that same timeframe. (See Section 1, paragraph 9 of this report for overall crime trends and statistics).

Suspected predicate offences on STRs	**2004**	**2005**
Suspected Narcotics Cases	260	245
Suspected Fraud Cases	7	4
Diverse	34	35
Total	301	284

194. Based on the statistics provided, the following trends can be observed:

- During the period 1999-2005 there has been over a 500% increase in the number of STRs;
- There has been a 1203% increase in the dollar value of the STRs reported to the FIU;
- During the period 2000-2004 there has been a 214% increase in the number of narcotics offences which have been reported;
- This increase in STRs has also coincided with a large growth in the financial services sector.

3.2.3 Recommendations and Comments

195. Overall, the FIU does not have sufficient structural or operational independence, and the lack of a sufficient financial and human resources has inhibited its ability to effectively perform many FIU tasks. The new regulation 626/2006, issued in July 2006, should be fully implemented in this regard. While authorities reported that the staffing numbers of the Economic Crime Investigation Unit have increased by 10 people since the FATF's 2nd Mutual Evaluation of Iceland in February 1999, there has not been any increase in the level of resources dedicated to the FIU. As a result, this FIU has not kept pace with the increase in the number of STRs and/or the number of reported drug related offences.

196. Over the course of the last few years, there has been a significant increase in the size of the Icelandic financial sector. There has also been an increase in the level of drug trafficking activity, as well as a correspondent rise in the number and overall value of the STRs. However, these increases have not translated into, nor are they reflected in the number of money laundering cases being investigated, analytical studies or other AML/CFT work being done by the FIU. In fact, the number of money laundering prosecutions has significantly decreased since 2000/2001. These facts indicate that the FIU is limited in its ability and effectiveness vis-à-vis AML/CFT matters.

197. The assessment team recommends that the Icelandic FIU take a series of immediate steps to enable the FIU to more effectively fulfil its responsibilities, namely:

- improve the structural and operational independence of the FIU by fully implementing the new Regulation 626/2006;
- secure an increased level financial and human resources to enhance its ability to effectively perform the functions of an FIU;
- develop written guidance and direction to reporting entities concerning the manner of reporting STRs;
- develop a standardised STR reporting format for all reporting entities;
- initiate proactive analysis of STRs and police data to enhance the effectiveness of targeting entities involved in suspected ML and FT;
- increase international cooperation between the FIU and other international partners through more active participation in the Egmont Group;
- produce annual reports on trends and typologies (as required in the new regulation 626/2006);
- develop educational programs for the public on AML/CFT issues;

- pursue training and educational opportunities for FIU personnel, the financial sector and other police agencies. (The training issues could be pursued through the Training Working Group of the Egmont Group.);
- The FIU should consider taking measures regarding the "disaster recovery" of their database. At the present time the database is backed-up; however, this is currently a manual process. Consideration should be given to having the system automatically back-up the information at regular intervals with the back-up information being stored off site. To assist in this process, the FIU could its their membership in the Egmont Group and consult with the IT Working Group to enhance their IT system and examine new software applications which may facilitate their analytical capacity and effectiveness.

2.5.3 Compliance with Recommendation 26

	Rating	Summary of factors relevant to s.2.5 underlying overall rating
R.26	**PC**	• Overall, the FIU does not appear to be effectively addressing AML/CFT issues. • At the time of the on-site visit, the FIU did not have sufficient structural or operational independence. • Insufficient human and financial resources to effectively perform FIU functions. • The FIU staffing, activities, and results have not increased despite a large increase in the financial sector, drug trafficking crimes, and STRs. • Limited AML/CFT training provided to FIU personnel. • There has been no written guidance or forms to reporting entities. • No annual public reports concerning FIU activities, typologies or AML/CFT trends analysis have yet been issued. • There is no standardised or uniform process for reporting STRs.

2.6 Law enforcement, prosecution and other competent authorities – the framework for the investigation and prosecution of offences, and for confiscation and freezing (R.27, 28, 30 & 32)

2.6.1 Description and Analysis

Recommendation 27

198. According to 2005 statistics, there are 671 police officers and 80 reservists in Iceland. The majority of the money laundering matters is investigated by the Economic Crime Unit within the National Commissioner of Icelandic Police. However, STRs are sometimes referred to the police districts by the FIU for further investigation. The majority of the referred cases are related to narcotics trafficking which fall under the investigative mandate of any of the police agencies within the country which receive these STRs. An issue which is complicating the investigative process is that there is no specific ML/FT training provided to the Reykjavik Police or to Customs officers to deal with these types of matters. If specific ML and/or FT knowledge is required for investigative and prosecutorial purposes, these agencies seek out the assistance of the Economic and Crime Unit. This is also the trend with other police districts in Iceland.

199. Icelandic authorities also indicated that all terrorist financing matters would also be investigated by the Economic Crime Unit. However, to date there have been no such investigations.

200. Icelandic law enforcement authorities have the investigative leeway and discretion to postpone the arrest(s) of a person(s) in a money laundering case if it is deemed to be appropriate for the gathering of additional evidence and that it will be of an overall benefit to the investigation as a whole. There were no statistics available to illustrate the number of investigations where this had occurred, nor is there any information to demonstrate recent investigations and/or prosecutions.

Additional elements

201. The Icelandic Law Enforcement and Prosecutorial authorities do have rules and instructions which allow them to use various investigative techniques. In particular they include;

- the use of Informants;
- the use of Decoys;
- the use of Controlled Deliveries and;
- the use of Tracking Equipment.

202. Icelandic Law Enforcement and Prosecution officials also acknowledged that telephone wiretaps are widely used as an investigative technique. This is done pursuant Section 86 of the Code of Criminal Procedure.

203. Prosecution authorities stated that in 2005 the Icelandic Police used the wiretap provisions of the Code of Criminal Procedure approximately two hundred and fifty (250) times. These cases were primarily related to narcotics trafficking. The other techniques are also used, with the exception of Decoys. It was explained that given the size and population of Iceland it is extremely difficult to use "Decoys", i.e. undercover police officers, in investigations. There were no statistics illustrating the number of times that these latter techniques had been used.

204. The Economic Crime Unit has the primary investigative responsibility for complex economic and proceeds of crime cases. Other police forces within Iceland, such as the Reykjavik Police do conduct investigations where the proceeds of crime are seized and confiscated. However, if they require a more in-depth investigative knowledge regarding proceeds of crime, they will contact the Economic Crime Unit for assistance.

205. Law enforcement authorities in Iceland work closely with their Scandinavian partners as part of the Schengen Convention. The rules and regulations regarding the various investigative techniques are clearly outlined by the Prosecutor General. However, there are no statistics which demonstrate the number of times the various investigative techniques have been used in a collaborative manner with other competent foreign authorities.

206. The Director of Public Prosecutions (DPP) has issued guidelines on the use of special investigative techniques which may be used in ML and FT cases. There is no indication that the various ML and TF methods, techniques and trends are reviewed and discussed amongst the various Icelandic law enforcement authorities, the FIU and/or other competent authorities.

Recommendation 28

207. Icelandic law permits law enforcement authorities to compel the production of documents, records and other relevant information in furtherance of ML, TF and predicate offence investigations. The primary provisions to search and seize evidence of any kind are found in the Code of Criminal Procedure, No 19/1991. Articles 78 indicates "Items shall be seized if they are reasonably believed to be of evidential value in a criminal case, if they have been obtained by criminal means, or if it is reasonably believed that they may become subject to confiscation." Article 85 authorises a person in charge of an investigation, or the DPP, to obtain security for a fine, compensation, legal costs, or confiscation, request an order barring a suspect from disposing of his property if it is deemed to be in danger of being secreted, (covering seizure). Article 89 authorises a broad range of search powers. Article 90 indicates that search authorisations shall be provided for in the decision of a judge, unless the person in question consents to the search. However, an investigator may also conduct a search without a judicial warrant if there is an imminent danger of evidence being prejudiced by awaiting a judge's decision. The search of a person to be arrested may also take place without a judicial warrant if while awaiting a judge's decision a risk exists that the arrested individual will abscond.

208. When seeking information from a financial institution for court purposes, such as; account activity and transactions, various documents and records, etc., law enforcement will obtain a production order pursuant to Article 90. The compliance officers at these institutions will work with law enforcement officials and provide the information being sought. To date, the financial institutions have not encountered any problems with the production orders that they have received. In the event that a police investigation has been initiated as a result of an STR received from a financial institution, the police may acquire additional information from the institution by drafting a letter confirming that an investigation has been undertaken. In this case, judicial authorization is not required.

209. In the opinion of the assessment team, all information can be obtained, but in many cases a production order would be necessary. This information can then be used as evidence.

210. The police may take witnesses´ statements pursuant to Article 69 of the Code of Criminal Procedure, item 1 which states "Subject to Article 74a, the investigator shall collect reports from the accused person and any witnesses". However, there is no duty for the witness to answer any questions at the time. However, if witnesses refuse to do so they may be called into court for questioning by a prosecutor, in which case they have to answer the questions of the court unless they are covered by a special exemption.

Structure, resources, integrity standards and training[19]

Director of Public Prosecutions (DPP)

211. The DPP is the highest holder of prosecution authority. His role is to ensure that legally prescribed sanctions are applied against persons who have committed criminal violations, the DPP

[19] As related to Recommendation 30; see Section 7.1 for the compliance rating for this Recommendation.

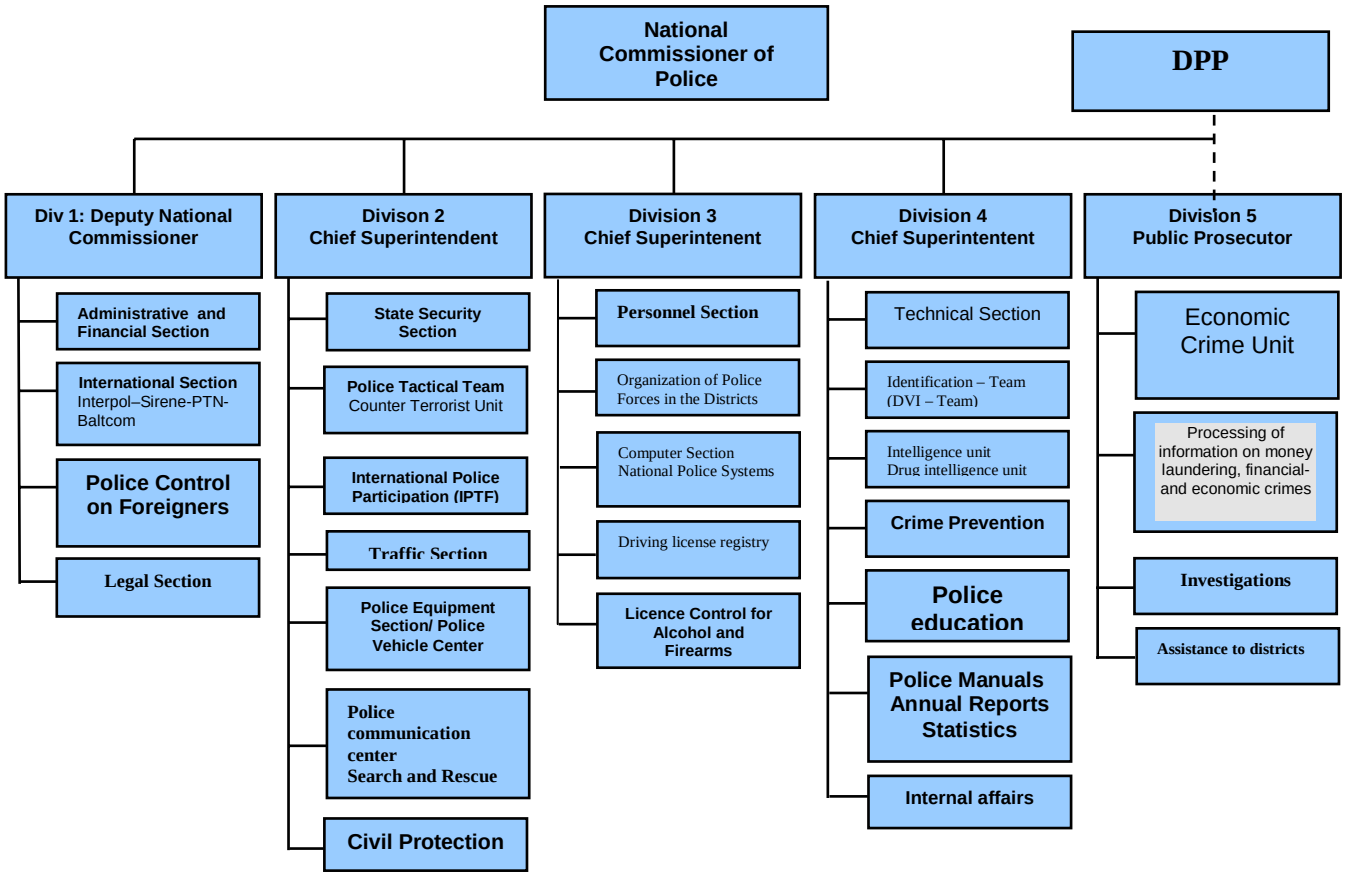
provides general instructions on the commission of prosecution authority and supervises the exercise of prosecution authority by the Commissioners of Police, including district chiefs and the National Commissioner of Police. The DPP may give instructions concerning specific cases and he may decide to commence investigation, give orders as to its commission and supervise it. Commissioners of Police are in charge of criminal investigation and public prosecution within the area of their office. The Commissioners of Police have the authority to prosecute before the District Courts offences other than those handled by the office the Director of Public Prosecutions.

212. The DPP conducts all criminal cases of appeal before the Supreme Court and prosecutes before the District Courts the more serious offences against the General Penal Code. Although the DPP formally reports to the Minister of Justice, the office has by law a special independent status intended to secure its independence similar to the status of judges.

213. The budget for the police and the prosecutors is approved by the Parliament, and the budget in this field has been increased when needed. The DPP's Office consists of seventeen personnel. The budget for DPP's office for 2006 is 99.6 million ISK.

National Commissioner of Police

214. The National Commissioner of Police falls under the Minister of Justice and is in charge of police in Iceland. The role of the Commissioner is to perform various supervisory and administrative functions in fields related to country-wide law enforcement and international co-operation through Interpol and Europol. The Commissioner is also in charge of national security and civil protection matters, which shortens the lines of communication in CFT cases. Prosecution of economic crimes rests with the National Commissioner of Police. District police chiefs (sheriffs) investigate and prosecute the less serious crimes and misdemeanours (the vast majority of offences). There are five specific divisions under the Commissioner.



Economic Crime Unit

215. There are five specific divisions under the Commissioner, one of which is the Economic Crime Unit, which investigates and prosecutes these crimes. This division, is headed by a public prosecutor is comprised of 14 police officers, one prosecutor and 3 police attorneys, which is an increase by 10 since 1998. This unit incorporates the duties of Financial Intelligence Unit and has divided its work and staff accordingly on an ad hoc basis. A few large economic fraud cases have recently absorbed greatly the resources of the division, but a reorganisation is now underway making it possible to allocate more resources to AML/CFT problems and more proactive work in the field. The current budget for the unit amounts to ISK 135 million/year.

216. Law enforcement officers within the country of Iceland are hired in accordance with the selection criteria and the professional standards outlined in Article 38 of the Police Act No. 90, 13th June, 1996. Articles 22 of the Police Act and Article 6 of the Police Code of Ethics outline the obligation of "confidentiality" and the maintenance of a high level of integrity that must be observed by all officers.

217. Law enforcement personnel do have the requisite knowledge concerning the predicate offences. However, the skill level of law enforcement personnel regarding ML and FT issues needs to be enhanced. This is based on the observation that AML/CFT training is inadequate and there is no mechanism in place to ensure that those who investigate/prosecute ML or assist the work of the FIU remain current in their knowledge and experience. There appears to be very little formal training provided to law enforcement personnel, both upon engagement as well as on an ongoing basis regarding AML and CFT investigations. This Commissioner of Icelandic Police confirmed that at the present time there are no specialized courses in Iceland which specifically teach AML and CFT investigative skills. The only AML training they receive is subsumed within an Economic Crime Course which is given at the Icelandic Police College. Icelandic police authorities have received training from foreign counterparts in the past; however, the last time the Economic Crime Unit participated in this type of training outside the country was in 1999.

218. There are no current (2004-2006) statistics available concerning the number of ongoing ML investigations. Icelandic law enforcement and prosecution authorities did state that they have not yet experienced any investigations related to FT. Authorities did provide statistics on the number of money laundering prosecutions and convictions (See paragraph 88); however, there is not a systematic manner of recording this information and making it available. Authorities did indicate that several STRs either led to money laundering prosecutions or assisted the money laundering cases described. However, clear statistics could not be provided. Overall, it did not appear that investigation and prosecution authorities adequately pursued money laundering cases, despite the increase in drug crimes and continued prevalence of profit generating crimes, the vast increase in the financial sector, and the large increase in the number of STRs reported.

2.6.2 Recommendations and Comments

219. Icelandic authorities should take a more proactive approach to investigating and prosecuting money laundering. The Icelandic law enforcement authorities have limited experience and training regarding AML and CFT investigative techniques. Therefore, more frequent and in-depth training should also be provided to law enforcement and prosecution personnel.

2.6.3 Compliance with Recommendations 27 & 28

	Rating	Summary of factors relevant to s.2.6 underlying overall rating
R.27	**LC**	• Overall it did not appear that investigation and prosecution authorities adequately pursued money laundering cases. • AML/CFT training is inadequate, and there is no mechanism in place to ensure that those who investigate/prosecute ML remain current in their knowledge and experience.

R.28	**C**	

2.7 Cross Border Declaration or Disclosure (SR.IX)

2.7.1 Description and Analysis

Special Recommendation IX

220. According to the new Article 27 of the Customs Act 88/2005, which came into force on 1 January 2006 entitled : "Declarations by travellers and crew members", travellers and crew members arriving in or departing Iceland "shall voluntarily declare amounts of cash which they have in their possession exceeding an amount equal to EUR 15,000." Although the term "cash" is used; the preparatory works also indicated that "'cash' covers currency and bearer instruments, including traveller's cheques." While this may create a legally enforceable obligation vis-à-vis bearer instruments, the evaluation team had concerns about the practical applications of this. For example, as indicated below, the English pamphlets and forms provided (where they are provided) use the word "cash," and it would therefore be difficult for arriving passengers to be fully aware of their obligations.

221. Article 27 does not apply to shipments of currency through containerised cargo or the mailing of currency or bearer negotiable instruments by a natural or legal person. However, Articles 22 and 28 of the Customs Act require customs declarations to be submitted concerning all imported "goods," which would include containerised cargo or the mail. "Goods" includes cash and any other bearer negotiable instrument. In addition, Art. 144 of the Customs Act indicates that all provisions of the Act regarding importation also apply to exportation and transit. Therefore, it appears that the requirements of Articles 22 and 28 also apply to *exporting* of currency/bearer negotiable instruments in containerised cargo or the mail.

222. Crew members are required to submit a written declaration. Icelandic authorities have not implemented a written form for passengers. Instead, Article 27 indicates: "In facilities where the customs clearance of travellers takes place, the director of customs is authorised to have separate customs clearance channels on the one hand for those bringing with them dutiable goods or goods subject to special import restrictions or prohibited from importation into the country, and on the other hand for those having no such goods in their possession. Travellers must themselves choose a customs clearance channel, and by their selection they are deemed to have indicated whether they have in their possession goods which they should declare to the customs." Any person who intentionally provides incorrect or misleading information or neglects to submit any required written documentation may be subject to fines, or for repeated violations, imprisonment according to Article 172 of the Customs Act.

223. The evaluation team had several concerns about the implementation of this system. Firstly, while the law creates a general obligation for the passenger to "declare", the mechanism for declaring would only apply where there is customs clearance of passengers. Since no form is provided to arriving passengers it is not clear that they would be aware of their obligations to declare. At the time of the on-site visit, a pamphlet was being prepared in order to inform ferry passengers of their obligations but it was not clear how or when this would be distributed. The English language version of the pamphlet refers to the obligation to declare "cash" (but not bearer negotiable instruments.") A pamphlet for arriving air passengers was not yet envisioned. Secondly, the system authorises, but does not require, the customs to create separate customs clearance channels, and therefore the "declaration" system does not apply everywhere. Finally, using the incoming customs clearance channels to implement the declaration system means that, while the legal obligations still apply to outgoing currency, there is no practical mechanism in place for "declaring" outgoing currency movements.

224. Upon discovery of a false declaration of currency, authorities have the authority to request and obtain further information from the carrier with regard to the origin of the currency or bearer negotiable instruments and their intended use. The customs authorities may require necessary information from the

parties involved in any form, as stipulated in Paragraph 3 of Article 30 of the Customs Act. What constitutes necessary information as regards imports or exports is left to the discretion of the customs authorities, e.g. the origin of a shipment or the purpose of the import or export.

225. Customs authorities are able to stop or restrain currency for a reasonable time in order to ascertain whether evidence of money laundering or terrorist financing may be found where there is a suspicion of any Penal Code violation, which includes money laundering or terrorist financing. In addition, Art. of 146 in Penal Code indicates that providing any incorrect details regarding matters where he or she is required to grant information to authorities is punishable by four months in prison. Therefore, Iceland officials also have the authority to stop or restrain currency upon discovery of a false declaration.

226. There are no specific requirements that at a minimum, information on the amount of currency declared or otherwise detected, and the identification data of the bearer(s) shall be retained for use by the appropriate authorities in instances when: (a) a declaration which exceeds the prescribed threshold is made; (b) Where there is a false declaration/disclosure; or (c) where there is a suspicion of money laundering or terrorist financing. In the cases where there is a declaration which exceeds the prescribed threshold or is made or where there is a suspicion of money laundering or terrorist financing, customs officials would have the authority to retain this information. More generally, Iceland authorities indicate that in the case of all criminal investigations, information concerning such cases is preserved and disclosed to other authorities as provided by law. Customs authorities are also required to deliver information concerning money laundering to the police authorities according to Article 26 of Act No. 64/2006 on measures against money laundering and terrorist financing. Nevertheless, the evaluation team could not conclude that all the required information would necessarily be kept. No declaration above the threshold had yet been made.

227. Information obtained through the processes declaration system would probably be available to the financial intelligence unit (FIU). Article 162 of the Customs Act states, "the director of Customs shall notify the relevant chief of police of a seizure" of currency suspected of being linked to money laundering or terrorist financing. In the Icelandic context, the FIU is housed within the National Commissioner of Icelandic Police and it is therefore notified. While this article applies to the seizure of cash and not directly to the declaration per se, customs officials indicated that it would alert the FIU if a declaration above the threshold were made, in a similar manner to other cases where it has reported to the FIU. In addition, all government (e.g. Customs) and professional authorities are required to deliver any information suspected of being linked with money laundering or terrorist financing according to Article 26 of Act No. 64/2006 (the AML/CFT Act of 22 June 2006.) While no definitive statistics were available to illustrate this, the Keflavik Airport Police and Customs officials have stated that there have been six or seven cross border cash interventions over the last ten (10) years which were reported to the FIU.

228. At the domestic level, it appears that there is adequate co-ordination among customs, immigration, police, FIU and other related authorities on issues related to the implementation of Special Recommendation IX. A separate agreement is in effect between the customs authorities and police authorities concerning co-operation on customs and police affairs

229. The Icelandic system allows for international co-operation and assistance amongst competent authorities, consistent with the obligations under Recommendations 35 to 40 and Special Recommendation V. Iceland is a member of the World Customs Organization (WCO) and has therefore committed to work in concert with their colleagues around the world. Part of this international commitment is the sharing of information via-à-vis the cross border movement of goods and commodities. There are not written customs agreements in place with other countries; however, customs officials described several cases where informal arrangements with foreign authorities were successful in seizing incoming and outgoing suspects and drugs. In addition to its membership of WCO, Iceland is a party to several international agreements on mutual assistance in customs matters. Examples include an agreement between the Nordic States and with Germany and Poland, in addition to the provisions of the EFTA and EEA agreements.

230. There are criminal sanctions available for persons who make a false declaration. According to Article 172 of the Customs Act person who intentionally or by gross recklessness provides incorrect or misleading information or neglects to submit documentation as required by the Customs Act may be liable to fines, and in the cases of repeated offences, up to six years imprisonment. As indicated above, providing incorrect information to authorities is also punishable by up to four months imprisonment according to Art. 146 of the Penal Code. There are no specific criminal sanctions for persons who carry out a physical cross-border transportation of currency or bearer negotiable instruments that are related to terrorist financing or money laundering contrary to the obligations under SR IX. However, this money may be seized pursuant to Article 162 of the Customs Act.

231. Iceland can apply freezing measures and seizing measures to persons who are carrying out a physical cross-border transportation of currency that are related to terrorist financing or money laundering. According to Article 162 of the Customs Act "the executive officers of customs enforcement authority are authorized to seize these valuables when there is a suspicion that they will be used for violations of provisions punishable by the Penal Code. With regard to confiscation, the general rules on confiscation, as described in the discussion on Recommendation 3, would apply. In addition to the seizure provisions in Article 162 as regards travellers and crew, a general seizure authorisation is laid down in Article 161, which is invoked in other instances.

232. With regard to the application of freezing obligations pursuant to the requirements of SRIII, Icelandic authorities indicated that initially the seizing provisions will be used in all situations even if the situation is covered by freezing provisions.

233. The Icelandic Customs Service is a member of the WCO and therefore there is cooperation with other customs services which plays an essential and integral part of the process. Icelandic authorities therefore indicated that if they discovered an unusual cross-border movement of gold, precious metals or precious stones, it would consider notifying, as appropriate, the Customs Service or other competent authorities of the countries from which these items originated and/or to which they are destined, and could co-operate with a view toward establishing the source, destination, and purpose of the movement of such items and toward the taking of appropriate action.

234. The system for reporting cross border transactions appears to be generally subject to adequate safeguards to ensure proper use of the information or data that is reported or recorded. General data legislation is in effect in the form of the Personal Data Protection Act No. 77/2000. The provisions of this Act, together with the provisions of Article 188 of the Customs Act (which requires customs officials to maintain confidentiality concerning information gained during their work) and the provisions of agreements to which Iceland is a party concerning mutual assistance in customs matters, should ensure the secure processing of information.

Additional elements

235. Facial recognition technology has been implemented at the Keflavik Airport which may assist in detecting known criminals who travel into the country. Additional consideration should be given to using other effective methods outlined in the SR IX Best Practices Paper.

236. The customs service uses a computer system for clearing through customs. This system is operated centrally by the Directorate of Customs in Reykjavík for the entire country. Individual customs authorities do not have special databases within the computer systems for surveillance purposes. They do, however, have access to a special program and business objects, which may be used for surveillance, but its principal purpose is to gather and store data concerning clearance through customs. The Directorate of Customs in Reykjavík intends to increase emphasis on systematic risk analysis for customs surveillance throughout the country. Attention will especially be drawn to computerize data banks for the purpose of customs surveillance. According to the recently enacted Customs Act, the Director of Customs of Reykjavík is entrusted with the role of organizing customs risk assessment and preparing surveillance plans throughout the country, as provided in Sub-section (10) of Article 43 of the

Act. The Office of the Director of Customs has emphasized the importance of this work for customs surveillance.

237. Overall, the assessment team did not view that the current system for detecting and preventing cross border movements of currency or bearer negotiable instruments related to money laundering or terrorist financing is effective. No "declaration" above the threshold has yet been made, and no stops or seizures have been made under the new provisions. In addition to the issues indicated above, there are no statistics available which detail the number of STRs filed as a result of cross border currency interdictions. The only statistical information that was available was anecdotal in nature and indicted that in the last ten (10) years there have been six (6) or seven (7) incidents where police have seized currency.

2.7.2 Recommendations and Comments

238. Iceland should implement a system to comprehensively address the remaining requirements in SR IX. There should be a system that applies more explicitly to bearer negotiable instruments. Iceland authorities should provide additional guidance so as to better inform arriving and departing passengers about their obligations to make a declaration, and should also implement procedures for declaring or disclosing outgoing movements of currency or bearer negotiable instruments. Iceland should also adopt criminal sanctions for persons who transport currency that is related to money laundering or terrorist financing.

239. Authorities should ensure that, at a minimum, information on the amount of currency declared or otherwise detected, and the identification data of the bearer(s) is retained for use by the appropriate authorities in instances when: (a) a declaration which exceeds the prescribed threshold is made; (b) where there is a false declaration/disclosure; or (c) where there is a suspicion of money laundering or terrorist financing.

240. It is the assessment team's recommendation that Icelandic Customs authorities should consider the implementation of new investigative techniques and methods similar to those outlined in the Best Practices Paper for SR IX, e.g. canine units specifically trained to detect currency, as there is presently not adequate awareness of these techniques.

241. Customs officials should also consider working more closely with the Icelandic FIU and other law enforcement authorities to develop typologies, analyse trends and develop protocols for the sharing of information amongst themselves to more effectively combat cross border ML and FT issues.

2.7.3 Compliance with Special Recommendation IX

	Rating	Summary of factors relevant to s.2.7 underlying overall rating
SR.IX	**PC**	• The assessment team did not view that the current system for detecting and preventing cross border movements of currency or bearer negotiable instruments related to money laundering or terrorist financing is effective. No currency declaration had yet been made. • The requirement to declare bearer negotiable instruments does not appear adequately addressed in the law or in guidance to the public. • The system authorises, but does not require, the customs to create separate customs clearance channels, and therefore the mechanism to declare does not apply everywhere. • There is no practical mechanism in place for declaring outgoing currency movements. • There are no specific criminal sanctions available for persons who carry out a physical cross-border transportation of currency or bearer negotiable instruments that are related to terrorist financing or money laundering contrary to the obligations under SR IX.

		• There are no specific requirements that at a minimum, information on the amount of currency declared or otherwise detected, and the identification data of the bearer(s) shall be retained for use by the appropriate authorities in instances when: (a) a declaration which exceeds the prescribed threshold is made; (b) where there is a false declaration/disclosure; or (c) where there is a suspicion of money laundering or terrorist financing.

3. Preventive Measures – Financial Institutions

The scope of the Act on Measures to counteract Money Laundering, No. 80/1993 (as updated in 1999) (MLA)

242. The MLA applies to individuals and legal entities authorized to provide services to the public in Iceland or abroad and which are covered by one or more of the following:

1. Receiving funds for deposits and other repayable financial assets from the public
2. Credit activities (incl. consumer credit, mortgage, factoring and purchase of debt instruments and commercial credit).
3. Leasing of assets
4. Clearing of payments
5. Issuing and administering means of credit cards and other means of payment
6. Guarantees and commitments
7. Trading for own account or for account of customers in:
   a. Money market instruments
   b. Foreign exchange
   c. Financial futures and options
   d. Exchange and interest rate instruments
   e. Transferable securities
   f. Real estate
8. Participation in securities issues and the provision of services related to such issues.
9. Reception of financial assets in connection with the development of capital structure of undertakings, or in connection with the purchase, takeover or merger of undertakings.
10. Money handling (incl. bureaux de change)[20]
11. Safekeeping, custody and management of financial instruments (incl. electronic financial instruments)
12. Rental of safety deposits boxes
13. Securities transactions in accordance with the Act on Securities Transactions.
14. Life insurance services and the activities of pension funds
15. Real estate agency
16. Shipping brokerage
17. Trading of precious metals and gems when a particular trading activity exceeds the amount specified in Art. 3.2 or in cases where the amount is lower than that specified in Art. 3.2 and the trading is carried out in a number of inter-related trading activities.
18. Trading of works of art when a particular trading activity exceeds the amount specified in Art. 3.2 or in cases where the amount is lower than that specified in Art. 3.2 and the trading is carried out in a number of inter-related trading activities.

243. Icelandic authorities indicated that item 10 above included money transfer but not other "value" transfer. Both money and value transfer are specifically covered under the new AML/CFT Act 2006 (see below.)

244. In addition to the MLA, the Regulation on the role of financial institutions in measures against money laundering (No. 272/1994) (the Regulation) regulates more detailed requirements for the following financial institutions:

a. commercial banks, savings banks and their subsidiaries,
b. institutions governed by the Act on Credit Institutions other than commercial banks and savings banks,

[20] This has alternately been translated as "money handling" in a different translation of the law.

c. life insurance companies and individual retirement trusts,
d. securities companies and undertakings for collective investment in transferable securities (UCITS)
e. domestic branches of foreign financial institutions carrying out activities in accordance with subparagraphs 1-4.

245. It should be noted that while the MLA Act applied to insurance and securities intermediaries, this regulation did not apply to them and hence the more specific obligations in the Regulation did not apply to these entities.

The scope of the Act on Measures against Money Laundering and Terrorist Financing, No. 64/2006 (AML/CFT Act 2006)

246. New legislation updating the AML/CFT regime, Act. No. 64/2006 on Measures against Money Laundering and Terrorist Financing (hereafter "AML/CFT Act 2006") came into force on 22 June 2006. The new legislation generally covers the same scope but is more precise and instead of describing the activities that are covered, the professions are listed (Art. 2):

a. Financial undertakings pursuant to the definition in the Act on Financial Undertakings;
b. Life insurance companies and pension funds;
c. Insurance brokers and insurance intermediaries pursuant to the legislation on insurance brokerage when they broker life insurance or other savings-related insurance pursuant to Article 23 of the Insurance Act;
d. Branches of foreign undertakings established in Iceland and falling within the scope of Sub-sections (a) to (c);
e. Natural or legal persons professionally engaged in currency exchange or transferring money and other valuables.
f. Attorneys and other legal professionals in the following instances:
    i When they manage or represent their clients in any form of financial or real estate dealings;
    ii When they assist in the organisation or conduct of business for their clients with respect to the purchase and sale of real estate or enterprises, management of cash or securities or other assets of their clients, open or manage commercial bank accounts, savings bank accounts or securities accounts, arrangement of financing needed for the establishment, operation or management of enterprises or establishment, operation or management of custody accounts, enterprises and similar organisations;
g. Auditors;
h. Other natural or legal persons when, in the course of their work, they perform the same services as those listed in Sub-section (f), e.g. tax consultants or other external consultants;
i. Brokers of real estate, enterprises or vessels;
j. Natural or legal persons professionally engaged in trading in goods for payment in cash in the amount of EUR 15 000 or more, based on the officially posted exchange rate at any time, whether the transaction is executed in a single operation or in several operations which appear to be linked;
k. Service providers in the field of financial custody and corporate services, cf. the definition in Article 3 of the Act;
l. Legal or natural persons who have been granted an operating licence on the basis of the Act on conducting lotteries, and parties permitted under special legislation to conduct fund-raising activities or lotteries where prizes are paid out in cash;

247. Article 2 (a) of the AML/CFT Act 2006 refers to the Act on Financial Undertakings (No. 161/2002) (FUA) for the definition of financial undertakings. According to article 4 of the FUA financial undertakings are:

a. Commercial banks

b. Savings banks
c. Credit undertakings
d. Electronic money undertaking
e. Securities companies
f. Securities brokerage
g. Management companies of Undertakings for Collective Investment in Transferable Securities (UCITS)

Customer Due Diligence & Record Keeping

3.1 Risk of money laundering or terrorist financing

248. The MLA in force at the time of the on-site visit (24 April – 5 May 2006) was not based on risk assessments in the manner intended by the revised 40 Recommendations, as the legislation dates from 1993 and was revised in 1999. However, Iceland has extended the scope of this Act to DNFBP sectors not covered by the Recommendations, including shipping brokerage, trading in works of art above Euro 15.000 and lotteries and raffles. While drafting the new AML/CFT Act, the Icelandic government has not made an overall assessment of money laundering and terrorist financing risks regarding sectors to be covered. Overall it was found that the scope of the 3rd EU Money Laundering Directive was found to cover the financial sector and DNFBPs sufficiently. The MLA is based on the 1st and 2nd EU Anti Money Laundering Directives (91/308/EU and 2001/97/EU). The Regulation of 1994 is based on the MLA 1993 (but not updated when the law was amended in 1999).

249. The new AML/CFT Act, which entered into force on 22 June 2006, incorporates the issue of risk into preventative measures for financial institutions and DNFBPs. Article 2 indicates that the "Financial Supervisory Authority may decide that parties falling within the scope of…[the Act] and engaging in financial activities on an occasional or very limited basis, and where there is little risk of money laundering or terrorist financing, should be exempt from the provisions of the act." However, no parties or sectors have so far been exempted on this basis. Article 7 also allows covered persons to implement the CDD provisions on the act on a risk-sensitive basis, where the extent of information gathering and other measures pursuant to this Act in respect of each customer are based on an assessment of the risk of money laundering and terrorist financing. Persons must establish rules on the conduct of risk assessment, which must be approved by the FSA in the case of financial institutions, and by the police, for other persons covered by the Act.

3.2 Customer due diligence, including enhanced or reduced measures (R.5 to 8)

3.2.1 Description and Analysis

Recommendation 5

General description and context: MLA 1993/1999 and the AML/CFT Act 2006

250. The CDD requirements are implemented in chapter II of the MLA (from 1993 and amended in 1999) and in its Regulation. At the time of the on-site visit (24 April – 5 May), a draft MLA was proposed to the *Althingi* (the Parliament), aimed at implementing the 3rd EU Anti Money Laundering Directive. This draft was adopted by the *Althingi* on 2 June 2006 and came into force on 22 June 2006 (except for article 12, regarding PEPs, which enters into force on 1 January 2007). This new legislation contains CDD measures in chapter II. In this report, the MLA in force at the time of the on site visit will be addressed as "MLA 1999", while the new law entering into force on 22 June will be called the "AML/CFT Act 2006."

251. The scope of the MLA 1999 is limited to basic customer due diligence requirements and does not contain the broad range of CDD measures in conformity with the FATF Recommendations 2003. Customer identification requirements are to be applied by the financial institutions covered by the MLA and the Regulation 1999. While the MLA 1999 covers insurance and security intermediaries, these are not covered by the Regulation, which gives additional and more detailed requirements. The AML/CFT Act 2006 covers insurance and security intermediaries (and generally include the requirements that were previously only covered by the Regulation) and both money and value transfer services. However, while all money exchange services were covered in the old and new money laundering legislation, there are still no provisions on monitoring compliance with their AML/CFT obligations if their activities that take place outside of banks, and therefore they are still "blind spot" in the AML/CFT supervision.

252. While the legislation at the time of the on-site visit was limited to customer identification requirements, the private sector was farther in its approach to apply established CDD measures to know their customers. This stems from a prudential point of view in which banks need to know their customer to overcome prudential risks, more than from an AML/CFT point of view. In general, banks have taken the Basel CDD paper into consideration.

Anonymous accounts and accounts in fictitious names

253. The opening and operation of anonymous accounts and accounts in fictitious names is under Icelandic law not permitted. Financial institutions are required to identify every customer when a business relationship is established (including opening an account) and record the name, the domicile and national identification number. Furthermore, according to Article 113 of the Act on Financial Undertakings, all accounts must be registered in the name of the customer together with his/her address and national identification number. Therefore, it is not permitted to hold numbered accounts. All accounts must be assigned to a name and national identification number.

When CDD is required

254. In the MLA 1999, Iceland implemented some customer identification obligations, but it had not implemented full customer due diligence (CDD) measures. The identification of the customer and verification of the identity were required when establishing business relationships and when performing occasional transactions above the threshold of euro 15,000 (article 3) and in case of lotteries, raffles and fund raising where prizes are paid out, the amount is EUR 1,000. If the amount was not known at the time of the transaction, or if the transaction is carried out in one or more operations which appear to be connected, the proof of identity is required as soon as the sum becomes known and it becomes clear that it exceeds the above limit.

255. The term "business relationship" was defined in Article 2 of the Regulation 1994 to mean the drawing up of a contract between a financial institution and a customer on a business relationship which will foreseeable be continued, for example the opening of an account, the drawing up of a loan agreement, a custody agreement or the opening up of a safe deposit box.

256. The MLA 1999 did not provide identification requirements in the case of wire transfers in circumstances covered by the Interpretative Note to SR VII. As such, they were treated as occasional transactions for which identification is only required if EUR 15.000 or more. The MLA 1999 did not contain a requirement to undertake CDD measures when there were doubts about the veracity or adequacy of previously obtained customer identification data. Regarding the requirement to undertake such measures when there was a suspicion of money laundering or terrorist financing, Iceland implemented this requirement regarding suspicion of money laundering, (article 3(3) and 4 and articles 2(4) and 4 of Regulation 1994).

257. At the time of the on-site visit, Iceland had only indirectly addressed identification when there was a suspicion of terrorist financing. The Public Announcement No 867/2001 required all parties subject to the MLA 1999, to notify the National Commissioner of the Police if such suspicions rise, giving only a basic regulation of an identification obligation in the case of a suspicion of terrorist financing.

258. The AML/CFT Act 2006 (Art. 4) includes the requirements in the old legislation and also extends the requirements in three areas. It now requires CDD when carrying out foreign exchange transactions of at least EUR 1,000 or its equivalent (whether carried out together or in transactions that appear linked) and also extends the requirement to undertake CDD measures to the situation when there are doubts about the veracity or adequacy of previously obtained customer identification data (Article 4, e) and when there is a suspicion of terrorist financing (Article 4, d).

Required CDD measures: Identification of natural persons

259. Under the law, every Icelandic national must be registered at the National Registry. When registered, a person receives a national identification number (based on date of birth), which is necessary to get financial services. Foreigners arriving in Iceland for a longer stay (work, study, etc.) must be registered as well as when they want to use financial services. Financial institutions will ask for a national identification number in addition to an identification document (passport, driver's license or identity card). The National Registry's current registration system dates from 1986. Entries from before 1986 have been reviewed, as there were cases of double or incorrect registration and identity theft, but it is not clear if this review has been done to the widest extent.

260. The above mentioned article 3 of the MLA 1999 contained the general rule that upon commencing a business relationship, in particular upon opening an account or depositing assets for custody, financial institutions should require customers to prove their identity by presenting personal identification documents attesting to the name, legal domicile and national registry number in accordance with a certificate issued by the National Statistics Office or the Tax Directorate. The AML/CFT Act 2006 holds this same identification requirement in Article 5.

261. Personal identification documents presented have to be documents issued by public authorities, with photograph, name and identification number of the individual concerned, e.g. passport, driver's license or identity card.

262. The Iceland legislation does not have detailed rules on the types of documents which can be used for identification and verification purposes. This can for example create the risk that foreign documents might be used by a foreign national which cannot be assessed fully by the financial institution on validity and authenticity, or creates different difficulties for a financial institution when verifying the identity of the customer; it also became clear from meetings with the private sector that the authorities should issue clear guidance on basic CDD requirements, including the identification of clients.

263. With the introduction of the new AML/CFT Act in June 2006 that some guidance is given on types of identification documents. The explanatory notes concerning article 5 of the AML/CFT Act 2006 stipulate: "Natural persons should be required to present identification papers with a photograph and name and other information confirming the identity of the person in question. It varies depending on identification documents what information they contain, but only documents issued by government authorities should be accepted, e.g. passports, drivers' licenses or other comparable documents." Still, Iceland should provide additional regulation or guidance or to assist the private sector in knowing which identification documents to accept or not. It can also be mentioned that the FSA is currently working on guidelines which will include guidance regarding the types of identification documents.

Identification of legal persons

264. While article 3 of the MLA 1999 states the general identification rule, which is also applicable for identification of a legal person, the MLA 1999 and Regulation 1994 do not hold further provisions on the verification of the identity of a legal person itself.

265. In practice, financial institutions require a national identification number for legal persons as well, before financial services are rendered. When a legal person does not have such a number yet, to obtain a national registration number, legal persons provide the financial institution in general with the necessary

documentation with which the financial institution will apply for a national identification number at the National Registry. This means that the customer has to provide the financial institution with documents like memorandums of association, statutes and auditor report. In case of a foreign legal person, an original certificate of incorporation is required. The National Registry does not perform further due diligence as long as there is an auditor's report or a report from a lawyer confirming the legality of foundation.

266. According to article 5(2) of Regulation 1994, "the legal person's holder of power of procuration shall *provide his identity in the same manner* as in transactions involving individuals *and he shall also prove that he holds a power of procuration*," which satisfied the requirement that financial institutions shall verify that the person purporting to act on behalf of the customer which is a legal person or legal arrangement, is so authorised and that he be adequately identified. The mentioned article of Regulation 1994 also stipulates the requirement to verify the legal status of the legal person/arrangement, but does not require financial institutions to obtain information on the directors and provisions regulating the power to bind the legal person or arrangement.

267. Banks do, notwithstanding the lack of sufficient regulation, demand a certificate of incorporation and they check through using an online access to the database of the national registry besides information on the holders of a power of procuration and information on the board of directors and business objectives of the legal person.

268. In Article 5 of the AML/CFT Act 2006, a requirement is introduced stating that the identity of a legal person must be verified by the submission of a certificate from the Register of Enterprises or a comparable public agency, with the name, domicile and national identification number or comparable information. The article also requires the holders of powers of procuration to prove their identity as required for natural persons (see above).

269. The regulation 550/2006 of the AML/CFT Act 2006 came into force on 4 July 2006 and superseded the 1994 Regulation and its requirements described in paragraph 266 above). Under the new legislation, there is no longer a requirement that the holder of a power of procuration has to prove that fact, which requirement was previously held in the 1994 Regulation. The explanatory notes concerning Art. 5 stipulate that he should demonstrate that he is empowered to represent the legal person. However, in contrast to other explanatory notes for the AML/CFT Act 2006, where the notes provide additional detail to the main rule based in the law, in this case the notes appear to contain the basic obligation itself, while the rule should be based in the law, which currently states that he only needs to be identified. Therefore, it is not clear that there is a sufficient legal obligation to verify that the natural person purporting to act on behalf of a legal person or legal arrangement is so authorised.

270. There is not a direct requirement in the legislation to obtain information on the directors and provisions regulating the power to bind the legal person or arrangement. The explanatory notes concerning Article 5 of the MLA 2006 only stipulate that "the FATF Recommendations assume that in order to establish the legal existence and corporate form of a legal person, information must be provided concerning the name, legal form, domicile, *directors and rules on who is authorised to bind the legal person*". While the legal requirement itself, Article 5, does not hold the necessary information to be obtained, the explanatory notes only give a notice about how the FATF Recommendations should be read without explaining the implementation of this rule into the Icelandic system.

<u>Beneficial ownership</u>

271. In the MLA 1999, there was no explicit requirement for financial institutions to identify the beneficial owner and take reasonable steps to identify the beneficial owner such that the financial institutions is satisfied that it knows who the beneficial owner is. At the time of the on-site visit, Icelandic law only required financial institutions to identify the person on whose behalf the account is held or transaction conducted (Article 5 of the MLA 1999) in certain circumstances. Article 5 indicates that: "Should an individual or an employee of a legal entity referred to in Article 1(1) know or have reason to suspect that specific transactions are being conducted for the benefit of a third party, he/she

shall request that the customer disclose the identity of the third party in question." This article therefore covers beneficial ownership only to a limited extent. Internal procedures of banks address the identification of the beneficial owners to a larger extent. However, in practice most of the time, information is only demanded in some cases of foreign clients.

272. The AML/CFT Act 2006 changes the situation with regard to legal persons, as Article 5 (b) states that the financial institution shall require the provision of adequate information concerning any beneficial owner for customers that are legal persons, cf. Article 3. This Article holds the following definition of beneficial owner, generally in line with the definition from the 3rd EU Directive:

> "…the natural person or persons who ultimately own or control the natural person and/or legal person in whose name the transaction is effected or who effects the transaction. A beneficial owner may include:
>
> > a) the natural person or persons who ultimately own or control a legal person through direct or indirect ownership of more than a 25% share in the legal person or control more than 25% of the voting rights or are deemed to exercise control by other means of the legal person. However, the provision does not apply to legal persons listed on a regulated market pursuant to the definition in the Act on Stock Exchanges and Regulated OTC Markets.
> >
> > b) the natural person or persons who are the future owners of 25% or more of the assets of a trust or a similar legal arrangement or who control more than 25% of its assets. Where the individuals that benefit from such trust have yet to be determined, the beneficiary is the person or persons in whose interest the fund is set up or operates."

273. With this definition of beneficial ownership, Iceland has chosen a basic regulation of the issue, which holds, corresponding with the 3rd EU Directive, some examples of beneficial ownership which are not exhaustive. The explanatory notes concerning Articles 3 and 5 point out that the concept of beneficial owner should include in any way any party who, alone or with others, ultimately owns or controls a legal person through direct or indirect ownership of over 25% share in the legal person or control over 25% of the voting rights and furthermore, a party that directly controls or exercises control over the management of a legal person. Regarding the identification of the beneficial owner the explanatory notes state that "it is also provided that if it is not clear who the beneficial owner is, it should be mandatory to provide information concerning the beneficial owner's identity." This seems to be opening up the possibility not to gather the necessary identification information when a financial institution has the opinion for itself that it believes it knows who the beneficial owner is, without the safeguard of having gathered the proper information. Therefore, there is still the question of whether financial institutions have sufficient guidance for implementation of this requirement. The FSA states that further guidance regarding the identification of the beneficial owner will be issued in the near future.

274. As stated above, the new requirements for beneficial ownership do not apply to customers who are natural persons but only to customers that are legal persons (Article 5 (b)). Article 5 (3) of the MLA 2006 parallels Article 5 of the MLA 1999, i.e., it requires customers to produce information concerning the identity of a third party where the financial institution knows or has reason to suspect that the transaction is being conducted for the benefit of a third party. Therefore, regarding all customers, it is not required for financial institutions to determine actively if the customer is acting for someone else and take reasonable measures to obtain sufficient identification data to verify the identity of the third person.

275. With regard to customers that are legal persons, there is, with the introduction of the AML/CFT Act 2006, the requirement that financial institutions must provide "adequate information concerning any beneficial owner", which could have been more specific to clearly state a requirement to take reasonable measures to understand the ownership and control structure regarding legal persons, or to determine the natural persons who ultimately own or control the legal person. With such a general requirement it seems very useful to give appropriate direction to the financial institutions to make clear what will be expected from them regarding the information on the beneficial owner(s) to be obtained.

Purpose and intended nature of the relationship

276. There was no requirement in the MLA 1999 to obtain information on the purpose and intended nature of the business relationship. The AML/CFT Act 2006 contains a requirement in Article 5: "information shall be obtained concerning the purpose of the intended business with the proposed customer."

Ongoing due diligence

277. Icelandic legislation did not require financial institutions to conduct ongoing due diligence on the business relationship. The AML/CFT Act 2006 now requires financial institutions to conduct ongoing monitoring of the business relationship with their customers to ensure that their transactions are consistent with the available information on the customers, e.g. by scrutiny of the transactions undertaken throughout the course of the contractual relationship. Information has to be updated and further information obtained as needed (Article 6). This seems to be in line with Recommendation 5 (criterion 5.7), although a reference made to higher risk categories of customers or business relationships has not been implemented. It is arguable that the obligation is a general requirement which counts for all customers or business relationships, so it therefore includes the higher-risk categories.

Risk

278. A requirement to perform enhanced due diligence for higher risk categories of customer, business relationship or transaction could not be found in the MLA 1999, except for the example of 'distant selling', (which is described as non-face to face transactions) in which situation the financial institution is required to obtain some additional information regarding the customer (article 3(4) of the MLA 1999).

279. Article 3(4) of the MLA 1999 stated the following:

> "Upon commencing a business activity regarding distant selling, entering into agreements utilizing distant selling methods or similar methods, additional information on the customer shall be acquired, when needed, as well as the requirement that the first payment relating to the business activity should be rendered in the name of the customer debited to a bank account established in a licensed credit institution or financial institution."

280. The AML/CFT Act 2006 holds enhanced CDD requirements in Chapter III, concerning distance selling (Article 10), correspondent banking (Article 11), PEPs (Article 12), correspondent banking business with shell banks (Article 13) and products or transactions that might favour anonymity (Article 14). (In this report the requirements concerning correspondent banking, PEPs, shell banks and products or transactions that might favour anonymity are addressed under the relevant Recommendations.).

281. Article 10 of the AML/CFT Act 2006, regarding distant selling, indicates:

> " At the start of a distance selling transaction, the establishment of contracts through the use of telecommunications or comparable methods where the customer is not present to prove his/her identity, additional information should be obtained about customers if necessary, and it should be required that the first payment should be made in the name of the customer and through an account established by the customer in a financial undertaking."

282. Regarding distant selling, both the old and new legislation state that enhanced CDD measures need to be taken 'when needed' (MLA 1999) or 'if necessary' (AML/CFT Act 2006). The question rises if this gives financial institutions a broad possibility to decide not to perform enhanced CDD as it leaves considerable space to perform normal due diligence. From the meeting with the sector it is understood that banks do perform enhanced due diligence in these cases as a standard, notwithstanding this opening in the law. No guidance has been issued by the supervisor, the FSA, or other competent authorities. The

FSA has indicated that this issue will also be addressed in AML/CFT guidelines, planned for release in fall 2006.

283. Iceland exempts financial institutions from having to apply customer identification or any other CDD measure in the following circumstances:

- when a customer is a financial institution holding an operating license within the European Economic Area ('EEA') to provide [financial] services (article 4 of the MLA 1999 and article 4 of the Regulation 1994);
- in cases where it is established that payment for a transaction is to be debited from an account opened in the customer's name in a similar institution operating within the EEA, unless there is a suspicion that the transaction is connected with [money laundering] (article 4 of the MLA and article 4 of the Regulation);
- when drawing up a life assurance contract if the annual premium does not exceed ISK 80,000 [+/- euro 1,000] or in case of a single premium it does not exceed ISK 200,000 [+/- euro 2,500]. If the annual premium is raised beyond the amount of ISK 80,000 the presentation of personal identification documents is required (article 4 of the Regulation).

284. The possibilities created for financial institutions to apply simplified or reduced CDD measures in the legislation (both the 1999 and the 2006 versions) are overly broad. Rather than allowing simplified CDD measures, no CDD is required at all for a series of transactions and customers. The provision permitting financial institutions to refrain from identifying the customer when it is established that payment is to be debited from an account opened in the customer's name in a similar institution operating within the EEA, is too broad because of the lack of safeguards to establish in the situation in which the foreign account is opened and adequately monitored for AML/CFT issues.

285. In the above-mentioned cases, there is no requirement to limit the application of such measures to those countries that Icelandic authorities (or financial institutions) are satisfied that those countries (EEA) are in compliance with and have effectively implemented the FATF Recommendations. There are no mechanisms or checks in place for such an assessment nor is there any prove of a consideration made by the authorities based on which there is a satisfaction about compliance with the Recommendations by the mentioned countries. Regarding exemptions for life insurance contracts within the mentioned threshold, there is no limitation to the country where this exemption would apply, and there has been no consideration given to differentiate between countries where the customer can be from.

286. Under the AML/CFT Act 2006, simplified measures are allowed in the case when the customer is a financial undertaking or life insurance company or pension fund or corresponding legal persons possessing an operating licence in the EEA. Beside this group, Article 15 a) states that this also applies for regulated credit or financial institutions from countries outside the EEA which are subject to similar requirements as under the new AML/CFT Act.

287. Regarding the financial institutions from within the EEA, it has to be noted that here as well mechanisms or checks are not in place for an assessment or any consideration based on which there is a satisfaction about compliance with the Recommendations by these countries. Consideration regarding compliance is however part of the provision as far as it concerns financial institutions from outside the EEA.

288. The other two exemptions from Article 15 of the AML/CFT Act 2006, companies listed on a regulated stock exchange and Icelandic government authorities are in line with Recommendation 5 (criterion 5.9). The Regulation 2006 copies in Article 2 the exemptions regarding payment debited from account within EEA (Article 4 of the MLA 1993/1999 and Article 4 of Regulation 1994) and regarding a life assurance contract (Article 4 of Regulation 1994).

289. Overall the AML/CFT Act 2006 does create a obligation to perform basic identification on the customer, to be able to ascertain that the customer is a customer for which the exempting provisions do apply (Article 15(2)).

290. In addition, financial institutions are permitted to implement the requirements regarding CDD measures (Articles 5 and 6 of the AML/CFT Act 2006) on a risk-sensitive basis, where the extent of information gathering and other AML/CFT requirements for each customer are based on an assessment of the risk of money laundering and terrorist financing. Financial institutions wishing to use this approach must establish rules on the conduct of their risk assessment, which must be approved by the FSA (Article 7). Since the new Act just came into force, the FSA has not yet issued additional guidance regarding this risk assessment; however, FSA is currently working on the issue.

Timing of verification

291. According to paragraph 1 of Article 3 of the MLA 1999, undertakings were required to verify the identity of customers (but regarding the beneficial owner, only to a limited extent) before establishing a business relationship or conducting transactions. The FSA and the private sector interpret this requirement to mean that identification must take place as soon as possible and before any transaction could take place. It might be possible to give out an account number before the completion of the verification of the identity of the customer, but the use of the account (transactions from and to) may not take place until the identity has been verified. It was not seen as problematic in case of securities transactions to uphold the requirement to verify the customer's identity before conducting the transaction, as the customers are mostly known clients whose identity had been verified before. There seemed to be a misunderstanding about the interpretation of this requirement within the sector as it was not clear if this practice is carried broadly throughout the sector, and there was no clear understanding of possibilities under the MLA 1999 since there are no further regulations or guidelines on this issue.

292. In the case of occasional customers making a transaction involving a sum equivalent to or over EUR 15,000, the customer must be identified. If the amount involved was not known at the time of the transaction, or if the transaction was carried out in one or more operations which appear to be connected, identification was required as soon as the sum becomes known and it becomes clear that it exceeded the limit of EUR 15,000 (article 3(2) of the MLA 1999).

293. Article 8 of the AML/CFT Act 2006 introduces a possibility to postpone the identification and the verification of the identity of the customer when it is necessary not to interrupt the normal conduct of business and where little risk is perceived of money laundering or terrorist financing. The customer has to be identified as soon as practicable. Regarding the opening of a bank account, this provision states clearly that the account may be opened even if the mentioned conditions have not been met, provided that no transactions are carried out in respect of the customer until he/she has been identified. Furthermore it is permitted, in relation to life insurance, to allow the verification of the identity of the beneficiary under the policy to take place after the business relationship has been established, in which case the verification has to take place no later than at the time of payout or before the time the beneficiary intends to exercise rights vested under the policy. With these exemptions the new legislation seems in a sufficiently manner to contain risk-management measures concerning the conditions under which the business relationship may be utilised prior to verification.

Failure to satisfactorily complete CDD

294. The MLA 1999 required the financial institution to reject the business relationship or transaction if a customer failed to produce sufficient identification documents that applies prior to establishing the relationship or prior to performing the transaction. Article 6 of the Regulation 1994 indicated that a financial institution should not open an account and should reject the business relationship or transaction, if a customer failed to produce adequate personal identification documents pursuant or refuses to provide information. However, regarding the identification of the beneficial owner, there was only a limited requirement to stop the financial institution from opening an account, commence business relations or performing the transaction, when it was unable to identify the beneficial owner satisfactorily, as there were no full identification requirements in place. There was no direct requirement for financial institution to consider making a suspicious transaction report in the event that the financial institution was not able to complete CDD. In practice, Article 8 of the Regulation 1994 stated that a STR should be

made when a examination according to Article 7 *or other incidents* lead to a suspicion. In the view of the Icelandic authorities, this obliged a financial institution when it was not able to identify a customer to consider making a STR, although doubts arise if the institutions have interpreted this requirement in this respect.

295. The AML/CFT Act 2006 repairs the shortcoming regarding the identification of the beneficial owner and stopping the commencement of a relationship with the customer or performing the transaction, as an obligation to identify the beneficial owner of customers who are legal persons is implemented in this new act (Article 5 and Article 9). Article 9 also introduces a requirement holding that consideration must be given to notification of the FIU (the police) if it has not proven to be possible to comply with the identification and verification requirements.

296. Where the business relationship has already commenced, and the financial institution cannot complete CDD, there was no requirement in the MLA 1999 to terminate the business relationship or to consider making a STR. Similarly, the new AML/CFT Act 2006 fails to pick up this shortcoming and only looks at the situation prior to the commencement of the relationship or prior to performing the transaction.

Existing customers

297. According to the MLA 1999, there was no requirement to apply CDD to existing customers (customers before the MLA came into force in 1993) in any circumstance, nor was there any regulatory measure in place. The new MLA introduces an obligation to conduct ongoing monitoring of the business relationship with all their customers. This requirement holds the obligation to update information on customers as needed. The explanatory notes concerning the requirement to perform ongoing due diligence express that this article extends to both new customers and customers of longer standing. This provision does not adequately cover an obligation to apply broad CDD-measures (i.e., beyond on-going due diligence) to existing customers (customers before the MLA first came into force in 1993) on the basis of materiality and risk, nor does it explain that due diligence should be conducted on such relationships at appropriate times. FSA indicated that further guidance on this issue will be developed

298. The FSA and the private sector believe that most of the customers from before 1993 have been identified, based on requirements from the Act on Financial Undertakings or other legislation like tax laws, which requires the financial institution to open an account in the name of the customer (no anonymous accounts or under fictitious names). However, it is unclear if those clients' identities have been verified properly, and the authorities do not consider it a serious issue to be addressed. The banks seem to pick up the problem with incorporating measures to verify the customer's identity at 'trigger moments' like opening a new account and performing certain transactions for the customer.

Recommendation 6

299. Iceland has not yet implemented any provision regarding the establishment and maintenance of a customer relationship with politically exposed persons (PEPs). Article 12 of the AML/CFT Act 2006 will only enter into force on 1 January 2007. This provision requires financial institutions to:

- determine whether the customer is a PEP (including natural persons who are or have been entrusted with prominent public functions and immediate family members, or persons known to be close associates of such persons),
- obtain senior management approval before entering into business transactions with such customers,
- take appropriate measures to verify the source of funds that are involved in the business relationship or transaction, and
- conduct regular monitoring of the business relationship.

300. There is no explicit obligation to obtain senior management approval to continue the business relationship where a customer has been accepted and he/she is subsequently found to be or subsequently becomes a PEP.

Additional elements

301. Iceland has chose to limit this provision (Art. 12) to persons residing in another country, so persons holding prominent public functions domestically are not included, based on a risk assessment as the society is small and closely-knit and corruption is considered to be minimal (see GRECO).

302. Iceland has not signed the United Nations Convention against Corruption.

Recommendation 7

303. Recommendation 7 was not implemented in the MLA 1993/1999, but Article 11 of the AML/CFT Act 2006 indicates that, in cross-border correspondent banking business with counterparts from countries outside the European Economic Area, credit institutions which are subject to this Act shall comply with the following conditions:

a. Gather sufficient information about the respondent's business and determine from publicly available information the reputation of the institution and the quality of supervision;
b. Assess the respondent's anti-money laundering and anti-terrorist financing controls;
c. Obtain approval from senior management before establishing new correspondent banking relationships;
d. Document the respective responsibilities of each institution pursuant to this Act, and;
e. With respect to payable-through accounts, be satisfied that the respondent has knowledge of the identity of, and conducts ongoing due diligence on, the customers having direct access to accounts of credit institutions which are subject to this Act and that it is able to provide relevant information concerning the customer upon request.

304. While the requirements are generally broad and based on the requirements of Recommendation 7, there are some significant deficiencies. Iceland has chosen to limit the obligation to respondent institutions from countries outside the EEA. As mentioned above, there is no proof of an assessment or other kind of check on which the privileged treatment of respondent institutions from within the EAA can be based. In addition, there is not a requirement to ascertain that the respondent institution's AML/CFT controls are adequate and effective. The explanatory notes for this article indicate that "The provision stipulates certain conditions to be met by a financial undertaking in correspondent banking with parties from countries outside the European Economic Area. Sub-sections (a) and (b) require assessment of the parties in question. The conduct of the assessment pursuant to Sub-section (a) shall be based on public information and among the relevant factors is whether the home state of the party in question complies with international standards relating to measures against money laundering and terrorist financing." However, while this applies to the overall AML/CFT regime of the country, and while the law requires an assessment of the foreign institution, it does not require that it ascertain that the institution's AML/CFT controls are adequate and effective. Regarding payable through accounts, it is not clearly required to be satisfied that the respondent has performed all normal CDD obligations; this is limited to the obligation to identify the customer and to perform ongoing due diligence. While Icelandic authorities indicate that the provision means 'knowing the identity of the customer,' this still would not adequately cover *other* required CDD measures such as beneficial ownership, and ascertaining the purpose and nature of the business relationship.

Recommendation 8

305. There is no general requirement for financial institutions to have policies in place or take such measures as may be needed to prevent the misuse of technological developments in ML or TF schemes. However, this is partly addressed by Article 14 of the AML/CFT Act 2006, which requires parties under the obligation to report "to show special caution in the case of products or transactions that might favor anonymity, and shall take measures, if needed, to prevent the use of such businesses for money laundering or terrorist financing purposes."

306. Financial institutions are required to have measures in place to deal with non-face to face relationships or transactions, including specific measures for managing the risks of non-face to face customers. Article 3 (4) of the MLA 1999 stated that: "Upon commencing a business activity regarding distant selling (or a "remote distance relationship"), entering into agreements utilizing distant selling methods or similar methods, additional information on the customer shall be acquired, when needed, as well as the requirement that the first payment relating to the business activity should be rendered in the name of the customer debited to a bank account established in a licensed credit institution or financial institution."

307. This same language regarding non face-to-face customers has been incorporated into Art. 10 of the AML/CFT Act 2006. This provision contains an additional requirement for more detailed rules in this area to be incorporated into the overall internal controls of the institutions to implement the Act. Icelandic officials indicate that this category would be included in the AML/CFT rules, which must also include rules on on-going due diligence and the requirement to update customer identification information as needed (Art. 6) see also the description of ongoing due diligence, par. 277).

308. The requirement to acquire additional information on the customer "when needed" is an open provision which needs further regulation or guidelines to make it effective. Recommendation 8 looks at the establishment of policies and procedures to address any specific risks associated with non-face to face business relationships or transactions. The provisions of both the MLA 1993/1999 and the AML/CFT Act 2006 do not hold such a requirement adequately, as they leave open the question as to when additional information is needed, or that financial institutions should address the risk through appropriate measures to be taken. The need for internal policies within financial institutions to prevent them from being misused for money laundering or the financing of terrorism purposes, seems not to be implemented sufficiently in that respect.

3.2.2 Recommendations and Comments

309. Iceland should implement the following elements from Recommendation 5 which have not been fully addressed:

a. Money exchange and money or value transfer should be fully and effectively brought under AML/CFT regulation and especially under customer due diligence requirements.
b. Financial institutions should be required to undertake CDD measures when carrying out occasional transactions that are wire transfer in circumstances covered by the Interpretative Note to SR VII.
c. The provisions regarding obtaining information concerning the legal person or arrangement should be extended to information concerning the directors and provisions regulating the power to bind the legal person or arrangement.
d. There should be a more general requirement to identify beneficial owners for all customers. The financial institution should be required to actively determine if the customer is acting for someone else and it should take reasonable steps to obtain sufficient identification data to verify the identity of the third person. Furthermore, reasonable measures should be taken to understand the ownership and control structure of the legal person. It should be made clear what is expected from the sector.
e. There should be some consideration/assessment made based on which there is a satisfaction about compliance with the Recommendations by countries which are currently seen as compliant without any doubt.
f. Rules regulating the CDD treatment of existing customers should be introduced.

310. Several new requirements just introduced with the new AML/CFT Act on 22 June 2006 should be now be effectively put into practice:

g. The requirement to undertake CDD measures in cases where there is a suspicion of terrorist financing and in cases where there are doubts about the veracity or adequacy of previously obtained customer identification data;
h. Rules on the verification of the identity of legal persons;
i. The requirements regarding identification and verification of the beneficial owner for legal persons, including the obligation to determine the natural persons who ultimately own or control the legal person.
j. The obligation to obtain information on the purpose and intended nature of the business relationship.
k. Performing enhanced due diligence on higher risk categories of customers, business relationships or transactions.
l. In case of applying simplified or reduced due diligence there has been introduced a basic identification regime instead of no customer identification regime at all, but practice has to pick it up in an effective manner.
m. When regulating the identification and verification of beneficial owners, a requirement to stop the financial institution from opening an account, commence business relations or performing transactions when it is unable to identify the beneficial owner satisfactorily.
n. The requirement to terminate the business relationship and to consider making a suspicious transaction report when identification of the customer cannot be performed properly after the relationship has commenced.

311. Iceland should implement the necessary requirements pertaining to PEPs. With regard to correspondent banking, financially institutions should be required to determine that the respondent institution's AML/CFT controls are adequate and effective, and regarding payable through accounts, to be satisfied that the respondent has performed all normal CDD obligations. Iceland should clarify the requirement to establish policies and procedures to address any specific risks associated with non-face to face business relationships or transactions.

3.2.3 Compliance with Recommendations 5 to 8

	Rating	Summary of factors underlying rating
R.5	**PC**	• CDD measures are limited to customer identification requirements and not the full range of measures has been effectively implemented (just been introduced in the new MLA). • Undertaking CDD measures is not required when carrying out occasional transactions that are wire transfers in circumstances covered by the Interpretative Note to SR VII. • There is no general requirement to identify beneficial owners for all customers. Financial institutions are not required to determine actively if the customer is acting on behalf of someone else. • There is no supervision of money remittance or money transfer occurring outside of banks and therefore no means to verify if CDD measures are effectively applied. • No clear requirements regarding the need to take reasonable measures to understand the ownership and control structure regarding legal persons, nor to verify that the natural person purporting to act on behalf of a legal person or legal arrangement is so authorised; • The possibilities for financial institutions to apply no CDD measures are overly broad. There is no assessment to limit the application of such measures to those countries that Icelandic authorities (or financial institutions) are satisfied are in compliance with and have effectively implemented the FATF Recommendations. • No requirement to terminate the business relationship and to consider making a suspicious transaction report when the identification cannot be performed properly after the business relationship has commenced.

		• There are no general requirements to apply CDD measures (other than on-going due diligence) to existing customers on the basis of materiality and risk.
		• A series of obligations have just come into force and therefore have not yet been effectively implemented:
		  • conducting CDD when there is a suspicion of terrorist financing or when there are doubts about the veracity or adequacy of previously obtained customer identification data;
		  • the requirements on the verification of the identity of a legal person or arrangement;
		  • CDD requirements regarding the beneficial owner of legal persons, including the requirement to determine the natural persons who ultimately own or control the legal person,;
		  • the obligation to obtain information on the purpose and intended nature of the business relationship;
		  • enhanced CDD legislation for higher risk categories of customers, business relationships or transactions;
		  • the requirement to stop the financial institution from opening an account, commence business relations or performing the transaction when it is unable to identify the beneficial owner satisfactorily.

R.6	**NC**	• Iceland has not implemented any AML/CDD measures regarding the establishment and maintenance of customer relationships with politically exposed persons (PEPs). Provisions in the new MLA will enter into force in 2007.
R.7	**PC**	• There are no requirements applicable to banking relationships with institutions in EEA countries. • There is no requirement to ascertain that the respondent institution's AML/CFT controls are adequate and effective and, regarding payable through accounts, to be satisfied that the respondent has performed all normal CDD obligations. Regarding the latter, this is limited to the obligation to identify/verify the customer and to perform ongoing due diligence. • Measures regulating correspondent relationships have just been adopted and are not yet effectively implemented.
R.8	**LC**	• The requirement for financial institutions to have policies in place or take such measures as may be needed to prevent the misuse of technological developments in ML or TF schemes is only partially covered. • The requirement to acquire additional information on the customer "when needed" is an open provision which needs further regulation or guidelines to make it effective.

3.3 Third parties and introduced business (R.9)

3.3.1 Description and analysis

312. There were no provisions in the MLA 1999 or other law or regulations regarding the use of third-party introducers of customer identification. However, the private sector acknowledged the possibility to have a third party identifying the customer for the financial institution if this was practically impossible to be performed by the financial institution. There was a general assumption that countries within the EEA automatically are in compliance with the Recommendations. Finally, it seems that financial institutions are relying on third parties for customer identification and verification without the ultimate responsibility remaining with the financial institution.

313. Article 16 of the AML/CFT Act 2006 introduces provisions on the use of third parties and introduced business. This provision states that a financial institution is not required to conduct CDD if corresponding due diligence data is revealed through a financial institution which has been granted an operating licence in Iceland or in the EEA. The same applies for information revealed through a financial institution from outside the EEA which is subject to similar requirements as those from the new MLA. Iceland authorities have clarified that the "revealed" means that the information must be obtained from the foreign financial institution before the Icelandic institution may accept the introduced business. This provision also states that the final responsibility as regards CDD rests with the recipient of the information and that the third party shall, at request of the recipient of the information, promptly make the information available or forward a copy of the appropriate personal data and other appropriate documents proving the identity of the customer or beneficial owner.

314. With this regulation it seems that Recommendation 9 has only been partly addressed in Icelandic law. It seems that the financial institutions are not required to take adequate steps to satisfy themselves that copies of the relevant documentation will be made available from the third party upon request without delay. Article 16 states that the third party is required to provide this information, but in practice this is unenforceable, in case of a third party outside Iceland.

315. There is no general requirement that the financial institution must be satisfied that the third party is regulated and supervised and has measures in place to comply with the CDD requirements. In determining in which countries the third party that meets the conditions can be based, competent authorities do not take into account information available on whether those countries adequately apply the FATF Recommendations. The legislation exempts all third parties within the EEA, and there is no consideration of countries from within the EEA to determine how far they meet the mentioned conditions.

3.3.2 Recommendations and Comments

316. Iceland should clarify that the financial institution is required to take adequate steps to satisfy itself that copies of the relevant information will be made available upon request without delay. Furthermore, some kind of risk assessment should take place to establish that third parties from outside Iceland actually meet the mentioned conditions.

3.3.3 Compliance with Recommendation 9

	Rating	Summary of factors underlying rating
R.9	**PC**	• Certain requirements concerning reliance on third parties in practice are unenforceable, in case of a third party outside Iceland, since the obligations are placed on the third party to provide information upon request. • Financial institutions are not required to take adequate steps to satisfy themselves that copies of the relevant documentation will be made available from the third party upon request without delay. • There is no requirement that the financial institution must be satisfied that the third party is regulated and supervised and has measures in place to comply with the CDD requirements. In determining in which countries the third party that meets the conditions can be based, competent authorities do not take into account information available on whether those countries adequately apply the FATF Recommendations.

3.4 Financial institution secrecy or confidentiality (R.4)

Recommendation 4

3.4.1 Description and Analysis

317. Pursuant to article 58 of the Act on financial undertakings (No. 161/2002), the officers of such undertakings, their employees and other parties who perform services for such undertakings are bound by a duty of confidentiality concerning any kind of knowledge they obtain during the course of their employment and which relates to the personal or business affairs of its customers unless provisions of law stipulate otherwise. Violations of this confidentiality are punishable by a fine or up to one year in prison. Following on to this, Article 7 of the MLA 1999 and Article 17 of the AML/CFT Act 2006 provide that financial undertakings are obliged to thoroughly investigate every transaction where there is suspicion of money laundering and report such transactions to the police authorities. These provisions therefore provide an exception from the duty of confidentiality stipulated by article 58.

318. The same provisions from the MLA 1999 and the AML/CFT Act 2006 clearly hold the power of the police authorities (FIU) to obtain any information deemed necessary on account of a report. There are no provisions of current legislation which limit the possibilities of the police authorities in sharing information obtained pursuant to the above reporting duty, including sharing the information in connection with co-operation with foreign police authorities.

319. The FSA has the ability to access all information they require to perform their supervisory functions, including AML/CFT (Article 9 of the Act on Official Supervision of Financial Activities, No. 87/1998). Article 17 of the MLA 2006 stipulates the disclosure of information which has been disseminated to the police according to the reporting duty of financial institutions. All employees of the FSA are bound by an obligation of confidentiality (Article 13 of the Act on Official Supervision of Financial Activities), notwithstanding the disclosure of information in accordance with the law or based on a court order.

320. According to Article 14 of the mentioned Act the FSA may provide supervisory authorities of other EEA member states with information subject to obligations of confidentiality, if such is part of co-operation between states in supervision and such provision of information is of use in performing supervisory activities in accordance with the law. It may only be provided if it is subject to obligations of confidentiality in the state concerned. Regarding authorities from outside the EEA, agreements may be reached with their supervisory authorities for the exchange of information, provided that obligations of confidentiality are observed in accordance with the Act. The exchange of information between domestic authorities does not seem to be a problem.

321. When Recommendation 7, Recommendation 9 and Special Recommendation VII are fully implemented by law,, it appears that bank secrecy laws will not inhibit the overall implementation of the FATF Recommendations.

3.4.2 Recommendations and Comments

322. Iceland is fully compliant with this Recommendation.

3.4.3 Compliance with Recommendation 4

	Rating	Summary of factors underlying rating
R.4	**C**	

3.5 Record keeping and wire transfer rules (R.10 & SR.VII)

3.5.1 Description and Analysis

Recommendation 10

Transaction records

323. Until the adoption of the AML/CFT Act 2006, there were no provisions in Icelandic anti-money laundering legislation which required financial undertakings to maintain records on individual transactions. However, article 20 of the Act on Accounting (No. 145/1994). This provision requires financial undertakings, as well as other parties which come within the scope of the legislation, to maintain complete accounting records, including documents which accompany such records and any electronic data, for a period of seven years from the end of the relevant fiscal year. In effect this means that almost all Icelandic financial undertakings are under a duty stipulated by Recommendation 10.

324. Article 6 of the Act on Accounting stipulates that the accounts of a financial undertaking shall be kept in such a way that individual transactions and the use of financial resources can be traced easily. Furthermore, Art. 8 provides that every entry in the accounts shall be based on reliable and sufficient data or documents which stem from and are relevant to the transactions carried out, but only states that such documents shall include the identity of the issuer and recipient and such information as may be necessary to verify the transaction in question. This provision does not further specify which kind of information should be recorded.

325. The AML/CFT Act 2006 (article 23(3)) introduces a clear provision requiring the preservation of information on individual customer transactions for a minimum of five years. This covers all reporting entities in the Act. The explanatory notes for the article provide examples of the kind of information that should be kept. "The data should be sufficiently detailed so that the nature of the transaction can be understood and be used as evidence in criminal proceedings. The system must therefore be able to trace individual entries. The data that it is reasonable for a legal person to preserve include information on the name of the customer (and beneficial owner) in addition to address, identity number or other personally identifiable data, type of transaction, time frame of the transaction, currency of the transaction and amount, in addition to type and number of all accounts linked to the transaction."

Customer identification records and account files

326. Article 6 of the MLA 1999 stipulated that financial undertakings should maintain copies of the documents used to ascertain the identity of their customers for a period of five years after the completion of their business relationship. The same applied to documents used to ascertain the identity of legal persons, cf. article 5(3) of the Regulation 1994. Article 23(3) of the AML/CFT Act 2006 reiterates the obligation to maintain all records of customer identity.

327. The Accounting Act also requires financial institutions to maintain all business correspondence. For example, Article 19 requires parties "to keep in an organised manner all incoming letters, faxes and telegrams relevant to its business. He/she shall also keep duplicates of all letters, faxes and telegrams sent to others and are relevant to his/her business."

328. Under the old legislation, there was no general requirement for financial institutions to ensure that all customer and transaction records and information are available on a timely basis to domestic competent authorities upon appropriate authority. However, authorities indicated that the requirements under the Act on Accounting No. 145/1994 generally make it relatively easy for them to find and deliver any documents regarding their customers and their transactions which may be requested by the police authorities. Additionally, many of the Icelandic financial undertakings have incorporated a duty of this sort into their internal rules on money laundering. Nevertheless, article 22(3) of the AML/CFT Act 2006 stipulates that parties which fall within its scope are required to possess a system which enables them to respond swiftly to requests for information from the police authorities.

Special Recommendation VII

329. Iceland has not implemented requirements for Special Recommendation VII. However, authorities plan to address this in the near future. Article 28 of the AML/CFT Act 2006 allows for the Minster of Commerce to issue a government regulation with "further provisions on the implementation of this Act, including: "…(3) Further provisions of what information concerning a remittent must accompany transfers." Authorities plan to issue such a regulation in late 2006. Icelandic authorities also note that certain elements of SRVII are implemented in practice. For example, most domestic wire transfers are carried out by existing customers of the banking system and are cleared through a single clearing house. As a result, originator information is gathered and each transferred can be traced to its originator. Cross-border wire transfers use the SWIFT messaging system; therefore, they also contain originator information and a unique reference number.

3.5.2 Recommendations and Comments

330. Iceland should issue the regulation to implement the requirements of Special Recommendation VII as planned.

3.5.3 Compliance with Recommendation 10 and Special Recommendation VII

	Rating	Summary of factors underlying rating
R.10	**C**	
SR.VII	**NC**	• Iceland has not implemented any requirement regarding obtaining and maintaining information with wire transfers.

Unusual, Suspicious and other Transactions

3.6 Monitoring of transactions and relationship (R.11 & 21)

Recommendation 11

3.6.1 Description and Analysis

331. Pursuant to art. 7(1) of the MLA 1999, financial institutions were required to investigate thoroughly every transaction where there was suspicion of money laundering and report these to the police authorities. While this provision was too narrow to serve as a requirement to financial institutions to pay special attention to all complex, unusual large transactions, or unusual patterns of transactions that have no apparent or visible economic or lawful purpose, article 7 of the Regulation 1994 had a broader scope in that respect. Article 7 of the Regulation 1994 required financial institutions to examine any transaction which was considered unusual, extensive or complicated in view of the customer's normal business activities. Furthermore, the financial institutions had to examine all transactions that appear to have no financial or legal purpose. The background and purpose of such transactions shall be examined to the extent possible. Even though this provision did cover the requirement to monitor unusual transactions, the scope of the Regulation 1994 did not include insurance and securities intermediaries, or money exchange/money remittance businesses.

332. Article 17 of the AML/CFT Act 2006 regulates the transaction monitoring, and it also applies to insurance and securities intermediaries and money exchange/money remittance businesses. Article 17 indicates that "persons under the obligation to report are required to have any transactions suspected of being traceable to money laundering or terrorist financing carefully examined and notify the police of any transactions which are considered to have any such links. This applies in particular to transactions which are unusual, large or complex in the light of the normal business of the customer, or which have no apparent economic or visible lawful purpose."

333. Article 10(2) of the MLA 1999 stated that financial institutions were obliged to compile written reports of all suspicious or unusual dealings which were performed during transactions which they perform as a part of their business. Furthermore, according to article 7 of the Regulation 1994, the background and purpose of such unusual transactions had to be examined to the extent possible and a written report had to be drawn up on the results of such an examination. Article 10(2) also required that such reports must be kept for at least 5 years after the transaction was completed, cf. art. 6.

334. Under the AML/CFT Act 2006 (article 23(2)), all covered entities are required to prepare written reports on all suspicious and unusual records that occur in the course of effecting transactions in their business activities, maintain the records for five years, and have systems in place to be able respond promptly to queries from the police or other competent authorities. However, the requirement to examine the background and purpose of the transaction, from article 7 of Regulation 1994, is not implemented in the new legislation as an active requirement on financial institutions. (And with the coming into force of the new AML/CFT Act, its regulation superseded the 1994 Regulation.) Explanatory notes partly cover this area by stating that "the data should be sufficiently detailed so that *the nature of the transaction can be understood* and be used as evidence in criminal proceedings. The system must therefore be able to trace individual entries. The data that it is reasonable for a legal person to preserve include information on the name of the customer (and beneficial owner) in addition to address, identity number or other personally identifiable data, type of transaction, time frame of the transaction, currency of the transaction and amount, in addition to type and number of all accounts linked to the transaction."

Recommendation 21

335. According to Article 11(2) of the MLA 1999, financial institutions had to pay special attention to states or geographical regions which did not follow international recommendations or regulation on

measures against money laundering. Pursuant to the same provision, the FSA shall issue notices and instructions on cases where special attention shall be paid when conducting business with states or geographical regions which do not follow international recommendations or regulations on measures against money laundering. The same provisions can be found in the AML/CFT Act 2006 (article 26(2)). The FSA informs the financial sector about the NCCT list via a circular letter and publication of this letter on the website. The financial institutions seem to be sufficiently aware of the special attention to be given to these states or regions. Although the FSA has only issued notices regarding NCCTs, the authority exists under Article 26 to warn financial institutions about AML/CFT deficiencies in other countries as well.

336. Pursuant to article 10(2) of the MLA 1999 and article 7 of the Regulation, parties who are under a reporting duty are required to make written reports of any suspicious or unusual trades which take place during their course of business. A similar requirement can be found in article 23(2) of the AML/CFT Act 2006.

337. While the provisions are generally broad, the law does not specifically require financial institutions to examine as far as possible the background and purpose of such transactions, although the explanatory notes for article 23 (2), which covers what should be covered when making written reports, appears to partly cover this issue (see description in paragraph 334 above). There are no provisions dealing with the possibility to apply appropriate counter-measures where a country continues not to apply or insufficiently applies the Recommendations, nor seems there to be any action undertaken by Icelandic authorities to employ such counter measures.

3.6.2 Recommendations and Comments

338. The scope of the requirement to pay special attention to all complex, unusual large transactions or unusual patterns of transactions that have no apparent or visible economic or lawful purpose should be now be put effectively into practice for insurance and securities intermediaries, as obligations for these entities are new. Furthermore, the requirement to examine the background and purpose of the transaction needs to be clearly and effectively implemented.

339. Regarding Recommendation 21, it is recommended to implement provisions dealing with the application of appropriate counter-measures where countries continue not to apply or insufficiently apply the Recommendations.

3.6.3 Compliance with Recommendations 11 & 21

	Rating	Summary of factors underlying rating
R.11	**LC**	• The obligation to examine as far as possible the background and purpose of the transaction is not dealt with explicitly in the legislation and is only partly covered in the explanatory notes. • The monitoring requirements for insurance and securities intermediaries are new and not yet fully implemented.
R.21	**LC**	• The obligation to examine as far as possible the background and purpose of such transactions is not dealt with explicitly in the legislation and is only partly covered in the explanatory notes. • No provisions regulating application of counter-measures.

3.7 Suspicious transactions and other reporting (R.13-14, 19, 25 & SR.IV)

3.7.1 Description and Analysis[21]

Recommendation 13 and SR IV

340. According to Article 7 of Act No. 80/1993 on Measures to Counteract Money Laundering, financial institutions had a direct obligation to "notify" to the National Commissioner of the Icelandic Police any transactions suspected of being traceable to gains from a violation under the Penal Code. The law did not specify whether the obligation must be fulfilled in written form. While the law itself did not specify what level of suspicion is required, the preparatory works indicated that the suspicion must relate to some facts or grounds. This is taken to mean that the required suspicion is lower than reasonable grounds; any grounds to suspect is sufficient.

341. Article 8 of Regulation No. 272/1994 on the Role of Financial Institutions on Measures to Counteract Money Laundering provided further guidance in this area. It indicated that if an examination of a transaction leads to a suspicion that the transaction can be traced to a violation of the General Penal Code or the Addictive Drugs Act the financial institution shall notify the Director of Public Prosecutions and not the National Commissioner of Police. This was because the AML law was amended in 1999—after the 1994 Regulation—to redirect STRs now to be sent to the Police.

342. With the coming into force of the new AML/CFT Act on 22 June 2006 (Act No. 64/2006), the obligation to report STRs related to money laundering is reiterated, and an obligation to report transactions linked to terrorist financing has been strengthened and clarified. Article 17 of the new act states that "persons under the obligation to report are required to have any transactions suspected of being traceable to money laundering or terrorist financing carefully examined and notify the police of any transactions which are considered to have any such links." While this reporting obligation is generally very broad, it should be noted that the reporting obligation does not technically cover insider trading/marked manipulation and arms trafficking, and participation in an organised criminal group, as these are not predicate offences for money laundering. However, Icelandic authorities indicate that this would not present a problem in practice since financial institutions report based on suspicion and without the need to identify the underlying predicate offence.

343. The Regulation for the AML/CFT Act was issued on 27 June 2006 and published on 4 July 2006. Article 3 of the regulation specifies that the "if an examination according to Article 17 of Act No 64/2006 or other incidents lead to a suspicion that a transaction can be traced to money laundering or terrorist financing, a report shall be made to the Economic Crime Department of the National Commissioner of Police."

344. Previously, the reporting obligation in the MLA 1999 did not apply to transactions suspected of being related to terrorism or terrorist financing, including making funds available to a person/entity that committed/attempted to commit terrorist acts, an entity owned/controlled by such a person or any person/entity acting on behalf of/at the direction of such a person/entity. This reporting obligation in Article 7 referred to violations as specified in Article 2 of the law. Article 2 was limited to money laundering—"actions by which an individual or a legal entity accepts or acquires for itself or others, gains by means of a violation punishable under the Penal Code…"

345. Nevertheless, there was an obligation to report transactions linked to terrorism, terrorist organisations, etc, in Public Announcement 867/2001, which aims to implement S/RES/1373(2001). Article 4 of this provision indicates that "If an individual or legal entity with authorisation to provide general financial services in accordance with Section 1, Act no. 80/1993 concerning measures against money laundering, including subsequent amendments to the act, has suspicion of business dealings

[21] The description of the system for reporting suspicious transactions in s.3.7 is integrally linked with the description of the FIU in s.2.5, and the two texts need to be complementary and not duplicative.

covered by Items 1-3 of this Notice, he is obliged to notify the National Commissioner of the Icelandic Police in accordance with the provisions of the above-mentioned Act." Items 1-3 refer to financing of terrorist acts according to certain provisions in the General Penal Code. The provisions referred to include acts causing danger to the public, manslaughter and bodily injuries, and offences against personal freedom; however, the notice pre-dates the broader (but still not fully comprehensive) provisions in the Penal Code. Therefore, the scope of reporting obligation in this system did not fully cover all terrorist financing activity. (See the discussion of Special Recommendation III for further details on the Public Announcements.)

346. The STR obligation applies regardless of amount and regardless of whether they involve tax matters. With regard to attempted transactions, the reporting obligation refers to "any transaction" traceable to money laundering. While the law does not specify further, Icelandic authorities explained that the Icelandic terms are broad enough to include both completed and attempted transactions, and this is how the obligation is observed by the private sector. This is further clarified by the fact that reporting FIs are not permitted to carry out any transaction where there is knowledge of or reason to suspect that they are traceable to a violation as referred to in Art. 2 of the Act (Article 2, paragraph 3). In practice, the financial institution will normally call the FIU to determine whether or not to proceed with the transaction, so in many cases STRs are in fact filed when the transaction has not been completed. However, it should also be noted that the private sector expressed differing views on this subject. See section 2.5 of this report, which further details how the FIU receives and processes STRs.

347. The number of STRs received by the DPP and later the FIU is as follows:

Year	Number	Total amount involved (ISK)
1994	1	
1995	9	49,780,000
1996	2	11,691,000
1997	11	93,340,693
1998	25	11,097,672
1999	55	49,558,051
2000	113	130,875,898
2001	125	847,690,651
2002	189	250,036,428
2003	241	303,417,508
2004	301	393,829,668
2005	283	596,216,345

348. The origin of STRs 2003 – 2005

Sender	2003	2004	2005
Landsbanki Íslands (bank)	58	77	96
Glitnir (Íslandsbanki) (bank)	68	47	41
KB banki (bank)	18	20	39
Sparisjóður Kópavogs (s.bank)	10	2	
Sparisjóðurinn í Keflavík (s. bank)	7	10	1
Sparisjóður vélstjóra (s. bank)	19	16	15
Sparisjóður Vestfirðinga (s. bank)	2	0	
Sparisjóðabankinn (central s. bank)	1	1	1
Sparisjóður Ólafsvíkur (s. bank)	1	0	
Sparisjóður Húnaþings (s. bank)	1	0	
Spron (s. bank)			7
Sparisjóður Hafnarfjarðar (s.bank)			10
Sparisjóður Vestfjarða (s.bank)			1
Western Union	40	104	66
Kreditkort hf. (Creditcard issuer)	0	2	
Íslensk getspá (lotto and football tipping)			1
Icelandic Police			1
Other	3	6	
Total:	228	285	284

349. The statistics show a positive trend and appear to demonstrate a growing awareness and compliance within the banking sector with AML obligations. For the period 2000 to 2005, the number of STRs has increased by approximately 2.5 times and the value of these reported transactions has increased by approximately 4.6 times. Numbers of reports have increased steadily each year—with only a slight decline in 2005—and the amounts affiliated with those transactions have also increased. As expected, the larger "banks", which hold the vast majority of accounts and assets in Iceland, account for a large percentage of STRs. The FIU provided statistics for 2004 and 2005 that demonstrate that the vast majority of STRs that they have received are related to suspected narcotics cases. This also corresponds to the sharp increase of drug related offences over that same timeframe. (See Section 1 of this report for overall crime trends and statistics.

350. On the other hand, there is an uneven distribution from the reporting agencies. A large portion of STRs have been filed by Western Union; authorities at the Economic Crime Unit indicated that these transactions were higher threshold transfers suspected of being linked to drug trafficking. Fourteen savings banks have not yet filed an STR. No STR has been filed by the insurance or securities sectors; the foreign exchange office (Forex) has not filed an STR; although it has been in operation for a year. Overall, there are some concerns about the effectiveness of the system; there has been little guidance given to reporting entities on the form and manner of reporting, and there have been few results shown from the increased reporting which also corresponded to an increase in drug trafficking activity.

Recommendation 14

351. Act No. 80/1993 protected "good faith" reporting by providing a clear exemption from otherwise strict confidentiality rule. Article 12 indicated that "when an individual or legal entity covered by this Act provides to the police in good faith, with information as provided for in this Act, this shall not be deemed in conflict with obligations of confidentiality to which it/he/she may be subject by law or otherwise. Provision of such information shall not make the individuals, legal entities, or employees in question criminally liable or liable for civil damages." Consequently, filing an STR in good faith could not be used as a basis for bringing legal action against either the Reporting FI or its employees.

352. There is a general obligation to maintain confidentiality unless required by law to disclose information. According to Act No. 161/2002 on Financial Undertakings, the board of directors, managing directors, auditors, personnel and any persons undertaking tasks on behalf of the undertaking, shall be bound by an obligation of confidentiality concerning any information of which they may become

aware in the course of their duties concerning business dealings or private concerns of its customers, unless obliged by law to provide information.

353. Article 21 of the new Money Laundering Act (Act No. 64/2006) contains a similar exemption from criminal or civil damages or breaches of professional secrecy when reporting in good faith the police. It is very important that exceptions from this legal obligation of confidentiality are clear. Any communications between financial institutions and the National Commissioner of the Icelandic Police, on the grounds of Act No 80/1993 as an exception from the rule of confidentiality towards clients, had to be regulated thoroughly within the legal framework.

354. "Tipping off" a customer or any third party in connection with reporting a STR is prohibited. Article 9 of the MLA 1999 indicated that neither the customer nor any third party should be informed that such investigations were in progress. Nor should the customer or any third party be informed that information had been provided to the National Commissioner of Police (MLA 1999, article 9). Iceland reports that the prohibition against tipping off applies to the Reporting FI as well as its directors, officers and employees (whether permanent or temporary).

355. Article 20 of the Act No. 64/2006, first paragraph, contains the same prohibition on tipping of customers or other third persons. However, the second paragraph provides for some exemptions on this prohibition (i.e., permits the disclosure of information) in certain circumstances, including:

- to the FSA;
- between lawyers and/or auditors who are working for the same legal person or enterprise;
- between financial institutions or lawyers or auditors where both parties belong to the same professional category, the case concerns a natural or legal person who is a customer of both parties and concerns a transaction relating to both parties, both parties are subject to equivalent professional secrecy obligations, and the information is used exclusively for the purposes of preventing ML/FT.

Additional elements

356. Reporting STRs to the FIU is generally the responsibility of a senior manager who has been assigned special responsibility for this task (i.e. the compliance officer). Iceland reports that the identity of other employees (i.e. the person who initially formed the suspicion about the transaction) is kept confidential. No statutory legislation exists to protect the senior manager who bears this responsibility; however, only authorised persons at the National Commissioner of Police have access to the database containing this information. It is, however, unclear who the persons are, the team learned that several persons within the National Commissioner of Police had access to some received information from reporting entities. The name of the compliance officer does appear in the reports that are sent to the police districts, but not the name of the bank employee who was involved in the transaction. The secrecy safeguards at the police are now stipulated in detail in Art. 4 of the new Regulation No. 626/2006.

Recommendation 25 (Guidelines and feedback on STRs)

357. Competent authorities have not established guidelines that will assist financial institutions to implement and comply with STR requirements. Reporting entities that the assessors met with asked for guidance concerning AML/CFT obligations, including STRs.

358. The activity initiated by the authorities has so far been very limited in order to provide feedback. The FIU provides some case-specific feedback by way of acknowledging each STR received (which is required by pursuant to Article 8 of the MLA 1993/1999, Article 19 of the new AML/CFT Act of June 2006, and Article 12 of Regulation 626/2006). However, there is generally not feedback regarding any results of the STR filed. There is some very basic feedback provided by the FIU during meetings with representatives from the regulated sectors. However, there is no substantive general feedback such as statistics on the number of disclosures and results, information on techniques, methods and trends, or sanitised case examples.

359. This situation should be improved when the provisions of the new Regulation 626/2006 of 12 July 2006 are fully implemented. Article 12 requires that reporting entities be informed of the FIU's decision regarding the STR it receives (i.e., the deletion of the record, the registering of the STR in the database for intelligence purposes, or the decision to open an investigation.) General feedback and statistics must be published pursuant to Article 13 (see paragraph 183.)

360. During the on-site visit, the evaluation team was told that the AML/CFT Committee was working hard with future plans regarding guidelines and feedback and that guidelines would be issued from both the FSA and the FIU after the new AML/CFT Act enters into force. The FSA had already hired one new person to deal solely with AML/CFT issues; this person began work in June 2006 and tasks include the development of guidelines. The new legislation entered into force on 22 June 2006; the team was thereafter informed that guidelines were being prepared, with plans to issue a draft in October 2006 for consultation with financial institutions.

Recommendation 19

361. Iceland has considered the feasibility and utility of implementing a system where financial institutions report all transactions in currency above a fixed threshold to a national central agency with a computerised database. A new AML project is being developed jointly by Iceland's commercial banks and the Icelandic Bank's Data Center. The software system will cover retail banking, to include transactions, customers and accounts from financial institutions. The system will capture information on every customer transaction (including large cash transactions) and create a profile for every customer. The Data Centre monitors the pattern of the customers' transactions and provides technology for banks to target and assess ML risks and the identification of trends.

Recommendation 32[22] (Statistics)

362. Authorities maintain statistics on STRs received, including a breakdown by financial institution and DNFBP.

3.7.2 Recommendations and Comments

363. Iceland should ensure that non-bank financial institutions, including money exchange and MVTS providers, are properly supervised so as to comply with their reporting obligations. Steps should also be taken to refocus reporting in general to concentrate more on the nature of the transaction.

364. Comprehensive guidelines should be given to the financial sector which should be direct and broad and based on the different typologies, trends and techniques that focus more attention on the nature of transactions themselves. Additional guidelines that are more tailored to particular types of financial institutions should also be issued. The FIU should also deliver more specific feedback to reporting entities, particularly concerning the status of STRs and the outcome of specific cases. Iceland reports that the FIU's ability to deliver such feedback is expected to improve if the staffing problem is solved.

3.7.3 Compliance with Recommendations 13, 14, 19 and 25 (criteria 25.2), and SR IV

	Rating	Summary of factors underlying rating
R.13	**PC**	• The reporting obligation does not cover transactions related to insider trading/market manipulation, arms trafficking, and participation in an organised criminal group (or otherwise cover this fully through conspiracy) as these are not predicate offences for money laundering in Iceland. • The clear obligation to report an STR related to terrorist financing has just

[22] See Section 7.1 for the compliance rating for this Recommendation.

		been adopted in June 2006; its effectiveness cannot yet be assessed. • There are some concerns about the effectiveness of the system: the insurance and securities sectors have not filed an STR; exchange offices have not filed STRs (and are not subject to supervision) • There has been little guidance given to reporting entities on the form and manner of reporting, and there have been few results shown from the increased reporting.
R.14	**C**	• Recommendation 14 is fully observed.
R.19	**C**	
R.25	**NC**	• Competent authorities have not established guidelines that will assist financial institutions to implement and comply with STR requirements. • The activity initiated by the authorities has so far been very limited in order to provide feedback. There is only basic specific feedback and no substantive general feedback such as statistics on the number of disclosures and results, information on techniques, methods and trends, or sanitised case examples.
SR.IV	**LC**	• The clear obligation to report an STR related to terrorist financing was adopted in June 2006; its effectiveness cannot be assessed yet. • Some concerns raised above in Recommendation 13 about the effectiveness of the reporting system apply equally to SR IV.

Internal controls and other measures

3.8 Internal controls, compliance, audit and foreign branches (R.15 & 22)

Recommendation 15

Internal procedures, policies, and controls to prevent ML/FT

365. The MLA 1999 required financial institutions to maintain internal controls to combat money laundering. According to article 2(8) of the MLA 1999 all persons and entities covered by the MLA must develop co-ordinated working practice supporting the implementation of the MLA. "Individuals and legal entities referred to in Article 1, and their employees, shall be responsible for compliance with the provisions of this Act and of any regulations and rules adopted in accordance with it. They shall nominate a specific individual to be generally responsible for providing notifications in accordance with Article 7 and develop co-ordinated working practices supporting the implementation of this Act. The National Commissioner of Police shall be informed of the nomination of the responsible individual." In addition, Article 10(1) of the MLA 1999 read as follows: "Individuals and legal entities referred to in Article 1 shall operate a system of internal control designed to prevent use of their operations for crime-related transactions. To this end they shall for instance ensure that their employees receive special training."

366. While this generally covered the requirement for internal controls to prevent ML, the MLA 1999 did not require controls to prevent terrorist financing; nor did it require specific internal procedures and policies to prevent ML/FT. Also, neither the MLA nor does the Regulation 1994 included rules on the subject of such internal controls.

367. According to Article 23 of the AML/CFT Act 2006, persons under obligation to report are required to establish written internal rules and maintain internal controls designed to prevent their business activities from being used for both money laundering and terrorism financing. However, the law does not specify that they procedures should cover, inter alia, CDD, record retention, the detection of unusual and suspicious transactions and the reporting obligation. While the FSA indicates that in practices it looks for such controls to cover CDD measures, record keeping, the detection of unusual and suspicious transactions and the reporting obligations, these are not laid out in law, regulation, or other enforceable means. Icelandic authorities note that the explanatory notes for this state that the provision is meant to implement Articles 34(1) and 35(1) of the 3rd ML Directive, and Article 34 of the Directive specifies that the written internal rules should cover what is mentioned in the law, inter alia, CDD, record retention, etc. However, the evaluation team could not conclude that this was a satisfactory legal obligation on financial institutions.

Compliance management systems

368. While Article 8 of the MLA 1999 requires financial institutions to nominate a specific individual to notify and develop specific practices supporting implementation of the Act. While the law did not specify that that person should come from the management level, this was provided for in Article 12 of the Regulation 272/1994, which indicated that "each financial institution shall nominate an employee from among the managers who will be responsible for compliance with provisions of the MLA and the provisions of the Regulation. Such an officer shall be in charge of developing work procedures within the financial institution for this purpose. Furthermore, the compliance officer, shall be responsible for the institution's internal control of measures against money laundering, decides on a special examination in accordance with Article 7 of the Regulation and on a notification to the FIU." It should be noted, however, that the regulation did not cover insurance and securities intermediaries, or bureaux de change or money remittance activity outside of the banking sector, and therefore the requirement for a compliance officer at the management level did not apply to these persons.

369. This deficiency is clarified in the new legislation. According to Article 22 of the AML/CFT Act 2006, persons under the obligation to report shall nominate a person at the managerial rank to be generally responsible for notification and practices supporting implementation of the Act.

370. There is no requirement that the AML compliance officer and other appropriate staff have timely access to CDD, transaction, and other relevant information. However, it is the FSA's impression that all appropriate staff in the financial institutions has access to the information needed to carry out their duties, including access to customer records.

Internal audit function

371. There is not a specific requirement to maintain an adequately resourced and independent audit function to test compliance (including sample testing) with AML/CFT procedures and controls. There is a general requirement for all financial undertakings to have an auditing section handling internal auditing according to Article 16 of the Act on Financial Undertakings (FUA). The Board of Directors of a financial undertaking shall engage the director of the undertaking's auditing section, who shall be responsible for internal auditing on its behalf. It should be noted Article 16 does not apply to securities brokerages and electronic money undertakings. Internal auditing shall be part of a financial undertaking's organisational structure and one aspect of its internal surveillance system. The FSA may however, regarding the nature and scope of the operation, grant an exemption from the operation of such an auditing section and set conditions for undertakings granted such exemptions. Iceland authorities note that, in accordance with general principles and best practice, functions of internal audit departments of financial undertakings should cover all the activities of the institutions and their obligations in accordance with the legislation applicable to their operations (including AML/CFT issues); however, this is not laid out in law.

Training

372. Article 13 ("Training of Employees") of the AML/CFT Regulation 1994 required financial institutions to provide "employees with special instruction on their responsibilities under this Regulation and the Act on Measures against Money Laundering as well as special training to enable them to verify which transactions could possibly be linked to money laundering." Article 23 of the new AML/CFT Act 2006 broadens this requirement to cover all financial institutions and also covers terrorist financing. However, the training requirements do not specify that the training programs be on-going so as to be kept informed of new developments, or specify that they should cover ML And FT techniques, methods and trends. Icelandic authorities note that the explanatory notes concerning Article 23(1) state that the provision is meant to implement Articles 34(1) and 35(1) of the 3rd EU ML Directive, and that according to Article 35 undertakings are obliged to ensure that their employees have knowledge of the provisions of the Directive and ongoing training programs are especially mentioned. Nevertheless, the evaluation team could not conclude that this was a satisfactory legal obligation on financial institutions.

373. Internal rules of individual financial institutions also contain provisions on the training of employees. According to some of the rules employees shall be offered relevant training in those measures operated by financial institutions at any given time to prevent money laundering and terrorist financing. It shall be ensured that such knowledge and training is maintained and it shall take into account the technology and methods which are used to combat money laundering at any given time.

374. The team was told that some special training sessions for frontline employees are organised. These sessions include discussions of laws and regulations on measures against money laundering, which documents should be obtained when commencing a business relationship, to whom suspected money laundering should be reported and what obligations are employees of the financial institution pursuant to the Money Laundering Act. These employees receive special training which makes it easier for them to establish which transactions may be connected with money laundering. Other employees of financial institutions also attend courses at which regulations on the subject, and the relevant legislation on measures against money laundering and terrorist financing are discussed.

Screening procedures

375. Financial institutions are generally required to put in place screening procedures to ensure high standards when hiring employees. According to Article 10(3) of the MLA, legal entities covered by the Act must, when hiring personnel, adopt special rules as to what investigations shall be made into the background of applicants for positions with the companies and in what instances certificates of offences or other similar documentation on background and previous pursuits should be required. A similar requirement is included Article 23 of the new AML/CFT Act 2006.

Additional elements

376. An important issue is whether AML/CFT compliance officers are able to act independently and to report to senior management above the compliance officer's next reporting level or the board of directors. This situation is not clear in Iceland. The explanatory notes pertaining to Article 21 of the AML/CFT Act 2006 indicate "that it should be specified that person responsible should be of managerial rank; this is intended to implement FATF Recommendation 15. The words "of managerial rank" as regards smaller enterprises means that the person in question should have the position of managing director, but as regards larger enterprises that the person should be, e.g. assistant director or director of legal affairs." Therefore, the compliance officer should be able to report to senior management above and board of directors. This underlines his/her independence.

Recommendation 22

377. The vast majority of Icelandic financial institutions' foreign branches and subsidiaries are located in EEA countries. The three commercial banks operating in have activities abroad. One has subsidiaries in Sweden, Denmark, Norway, Finland, Faroe Islands, the United Kingdom, the United States, Switzerland and Luxembourg; One has subsidiaries in the United Kingdom, France, Ireland, and Luxembourg and operates one branch in the United Kingdom. Another has subsidiaries in Norway and Luxembourg and is operating branches in UK and Denmark. Two have opened a representative office in Canada and the other is in the process of opening a representative office in China. One investment bank is operating a branch in Denmark and another is operating a branch in the UK. One insurance company has a subsidiary in the UK. Two insurance companies are holding shares in insurance companies in Norway.

378. In general, all domestic legislation, including the MLA 1999 and the AML/CFT Act 2006, applies to foreign branches of domestic financial undertakings. The new AML/CFT Act 2006 also introduces some more detailed requirements. Article 24 requires that Icelandic institutions ensure that their branches and subsidiaries outside the EEA take equivalent measures regarding CDD or as similar as the legislation of the state in question will permit. There are no requirements for branch/subsidiaries in EEA countries—without any assessment of the particular AML/CFT risk of that country—to apply AML/CFT rules consistent with the Icelandic standard. There is no requirement that foreign branches and subsidiaries outside EEA countries observe Icelandic standards for AML/CFT other than for CDD.

379. Where the AML/CFT standards differ, there is no requirement to apply the higher AML/CFT standards. The legislation does not specify that financial institutions must pay particular attention that this principle is observed with respect to their branches and subsidiaries in countries which do not or insufficiently apply the FATF Recommendations. However, the explanatory notes to the article indicate: "the parties referred to in the provision should ensure that their branches and subsidiaries in states outside the European Economic Area should conduct customer due diligence in a manner comparable with the stipulations of this Act. This obligation includes the obligation to preserve photocopies of identity documents. The provision applies in particular where the branch or subsidiary is in a state which does not observe the FATF Recommendations in a satisfactory manner." However, this principle does not apply to branches or subsidiaries within the EEA.

380. The FSA is responsible for the supervision of Icelandic financial institutions, including their establishments abroad (unless such an establishment is under supervision of the host state), as well as any

other companies which may be part of the group. The evaluation team was informed that this has not been high on FSA's agenda up to this point, but it can also be pointed out that the vast majority of the foreign operations of the Icelandic banks have been in the form of subsidiaries and not branches. At the end of 2004, there were only two branches of Icelandic banks operating abroad, but the number of foreign branches today is nine. The evaluation team was also informed that during the year 2004, the FSA made visits to the two foreign branches operating at the time. The FSA has indicated that where permission is sought to establish a branch or subsidiary in a foreign country with lesser AML/CFT measures, it will adopt the policy of requiring that the foreign branch/subsidiary complies with Icelandic AML/CFT standards. However, no cases have so far emerged in relation to subsidiaries established abroad.

381. Article 24 of the new legislation introduces the requirement for a financial institutions (outside the EEA countries) to inform the FSA if its foreign branch or subsidiary is unable to observe appropriate AML/CFT measures because this is prohibited by the laws or regulations of the host country.

3.8.2 Recommendations and Comments

382. Reporting FIs should be obligated to implement satisfactory internal controls with respect to audit functions for AML/CFT. It should be clarified that the compliance officer should have timely access to CDD and other records, and that financial institutions should provide on-going training programs. Iceland should also implement comprehensive obligations for all foreign branches and subsidiaries to observe full AML/CFT measures consistent with Icelandic requirements and the FATF Recommendations to the extent that host country laws and regulations permits and that the branches and subsidiaries should apply the higher standard, where the AML/CFT standards differ. Iceland should also implement a requirement that a financial institution inform the FSA if its foreign branch or subsidiary in an EEA country is unable to observe appropriate AML/CFT measures because this is prohibited by the laws or regulations of the host country.

3.8.3 Compliance with Recommendations 15 & 22

	Rating	Summary of factors underlying rating
R.15	**PC**	• Neither the MLA 1999 nor the AML/CFT Act 2006 includes rules on the subjects that the internal controls should cover. • There is no requirement that the AML compliance officer and other appropriate staff have timely access to CDD, transaction, and other relevant information. • There is no specific requirement to maintain an adequately resourced and independent audit function to test compliance (including sample testing) with AML/CFT procedures, policies and controls. • The training requirements do not specify that the training programs be on-going so as to be kept informed of new developments, or specify that they should cover ML and FT techniques, methods and trends. • There are some preliminary concerns about how effectively internal controls have been implemented. For instance, there is no legal obligation to implement internal controls to ensure that full CDD is performed. • The requirement for all financial institutions to have a compliance officer at the managerial level is new and not yet fully implemented.

R.22	**PC**	• There are no requirements for branch/subsidiaries in EEA countries (the vast majority of foreign activities of Icelandic financial institutions)—without any assessment of the particular AML/CFT risk of that country—to:
		  • apply AML/CFT rules consistent with the Icelandic standard.
		  • pay particular attention that this principle is observed with respect to their branches and subsidiaries in countries within the EEA which do not or insufficiently apply the FATF Recommendations.

		• inform the FSA if its foreign branch or subsidiary is unable to observe appropriate AML/CFT measures because this is prohibited by the laws or regulations of the host country. • There is no requirement that foreign branches or subsidiaries (either within or outside EEA countries) observe Icelandic standards for AML/CFT other than for CDD. • Where the AML/CFT standards differ, there is no requirement to apply the higher AML/CFT standards. • The obligations that do exist are new and have not yet been put effectively into practice; there has not yet been adequate focus on the issue within the FSA.

3.9 Shell banks (R.18)

3.9.1 Description and Analysis

Recommendation 18

383. It is not possible to establish a shell bank in Iceland. According to Article 15 of the Act on Financial Undertakings, a financial undertaking, which has been granted an operating license in accordance with Article 6, must have its head office in Iceland. In addition, according to article 5 an application for an operating licence shall be *inter alia* accompanied by information on the operational structure, including information as to how the activities proposed will be carried out and information on the internal organisation of the undertaking, including rules on supervision and work procedures. According to Article 9 the FSA may revoke a financial undertaking's operating licence if the undertaking does not utilise its operating licence within twelve months of its granting.

384. According to Article 13 of the new AML/CFT Act 2006 Article ("Correspondent banking business with shell banks") credit institutions falling within the scope of the new AML are prohibited from entering into or continuing a correspondent banking relationship with a credit institution or another party engaged in similar business activities which is established within a jurisdiction where it has no real business activities or management and which is not related to a financial consolidation which is subject to regulation. Institutions are also prohibited from engaging in correspondent banking business with banks that permit such credit institutions to use their accounts. The requirements are generally broad, and it appeared that they were already being effectively implemented shortly after the coming into force of the law.

3.9.2 Recommendations and Comments

385. Iceland is fully compliant with this Recommendation.

3.9.3 Compliance with Recommendation 18

	Rating	Summary of factors underlying rating
R.18	**C**	

Regulation, supervision, guidance, monitoring and sanctions

3.10 The supervisory and oversight system – competent authorities and SROs: Role, functions, duties and powers (including sanctions) (R.23, 30, 29, 17, 32 & 25)

3.10.1 Description and Analysis

Authorities/SROs roles and duties & Structure and resources - R.23, 30

Recommendation 23 (Criteria 23.1 and 23.2)

386. The Financial Supervisory Authority is the designated competent authority to supervise a wide range of financial institutions, according to Act No. 161/2002 on Financial Undertaking. According to the Act, the FSA has power to supervise:

- commercial banks and savings banks,
- credit undertakings,
- insurance companies,
- companies and individuals acting as insurance brokers,
- securities companies and brokerage,
- mutual funds (UCITS) and management companies,
- stock exchanges and other regulated markets
- central securities depositories (CSD),
- pension funds,
- parties other than those mentioned in item 1 which are authorised by to law to receive deposits. (Depository Departments of Co-operative Societies)

387. The Act also governs the supervision of other activities which the FSA has been authorised to supervise in accordance with special laws. All licensed financial institutions and their branches in Iceland are covered by the MLA.

388. The number of financial institutions subject to supervision by the FSA were as follows as of 1 January 2006. These activities are all included in the Icelandic Money Laundering Act (MLA). A description of their institutions' activities according the FATF definition of "financial institution" is contained in the subsequent chart.

Institution	Number
Commercial banks	4
Savings banks	24
Credit undertakings:	10
Credit card companies	2
Leasing companies	2
Investment banks	4
Other credit undertakings	2
The Housing Financing Fund*	1
The New Business Venture Fund**	1
Securities companies	7
Securities brokerage	3
Life insurance companies	4
Insurance intermediaries:	
Licensed brokers	8
Authorised insurance agents (such as banks and other intermediaries) that act on behalf of insurance companies	Unknown
Management companies of UCITS	6

389. According to Article 8 of the Act no. 87/1998 on Official Supervision on Financial Activities, the FSA shall ensure that the activities of parties subject to supervision are in accordance with laws, regulations, rules or by-laws governing such activities, and that they are in other respects consistent with sound and proper business practices. At the time of the on-site visit, there was no specified authority for the FSA to supervise financial institutions for compliance with the Money Laundering Act; however, the FSA was using these general supervisory provisions for AML supervision. The new AML/CFT Act now specifies that the FSA is the competent authority for AML/CFT issues as to the entities covered by the act.

390. At the time of the on-site visit, there was no specific CFT regulation in place, so CFT supervision had not taken place. Nor did the ML Regulation in place cover insurance/securities intermediaries. Both of these issues have been incorporated in the new AML/CFT Act.

391. The supervision of financial undertakings comprises commercial banks, savings banks, credit undertakings, investment banks, electronic money undertakings, securities companies, securities brokerage and management companies for UCITS. The supervision of the insurance sector covers insurance companies and insurance brokers and agents. The securities market supervision includes undertakings permitted to operate stock exchanges, authorized markets and central securities depositories.

392. The FSA's supervision is largely conducted through regular collection of information on the operations and financial position of parties subject to supervision (off-site), various specific surveillance operations (on-site) and written enquiries on specific aspects.

393. The FSA co-operates with other Nordic financial supervisory authorities as well as taking part in European co-operation of supervisory authorities and expert groups in relation with Iceland's participation in the European Economic Area.

394. It is illegal to perform regulated activities (such as the provision of financial services as defined in Act 87/1998) without authorisation. However, MVTS operators are not covered under this legislation and not required to be licensed or registered. Icelandic authorities believe that there are no MVTS operating in Iceland outside regulated financial institutions. There is no other specific provision to regulate or supervise money transfer service businesses that might operate outside of banks.

395. All known money remittance services currently operate through institutions with banking licenses. Known money exchange business also occurs either through banks, although in one case this occurs through a foreign branch of a bank licensed in another Nordic country, and the supervision of this entity does not yet appear adequate. This branch has been in Icelandic for approximately one year; however, no supervision has yet taken place. In addition, there is one licensed money exchange business which operates outside of a banking license. This entity is licensed by the Central Bank but is not subject to any supervision.

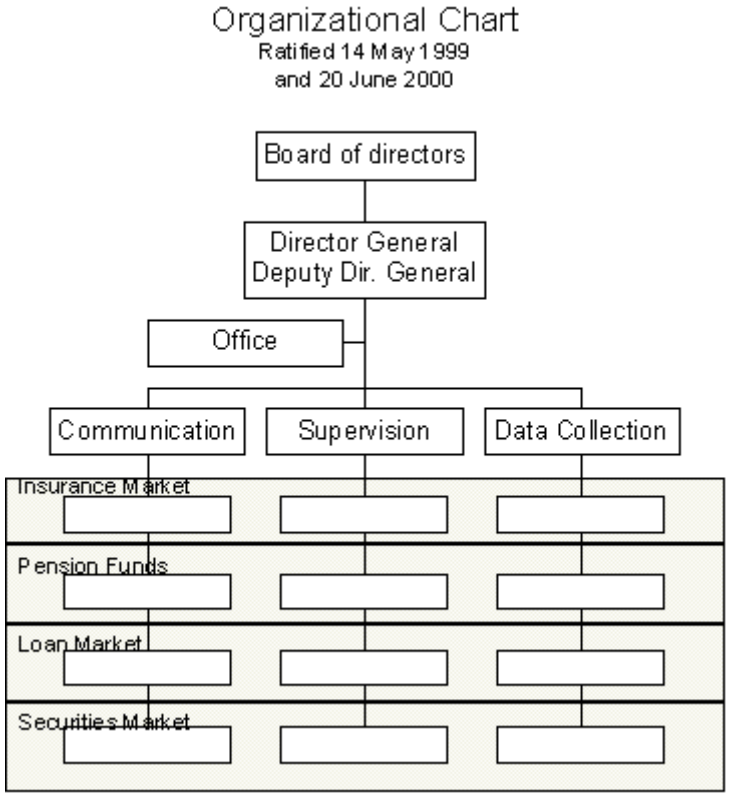
396. In line with the general practice of other financial regulators, the FSA allocates its supervisory resources on a risk sensitive basis. FSA supervision is also founded on a risk-based approach. According to Icelandic authorities, no entities supervised by the FSA are overlooked, but the weaker ones would generally get more attention than others considered to be better managed. The FSA has stated that it looks to Core Principles in its supervision of banks, insurers and investment firms and tries to co-ordinate this approach with AML/CFT supervision. FIs are obliged to produce self-assessment reports that are used by the FSA to determine which FIs will be visited on-site. However, these self-assessments are based on the prudential supervision and contain no AML/CFT questions.

397. There are concerns about how effectively the financial sector has been supervised regarding AML; while the FSA indicated that AML/CFT assessments of financial institutions are part of regular visits, the very limited findings – and number of warnings – indicates that the focus on AML/CTF has been inadequate. Only very limited information on AML supervision was provided, although the team learned that the approach will be changed in the future. Also, at the time of the on-site visit, financial

institutions were not subject to adequate supervision of compliance with CFT requirements (since CFT requirements were not in place). At the time of the on-site visit, the FSA was in the process of acquiring one full-time staff to be permanently tasked with AML/CFT issues.

FSA structure, funding, staffing, resources[23]

398. The FSA operates in accordance with the Act on Official Supervision of Financial Operations. The FSA is a public authority governed by a special Board of Directors, but under the administrative jurisdiction of the Minister of Commerce. The Board of Directors consists of three board members which are appointed by the Minister of Commerce for a term of four years. One Board Member is nominated by the Central Bank of Iceland. The Board appoints a Director General who is responsible for daily administration, but all major decisions must be referred to the Board for approval or rejection. The FSA began its operation on 1 January 1999. Before that time the Bank Inspectorate of the Central Bank of Iceland and the Insurance Supervisory Authority carried out the supervision.



399. At the time of the on-site visit, the FSA had 35 employees, of which 4 are secretaries and 31 have an academic education. By the end of 2006, the FSA expects to have a total of 40 employees. The supervisory role of the FSA is divided into 4 sectors; financial undertakings sector, insurance sector, pension funds sector and securities market sector.

400. It was the view of the evaluation team that adequate staff had not been provided for AML/CFT supervision. One person was in the process of being hired to specialise in these tasks (this person was hired in June 2006); it was therefore not clear if this would be adequate to deal with the workload, and additional resources might be needed. Icelandic authorities also recognised that, because of the relatively large and growing activities abroad provided by the Icelandic banking sector it was needed to strengthen the FSA with more staff etc.

[23] As related to Recommendation 30; see Section 7.1 for the compliance rating for this Recommendation.

401. A supervision fee paid by the parties subject to supervision covers the operational expenses of the FSA. The FSA budget is ISK 410 million for 2006. Approximately 3% of that is dedicated to training. The FSA believes that the current funding with regard to training is adequate; but the FSA is of the opinion that the budget needs to be increased in relation to increased responsibilities and the growing size of the financial sector.

Professional standards, integrity, and confidentiality

402. The FSA has recently adopted a new procedure regarding hiring new staff. Applicants are required to have appropriate knowledge of the financial market and the legislation covering the financial market and their knowledge and other skills are tested in the application procedure. Applicants shall also present a certification from the National Criminal Record.

403. To ensure the credibility of the FSA, its employees and the members of the Board, the Act on Official Supervision on Financial Operations contains provisions that are designated to avoid conflicts of interest between those individuals and the financial market (Articles 6(2) – 6(4)). In accordance with these articles, the Minister has set rules concerning relations by members of the Board, the General Director and employees with parties that are subject to supervision. Those rules include provisions concerning limitations on the extent to which financial obligations or shares may be held towards parties that are subject to supervision and require employees to report to the Director General.

404. The confidentiality of information on the operation of the Financial Supervisory Authority, the business and operation of parties subject to supervision, related parties or others, is required in the Act on Official Supervision on Financial Operations and an infringement of the provisions of the Act is punishable in accordance with the Penal Code. In addition, new staff is required to sign a declaration regarding the confidentiality obligation.

Training

405. The FSA has organised internal lectures on AML/CFT issues and the employees responsible for supervision have attended courses related to this matter. However, the FSA does not maintain statistics with regard to this.

406. Icelandic authorities indicated that the FIU, FSA and the AML Committee have provided lectures and seminars on actions against money laundering and financing of terrorism. For example, two lectures were held for AML compliance officers in February and March 2006. Nevertheless, in the view of the evaluation team, it did not appear that there was yet adequate training on AML/CFT issues, such as the scope of predicate offences, ML and FT typologies, and the techniques to be used by supervisors to ensure that financial institutions are complying with their obligations; the use of information technology and other resources relevant to the execution of their functions. The training activities should also cover the work related to fighting ML/FT internationally.

Authorities Powers and Sanctions – R.29 & 17

Recommendation 29

Powers to monitor and ensure compliance with AML/CFT obligations

407. According to Article 8 of the act on Official Supervision on financial undertakings, the FSA shall ensure that the activities of parties subject to supervision are in accordance with laws, regulations, rules or by-laws governing such activities, and that they are in other respects consistent with sound and proper business practices. In particular, the FSA is responsible for supervising the compliance of financial institutions with applicable AML measures, (and with the recent enactment of the revised MLA, CFT measures as well. This involves examining the financial institution's internal control measures, internal ethical and professional policies, practices and guidelines, including those related to AML/CFT

408. The Act gives the FSA generally comprehensive inspection and surveillance powers for supervised entities. The FSA has the power to require information from supervised institutions, and to conduct on-site inspections in addition to off-site review. On the other hand, no supervisory powers exist for unlicensed financial institutions not under FSA's supervision, such as foreign exchange companies or foreign remittance dealers that may operate outside of banks. There are no written regulations or guidelines prescribing the procedure that the FSA must follow during an inspection, particularly with regards to detecting breaches of AML/CFT legislation. The FSA is now in the process of reorganising the AML/CFT supervision, including the above mentioned.

409. The FSA's power to compel production of or obtain access to a financial institution's records is not predicated on the need to obtain a court order. At all times, the FI is obliged to furnish all information that the FSA may require. Article 9 ("Inspection and Access"), paragraph 1, of the Act on Official Supervision No. 87/1998 indicates that the "FSA shall inspect the operations of regulated entities as often as deemed necessary. These entities must grant the FSA access to all their accounts, minutes, documents and other data in their possession regarding their activities which the FSA considers necessary." Therefore, such inspections can include the review of policies, procedures, books and records and sample testing. The FSA has for the last years emphasised supervising the internal control and procedures of financial institutions subject to its supervision to ensure there is a sufficient risk management in place, rather than taking samples. If the FI does not comply with this disclosure duty, the duty may be imposed on the individual officers/employees of the FI. (As a rule, the FI will be notified in such cases.) Consequently, the FI's auditor may be ordered to disclose information that appears in the annual accounts, account forms, staff pay summaries and deduction sheets, auditor's records and auditor's report.

410. Article 9 (3) also authorises the appointment of a special expert and undertake specific supervision for a period of 4 weeks at a time. The expert shall be provided with working facilities on the premises of the regulated entity and given access to all requested accounts, minutes, documents, and other data possessed by the regulated entity. The expert shall be entitled to attend meetings of the Board as an observer with the right to speak. Article 9 (4) further authorises the FSA to conduct special on-site investigations and seize any material in accordance with the Code of Criminal Procedure, "provided that there "cogent reasons to suspect that the regulated entity has violated laws or regulations applicable to its activities, or if there is reason to believe that inspections or actions by the FSA will not otherwise achieve their objective."

Powers of enforcement and sanction

411. Criminal sanctions may apply to legal persons for violations of the MLA. A range of administrative sanctions may also apply be applied by the FSA, which include rectification orders, daily fines, and more serious financial penalties. While there is a range of sanctions available, the range is not sufficiently broad. There are no administrative penalties which can be imposed against directors and controlling owners of financial institutions directly for AML/CFT breaches, only indirectly by not meeting fit and proper criteria. Available sanctions for other senior management appear more limited. The available sanctions do not include the possibility to directly bar persons from the sector, unless they are convicted of an offence. In addition, there is not the general possibility to restrict or revoke a license for AML/CFT violations.

Recommendation 17

Criminal Sanctions

412. Criminal sanctions may apply to legal persons for certain violations of the MLA 1999. It is not clear in the MLA whether sanctions can be applied to the directors and senior management of the FI that was responsible for the violation by the FI. According to Article 14 of the MLA, criminal sanctions (fines) are available for violations of Articles 3, and 5-10 of the Act. These provisions refer to CDD,

record keeping, monitoring and reporting of suspicious transactions, "tipping off", and the requirements for internal controls. It does not cover article 11, which refers to the requirement to give special attention to countries which do not have adequate AML measures. Article 14 further specifies that fines can apply to legal entities, irrespective of guilt having been established on the part of the persons in charge or its staff members. If a person in charge of a legal entity or its staff member has become guilty of a violation of this Act, the legal entity may also be fined.

413. Criminal sanctions are found in the revised AML/CFT Act of 22 June 2006; however, the provisions appear more restrictive than in the previous MLA. Article 27 specifies that penalties may be imposed on "persons under the obligation to report"—i.e., covered entities (financial institutions) and individuals (lawyers, accountants, real estate dealers, etc.). Therefore, under the new legislation, criminal sanctions would not be available for directors or senior management of financial institutions. Penalties may be applied to persons obliged to report for failure to comply, either by intent or gross negligence, with CDD, record keeping, STR and tipping off, and internal control requirements. The legal person may also be fined irrespective of whether the guilt of its responsible manager or employee has been established. If the responsible manager of a legal entity or its staff member has infringed this Act, the legal entity may also be fined if the infringement was for its benefit.

414. The laws do not specify the amounts of fines; these would be determined by the courts. However, there are concerns about the effectiveness of these criminal sanctions since no such sanction has ever been applied for a violation of any version of the money laundering act (which date back to 1993).

Administrative sanctions

415. Administrative sanctions that the FSA may impose are contained in Articles 10-12 of the Act No. 87/1998 on Official Supervision of Financial Activities. Sanctions include rectification orders, daily fines, more serious financial penalties, and referral to the police.

416. If an inspection carried out by the FSA reveals that entities subject to supervision do not comply with the law or other regulations governing their activities, the FSA can insist on corrective action being taken within a certain time limit, pursuant Article 10. The FSA can also remark upon any aspect of the position or operation of an entity subject to supervision which it considers in other respects unsound and inconsistent with normal business practices and can demand that corrective action be taken within a certain time limit. When a situation arises, the FSA may call a board or executive meeting of the entity concerned to discuss its remarks and demands, and discuss corrective action. A representative of the FSA may chair the meeting and enjoy the right of speech and make proposals.

417. If the entity subject to supervision does not provide requested information or heed requests for corrective action within a certain time limit, the FSA may resort to sanctions in the form of daily fines, pursuant Article 11. These fines shall be collected until the party has complied with the demands of the FSA. The daily fines can amount to ISK 10,000 – ISK 1,000,000 and can be determined as a proportion of certain figures in the operations of the party. When determining the amount of daily fines, consideration shall be made for the nature of the negligence or violation, and the financial strength of the party subject to supervision. Decisions regarding daily fines shall be made by the board of the FSA.

418. Article 11 further authorises the FSA to impose financial penalties upon a party in violation of previous decisions of the FSA (such as rectification orders). The penalties can be between ISK 10,000 and ISK 2,000,000. When determining the amount of the liquidated damages, consideration shall be made for the seriousness of the violation, and the financial strength of the party subject to supervision. Decisions regarding liquidated damages shall be made by the board of the FSA.

419. In the event of a serious infringement where the entity subject to supervision has in the opinion of the FSA committed a criminal offence, the FSA is obliged to notify the State Police Commissioner, pursuant to Article 12.

420. The FSA can apply certain administrative sanctions to controlling owners, CEOs, and directors, where they do not meet the "fit and proper" criteria. With regard to controlling owners, the FSA can restrict the powers of owners of qualifying holding in financial institutions, by withdrawing their voting rights (See paragraph 428.) As described in further detail below, the main criteria for fit and properness for board members and CEOs is that they may not conduct themselves "in any manner which would give cause to expect them to abuse their position or injure the undertaking." According to amendments to the Act on Official Supervision on Financial Operations approved in June 2006, the FSA now has the power to dismiss individual board members and directors (but not other senior management), if they are not considered to be fit and proper. Iceland authorities therefore indicate that these powers could be applied for AML/CFT breaches; however, this power is new and it is not clear how effectively it could be applied for AML/CFT issues.

421. While there is a range of sanctions available, the range is not sufficiently broad. There are no administrative penalties which can be imposed against directors and controlling owners of financial institutions directly for AML/CFT breaches, only indirectly by not meeting fit and proper criteria. Available sanctions for other senior management appear more limited. The available sanctions do not include the possibility to directly bar persons from the sector, unless they are convicted of an offence. In addition, there is not the general possibility to restrict or revoke a license for AML/CFT violations. The grounds for revoking a license are contained in Article 9 on Act 161/2002 on Financial Undertakings, which include if the shareholders, members of the board and management do not satisfy the qualification requirements. These qualification requirements include for example, the financial position of the applicant and that he/she not be convicted of an offence. Icelandic authorities have explained that, in extreme cases, repeated non-compliance could entail that the FSA considers a member of the board or the CEO does not adequately meet the qualification requirements; if such a board member would not comply with the FSA's request to resign, the FSA could consider revoking the license of the institution in question. This power has not been used, and the evaluation team had concerns regarding how effectively this could be applied in practice.

422. The above mentioned powers of the FSA have rarely been used due to non compliance with the MLA—only a few cases of insisting on corrective action.

Markey entry – Recommendation 23 (Criteria 23.3, 23.3.1, 23.5, 23.7)

Licensing

423. The FSA licenses the various entities it supervises. According to Article 3 of Act 161/2002 on Financial undertakings, the following activities must obtain an operating license from the FSA:

a. receipt of repayable funds from the public, in the form of:
    1. deposits,
    2. debt certificates.
b. granting of credit which is financed by repayable funds from the public;
c. asset leasing, if such activity forms the principal activity of an undertaking. Asset leasing shall mean the leasing of movable assets or real estate where the lessor sells the lessee the leased property for the leasing fee agreed upon for a specified minimum rental period;
d. the issuing and handling of payment cards;
e. the issuing and handling of electronic money;
f. trade and services in financial instruments, in accordance with the Act on Securities Transactions;
    1. reception and transmission of instructions from customers concerning one or more financial instruments and the execution of such instructions for the account of a third party;
    2. asset management, cf. the Act on Securities Transactions;
    3. underwriting in connection with the issue of one or more financial instruments or the marketing of such an issue;
    4. administration of a securities offer;

g. operation of Undertakings for Collective Investment in Transferable Securities (UCITS).

424. Parties who propose to acquire a qualifying holding in a financial undertaking must seek the approval of the FSA in advance (Article 41). The approval of the FSA must, furthermore, be sought when an individual or legal entity increases his holding to such an extent that his direct or indirect share in its share capital, guarantee capital or voting rights exceeds 20%, 25%, 33%, or 50%, or comprises such a large portion that the financial undertaking can be regarded as its subsidiary company. A "qualifying holding" means a direct or indirect holding in an undertaking which represents 10% or more of its share capital, guarantee capital or voting rights, or other holding which enables the exercise of a significant influence on the management of the company concerned.

425. Parties intending on acquiring a holding in a financial undertaking, must make written application to the FSA containing information such as:

- the size of the holding or voting rights in which the applicant intends to invest,
- plans for changes in the pursuits of the financial undertaking;
- financing of the investment;
- the financial position of the applicant;
- the proposed commercial relationship of the applicant with the financial undertaking;
- the applicant's experience of financial activities;
- the ownership, board membership, or other participation of the applicant in the activities of a legal entity;
- any punishment to which the applicant has been sentenced and whether he/she is the object of a criminal investigation;
- close links of the applicant to other legal entities.

426. If an applicant is a legal entity the above list of items shall apply to the legal entity itself, the members of its board, its managing director and individuals and legal entities owning qualifying holdings in the legal entity. Information shall furthermore be given on the legal entity's auditor. The FSA may also request other information that is significance for assessment of the eligibility of owners of qualifying interests.

427. The FSA assesses whether an applicant is eligible to own the holding, having regard to the sound and prudent operation of a financial undertaking. In assessing the eligibility of an applicant, the FSA regards for instance, the following factors (according to article 42 of the Act):

- the financial position of the applicant and parties with which he/she has close links;
- the knowledge and experience of the applicant;
- whether such a holding by the applicant creates a risk of conflicts of interest in the financial market;
- the size of the holding or voting rights in which the applicant intends to invest;
- whether such a holding by the applicant could be expected to impede supervision of the financial undertaking concerned. The FSA shall in its assessment consider earlier dealings of the applicant with the FSA and whether close links between the applicant and individuals or legal entities could, in the estimation of the FSA, obstruct its normal supervision work, and whether laws or rules to which the applicant is subject to, can obstruct normal supervision;
- whether the applicant has provided the FSA with the required information together with supporting documentation and this information has proved to be correct;
- any punishment to which the applicant has been sentenced and whether he/she is the object of a criminal investigation.

428. In the case that a person or a legal entity is considered non fit to acquire a qualifying holding in a financial undertaking, the FSA may withdraw the voting right and order the relevant owner to reduce it's holding in the institution in question.

429. Similar rules apply to insurance companies, according to the Act on Insurance Activities No. 60/1994. Applications must be sent to the FSA (Article 21) approved by the FSA (Article 25). In assessing the application, the FSA may refuse the application if it is of the opinion that those holding qualified holdings in the company are deemed unable to adequately ensure sound and prudent management (Article 25.) The approval of the FSA must also be sought when an individual or legal entity increases his qualified (i.e., 10%) holding to such an extent that his direct or indirect share in its share capital, guarantee capital or voting rights exceeds 20%, 25%, 33% or 50%, or comprises such a large portion that the financial undertaking can be regarded as its subsidiary company (Article 39). The FSA may deny the request if it deems the party concerned is not qualified to do so with a view to ensure sound the and prudent operations of the company. Similar rules apply to assessing the qualification of shareholders of insurance undertakings (Article 39 of the Act on Insurance Activities).

Fit and proper tests criteria for directors and senior management

430. The fit and proper criteria for financial undertakings are provided in Article 52 of the Act on financial undertakings which reads as follows:

> "Eligibility of board members and managing director:
>
> Members of the board and the managing director of a financial undertaking must be legally competent. They may not, during the last five years have been declared bankrupt in connection with business operations, nor convicted of a punishable offence under the Criminal Code, this Act or Acts on Public Limited Companies, Private Limited Companies, accounting, financial statements, bankruptcy or taxation, nor under special legislation applicable to parties subject to public supervision of financial activities."

431. In addition to the above requirements, board members and the managing director must possess sufficient knowledge and experience to be able to fulfil their position in a satisfactory manner. They may not have conducted themselves in any manner which would give cause to expect them to abuse their position or injure the undertaking."

432. Similar rules apply for insurance companies and brokers and pension funds in the Act on Insurance Activities No. 60/1994.

433. The FSA has recently adopted a new procedure regarding fit and proper assessment of board members and CEOs. According to this procedure, all new board members and CEOs must answer and sign a questionnaire in connection with the assessment and to provide evidence in the form of certified documentation for their compliance with the above mentioned article. In addition all new CEOs must be tested with the FSA, as to their knowledge of the rules and legislation (including the MLA 1999) applicable to the financial sector.

434. The requirements for fitness and properness of directors of institutions subject to the Core Principles are appear adequate. However, while fit and proper tests apply for directors and board members, they do not apply to other senior management.

Money exchange and transfer services

435. According to Article 8 in Act on Foreign Exchange, natural and legal persons providing currency changing service have licensed by the Central Bank. Article 8 reads as follows:

> "The Central Bank of Iceland may act as intermediary in foreign exchange transactions and buy and sell foreign currency. Other parties are prohibited from acting as intermediaries in foreign exchange transactions in Iceland unless authorised to do so by statute or by the provisions of international agreements to which Iceland is party, or licensed to do so by the Central Bank.

436. There is no general requirement for money or value transfer services to be licensed or registered; however, currently only Western Union and MoneyGram provide known transfer services, and these are conducted through an Icelandic bank and Forex, respectively.

Ongoing supervision and monitoring – R.23 (Criteria 23.4, 23.6, 23.7)

437. For financial institutions subject to the Core Principles, the regulatory and supervisory measures that apply for prudential purposes and which are also relevant to money laundering, generally apply in a similar manner for anti-money laundering and terrorist financing purposes. This includes requirements for i) licensing and structure; (ii) risk management processes to identify, measure, monitor and control material risks; (iii) ongoing supervision and (iv) global consolidated supervision where required by the Core Principles.

438. Before conducting an on-site inspection, the FSA sends a standard notice of inspection to the financial institution requesting it to supply the FSA with its internal AML/CFT routines. Although the FSA is not legally required to give prior notice that it is going to be conducting an on-site inspection, it seldom conducts an inspection of a bank, finance company, insurance company, insurance broker, investment firm or management company for securities funds without doing so. The FSA shall examine accounts and other records of the FIs, and can carry out any investigations of their position and activity as it deems necessary.

439. At on-site inspections, it is normal procedure to not make spot checks of how institutions carry out the mandatory customer identification checks.

Money exchange and remittance businesses

440. Although money exchange and remittance businesses that operate outside of banks are subject to the provisions of the revised Money Laundering Act, these entities are not subject to any system for monitoring and ensuring compliance with the AML/CFT requirements.

Recommendation 32[24] (Statistics)

441. No specific AML inspections have been conducted. The FSA indicated that it conducted 50 on-site inspections from July 2003—June 2004, and 41 on-site inspections from July 2004 to June 2005. There was no break down in terms of which financial institutions were covered or which ones also involved AML issues. Following an inspection, the approach of the FSA is to write a report of its findings which is sent to the company's board of directors. The board, in turn, is asked to comment on the report and to forward the report to the external auditor and control committee for their comments. The FSA reviews all of the comments and then concludes the inspection by writing final remarks that are submitted to the board of directors. The FSA reports that always, after allowing the reporting entity a reasonable period of time to implement improved routines and measures, it will follow up the finding from an inspection. Sanctions for AML/CFT breaches have not yet been effectively applied. On only two occasions, the FSA has issued formal warnings. The limited findings – and number of warnings – indicates that the focus on AML/CTF has been inadequate.

Guidelines – R.25 (Guidance for financial institutions other than on STRs)

442. According to paragraph 2 of Article 8 of the Act on Official Supervision on Financial Operations, the FSA has the power to issue general guidelines. The FSA has however, not issued any guidelines regarding ML/FT issues. The FSA is now working on guidelines for the financial sector, now that the new AML/CFT Act 2006 has been adopted.

3.10.2 Recommendations and Comments

[24] See Section 7.1 for the compliance rating for this Recommendation.

443. *Recommendation 17:* The range of administrative sanctions should be broadened for directors and senior management of financial institutions, to include the more direct possibility to bar persons from the sector, to be able to more broadly replace or restrict the powers of managers, directors, or controlling owners for AML/CFT breaches. In addition, there should be the possibility to restrict or revoke a license for AML/CFT violations.

444. *Recommendation 23:* In general, the FSA should give more attention to AML/CFT matters. The FSA is already taking steps to do this and have already hired an additional staff to focus on AML/CFT issues. In addition, while fit and proper tests apply for directors and board members, they should also apply to other senior management.

445. There should be a general requirement for money or value transfer services to be licensed or registered. Money value transfer services and money exchange services that operate outside of banks should also be made subject to a system for monitoring and ensuring compliance with the AML/CFT requirements.

446. The FSA indicated that its on-site inspection agenda used for inspection visits was revised in April 2006 to include questions relating to AML/CFT. Iceland should now ensure that AML/CFT assessments of Reporting FIs occur more regularly, particularly in high risk institutions.

447. *Recommendation 25:* The FSA and other authorities should complete and issue comprehensive AML/CFT guidance for the whole private sector covered by the obligations.

448. *Recommendation 29:* Icelandic authorities should give adequate powers to a designated authority to adequately supervise unlicensed financial institutions such as foreign exchange companies or foreign remittance dealers that may operate outside of banks. As indicated under Recommendation 17, the range of sanctions should also be broadened.

449. *Recommendation 30:* The FSA should be given additional resources to be allocated for AML/CFT supervision. The FSA should consider creating a well staffed stand alone AML/CFT unit or at least a team of examiners specialising in AML/CFT measures that check FIs compliance with AML/CFT on an on-going basis for all supervised entities.

3.10.3 Compliance with Recommendations 23, 29, 17, & 25

	Rating	Summary of factors relevant to s.3.10 underlying overall rating
R.17	**PC**	• It is not clear in the MLA 1999 whether sanctions can be applied to the directors and senior management of the FI that was responsible for the violation by the FI. Under AML/CFT Act 2006, criminal sanctions would not be available for directors or senior management of financial institutions. • There are concerns about the effectiveness of these criminal sanctions since no such sanction has ever been applied for a violation of any version of the money laundering act (dating back to 1993). • The range of administrative sanctions is not sufficiently broad. There are no administrative penalties which can be imposed against directors and controlling owners of financial institutions directly for AML/CFT breaches, only indirectly by not meeting fit and proper criteria. Sanctions for other senior managers appear more limited. The available sanctions do not include the possibility to directly bar persons from the sector, unless they are convicted of an offence. There is not the general possibility to restrict or revoke a license for AML/CFT violations. • Administrative sanctions for AML/CFT have not yet been effectively applied.

R.23	**PC**	• While fit and proper tests apply for directors and board members, they do not apply to other senior management. • There is no general requirement for money or value transfer services to be licensed or registered. • Money value transfer services and money exchange services are not subject to any system for monitoring and ensuring compliance with the AML/CFT requirements. • At on-site inspections, it is normal procedure to not make spot checks of how institutions carry out the mandatory customer identification checks. • At the time of the on-site visit, financial institutions were not subject to adequate supervision of compliance with CFT requirements. • There are concerns about how effectively the financial sector has been supervised regarding AML/CFT; while the FSA indicated that AML/CFT assessments of financial institutions are part of regular visits, the very limited findings – and number of warnings – indicates that the focus on AML/CTF has been inadequate.
R.25	**NC**	• The FSA has not issued any guidelines regarding ML/FT issues.
R.29	**LC**	• No supervisory powers exist for financial institutions not under FSA's supervision, such as foreign exchange companies or foreign remittance dealers that may operate outside of banks. • While there is a range of sanctions available, the range is not sufficiently broad. There are no administrative penalties which can be imposed against directors and controlling owners of financial institutions directly for AML/CFT breaches, only indirectly by not meeting fit and proper criteria. Available sanctions for other senior management appear more limited. The available sanctions do not include the possibility to directly bar persons from the sector, unless they are convicted of an offence. In addition, there is not the general possibility to restrict or revoke a license for AML/CFT violations.

3.11 Money or value transfer services (SR.VI)

3.11.1 Description and Analysis (summary)

450. Icelandic authorities indicate that all money transfer services operate out of banks. Western Union operates through various branches of an Icelandic bank. MoneyGram offers services through Forex, which operates under a foreign banking license from Sweden. Authorities were unaware of any alternative remittance system(s) that might be operating in Iceland. Nevertheless, the evaluation team could not conclude definitively that no alternative remittance operators exist.

451. There are currently no requirements to license or register natural and legal persons that perform money or value transfer services (MVT operators). There is no authority that maintains a list of names and addresses of such operators. MVT operators are not required to maintain a current list of their agents which must be made available to the designated competent authorities.

452. MVT operators are covered under the old and revised Money Laundering Acts and hence are responsible for implementing the various AML/CFT obligations that apply to other financial institutions covered by the act, although as noted above there are deficiencies regarding the extent of CDD and other AML/CFT requirements in general. The evaluation team also had concerns regarding supervision, since there is no mechanism for monitoring and ensuring compliance with the FATF Recommendations.

453. Legally, sanctions are available for failure to comply with AML/CFT provisions; however, there is no mechanism to discover deficiencies and apply sanctions and hence sanctions could not be applied. Sanctions for failure to comply with the other obligations of SR VI would not be available.

3.11.2 Recommendations and Comments

454. Iceland should implement the measures in SR.VI. Most importantly, Iceland should require all money or value transfer services (MVT operators) to be licensed or registered, maintain a list of such operators, and adopt a mechanism to adequately monitor and ensure compliance with the FATF Recommendations.

3.11.3 Compliance with Special Recommendation VI

	Rating	Summary of factors underlying rating
SR.VI	**NC**	• There are currently no requirements to license or register natural and legal persons that perform money or value transfer services (MVT operators). • There is no authority that maintains a list of names and addresses of such operators. • The deficiencies regarding the extent of CDD and other AML/CFT requirements apply also to MVT operators. • MVT operators are not required to maintain a current list of their agents which must be made available to the designated competent authorities. • The evaluation team had serious concerns regarding supervision, since there is no mechanism for monitoring and ensuring compliance, with the FATF Recommendations, including the practical inability to apply sanctions for AML/CFT deficiencies. • Sanctions for failure to comply with the other obligations of SR VI would not be available.

4. Preventive Measures – Designated Non-Financial Businesses and Professions

Overview of the scope of coverage of AML/CFT preventive measures

455. The MLA 1999 applied to activities by individuals and legal entities authorised to provide services to the public in Iceland or abroad. In addition to the various financial institutions that are covered by these activities, certain FATF-designated non-financial businesses and professions were also covered, namely:

- Real estate sales;
- Trading of precious metals and gems when a particular trading activity exceeds the amount specified in article 3(2) [i.e., EUR 15,000] or in cases where the amount is lower than that specified in article 3(2) and the trading is carried out in a number of inter-related trading activities.

456. Casino's, including Internet casinos, are not allowed in Iceland and therefore not covered by the MLA 1999.

457. The AML/CFT Act 2006, which came into force on 2 June 2006, covers a broader scope of DNFBPs in items (f)-(l) in Article 2 of the new Act:

f. Attorneys and other legal professionals in the following instances:
   i. When they manage or represent their clients in any form of financial or real estate dealings;
   ii. When they assist in the organisation or conduct of business for their clients with respect to the purchase and sale of real estate or enterprises, manage cash, securities or other assets of their clients, open or manage commercial bank accounts, savings bank accounts or securities accounts, arrange financing needed for the establishment, operation or management of enterprises or establish, operate or manage custody accounts, enterprises and similar entities;
g. Auditors;
h. Other natural or legal persons when, in the course of their work, they perform the same services as those listed in Sub-section (f), e.g. tax consultants or other external consultants;
i. Brokers of real estate, enterprises or vessels;
j. Natural or legal persons engaged, by way of business, in trading in goods for payment in cash in the amount of EUR 15,000 or more, based on the officially posted exchange rate at any time, whether the transaction is executed in a single operation or in several operations which appear to be linked;
k. Trust and company service providers, as defined in Article 3;[25]
l. Legal or natural persons who have been granted an operating licence on the basis of the Lotteries Act, and parties permitted under special legislation to conduct fund-raising activities or lotteries where prizes are paid out in cash;

[25] "Trust and company service providers" (as defined in Article 3): Natural or legal persons providing, by way of business, the following services:
a) Forming companies or other legal persons;
b) Acting as, or arranging for another person to act as, director or executive of an undertaking, as partner in a company or serve in a comparable position in another form of legal person.
c) Providing a domicile or other registered address which is used in a similar manner to contact the undertaking, or other related services;
d) Acting as, or arranging for another person to act as, a trustee of a trust or a similar legal arrangement;
e) Acting as, or arranging for another person to act as, a nominee shareholder for another person other than a company listed on a regulated market.

4.1 Customer due diligence and record-keeping (R.12)

(applying R.5, 6, and 8 to 11)

Applying Recommendation 5

458. *Casinos:* Casinos are not allowed in Iceland and gambling in general is prohibited according to the General Penal Code. Internet casinos do fall under this prohibition as well, but there is a basic disagreement in Iceland about whether Iceland has the capacity to prevent internet casinos from offering services which might be accessible in Iceland. It seems that there is no check on the activities of internet casinos, even if they operate from Iceland.

459. *Real estate agents* are formally covered by the MLA 1999, when they are involved in transactions for a client concerning the buying and selling of real estate. They have to identify both parties according to the MLA (for the measures to be taken, see section 3.2.1). Similar coverage is contained for real estate agents in the revised MLA, where they are subject to the range of CDD requirements as for financial institutions.

460. *Dealers in precious metals and stones* are covered by way of the AML/CFT Act 2006, article 2 (j), which covers all natural or legal persons engaged, by way of business, in trading in goods for payment in cash in the amount of EUR 15,000 or more.

461. *Lawyers, notaries, other independent legal professionals and accountants* are covered under the new act, Article 2 (f) and (g). However, it should be noted that the act refers to licensed "auditors" and therefore might not cover the full scope of individuals and entities carrying out accounting activities in Iceland. Iceland maintains that only licensed auditors prepare for or carry out transactions for their clients in activities in the five points mentioned in recommendation 12, point d, i.e. buying and selling of real estate; managing of clients money, securities or other assets etc. In addition, when conducting the activities covered in the Recommendation 12, they would also be covered under Article 2 (h) of the law above (See paragraph 457 above). Notaries exist but only perform formalistic functions; they are not authorised to perform the kinds of activities covered by the FATF Recommendations.

462. *Trust and company service providers* are covered through Article 2 (k) of the AML/CFT Act 2006, in the circumstances required by FATF Recommendation 12.

463. While the new legislation adequately covers the scope and situations required by the DNFBPs, the application of Recommendation 5 is lowered by the same deficiencies as applying Recommendation 5 for financial institutions. (See discussion under Recommendation 5.) Finally, the newer provisions in the MLA 2006 have not yet been effectively implemented.

464. In addition, it appears that real estate agents are not adequately implementing the AML requirements that have been in place since 1999. It became clear that real estate agents never identify natural persons having an Icelandic nationality, but they do identify a foreigner by his passport. In the case of foreign legal persons, it is practice to ask for some sort of paper from their local Chamber of Commerce. These identification rules are seen as being part of the Ethical rules, instead of following the MLA 1999 requirements. There is never really a check on the background of the client, while it is acknowledged that in the current booming real estate market it has became more difficult to oversee from where the money to purchase real estate comes.

Applying Recommendation 6

465. Recommendation 6 is not implemented in the MLA 1999. However, DNFBPs have obligations for politically exposed persons (PEP) under Article 12 of the new AML/CFT Act 2006. They are to:

- Determine whether the customer is a politically exposed person, which includes natural persons who are or have been entrusted with prominent public functions and immediate family members, or persons known to be close associates, of such persons;
- Obtain senior management approval before entering into business transactions with such customers;
- Take appropriate measures to verify the source of funds that are involved in the business relationship or transaction;
- Conduct regular monitoring of the business relationship.

466. The scope of requirements for PEPs is generally broad. However, there is not a requirement to obtain senior management approval to continue the business relationship, where a customer has already been accepted and the customer or beneficial owner is subsequently found to be, or subsequently becomes a PEP. In addition, none of the PEP requirements enter into force until 1 January 2007.

Applying Recommendations 8

467. Real estate agents and dealers in precious metals and stones, and lawyers as far as their activities fall under the scope of the MLA (see above), are covered by the same obligations as financial institutions regarding "distant selling" (see section 3.2.1 (R 8), but these DNFBPs were not adequately aware of their existing AML requirements, which indicates that they were not being effectively implemented.

468. The broader scope of DNFBPs have obligations regarding "distant selling" under article 10 of the AML/CFT Act 2006. It requires that where the customer is not present to prove his/her identity, additional information should be obtained about the customers if necessary, and it should be required that the first payment should be made in the name of the customer and through an account established by the customer in a credit institution. In addition, the internal rules of the DNFBP must contain more detailed provisions, where appropriate, concerning business using telecommunications and the preservation of date concerning such businesses. Article 14 of the Act also requires DNFBPs to show special caution in the case of products or transactions that might favour anonymity, and to take measures, if needed, to prevent the use of such businesses for money laundering or terrorist financing purposes.

469. While these provisions generally cover the requirement to have polices or procedures in place to address risks associated with non-face to face business or transactions at the start of a business relationship and during on-going due diligence. There is not a specific requirement to have measures in place as needed to prevent the misuse of other technological developments in money laundering or terrorist financing schemes, although the general requirement to take measures as needed to prevent the use of products or transactions that might favour anonymity for ML or FT partly covers this.

Applying Recommendation 9

470. At the time of the on-site visit, the private sector acknowledged the possibility to have a third party identifying the customer for financial institutions if this was practically impossible to be performed by the financial institution. It appeared that this was also possible for DNFBPs. Article 16 of the AML/CFT Act 2006 now introduces provisions on the use of third parties and introduced business. This provision states that a reporting entity is not required to conduct CDD if corresponding due diligence data is "revealed" through a financial institution which has been granted an operating licence in Iceland or in the EEA. The same applies for information revealed through a financial institution from outside the EEA which is subject to similar requirements as those from the new MLA. Iceland authorities have clarified that the "revealed" means that the information must be obtained from the foreign financial institution before the Icelandic institution may accept the introduced business.

471. While these measures are generally broad, DNFBPs relying on a third party are not required to take adequate steps to satisfy themselves that copies of identification data and other relevant documentation relating to CDD requirements will be made available from the third party upon request without delay; or that the DNFBP be satisfied that the third party is regulated and supervised and has measures in place to comply with the CDD requirements.

Applying Recommendation 10

472. Under the MLA 1999, real estate agents and dealers in precious metals and stones, fell under the scope of the MLA (see above) and were covered by the same obligations as financial institutions (see section 3.5.1 (R 10)). It is mentioned by DNFBPs that record keeping is not always required in line with Recommendation 10, but it followed more from 'good business practices' that they have to keep records in general.

473. Under the AML/CFT Act 2006, the broader scope of DNFBPs has the same obligations to maintain CDD records according to Article 5, as financial institutions. Article 23 further stipulates that parties must maintain individual customer transaction records for five years, and have systems in place which enable them to respond promptly to queries from the police or other competent authorities.

Applying Recommendation 11

474. Real estate agents and dealers in precious metals and stones were covered by the same obligations as financial institutions (see section 3.6.1 (R 11)), as contained in the MLA 1999. However, they were not covered by the AML Regulation 1994. Article 7 of the AML Regulation fulfils the main obligations of Recommendation 11—it specifically requires financial institutions to examine any transaction which is considered unusual, extensive or complicated in view of the customer's normal business activities. Furthermore, it the financial institutions must examine all transactions that appear to have no financial or legal purpose.) Since the Regulation 1994 did not apply to DNFBPs, they did not have general requirements to monitor for unusual transactions. Above all there was no awareness in these sectors of any monitoring obligation.

475. The wider scope of DNFBPs now has a broader obligation under Article 17 of the AML/CFT Act 2006. It indicates that all persons under the obligation to report "are required to have any transactions suspected of being traceable to money laundering or terrorist financing carefully examined and notify of the police of any transactions which are considered to have such links. This applies in particular to transactions which are unusual, large or complex in the light of the normal business of the customer, or which have no apparent economic or visible lawful purpose." Article 23 (2) further specifies that DNFBPs must prepare written reports on all suspicious and unusual records that occur in the course of effecting transactions in their business activities and keep these records for five years.

476. While generally broad, the provisions have just begun applying to the full range of DNFBPs and they are not yet effectively implemented.

4.1.2 Recommendations and Comments

477. Iceland should adopt and fully implement the full range of CDD measures, as discussed in section 3.2 and 3.3 of this report, so as to also apply to DNFBPs. Iceland should fully implement the new measures that apply to DNFBPs.

4.1.3 Compliance with Recommendation 12

	Rating	Summary of factors relevant to s.4.1 underlying overall rating
R.12	**PC**	• Similar deficiencies for CDD that apply to financial institutions (See ratings boxes for Recommendation 5) also apply to DNFBPs. • At the time of the on-site visit, real estate agents and traders in precious metals and gems did not appear adequately aware of existing AML requirements. • There are no requirements for PEPs in force—the requirements in the new law will enter into force until 1 January 2007. There will not be a requirement to obtain senior management approval to continue the business

		relationship, where a customer has already been accepted and the customer or beneficial owner is subsequently found to be, or subsequently becomes a PEP. • The requirement to have policies in place or take such measures as may be needed to prevent the misuse of technological developments in ML or TF schemes is only partially covered. The requirement to acquire additional information on the customer "when needed" is an open a provision which needs further regulation or guidelines to make it effective. • Certain rules for reliance on 3rd party introducers are unenforceable. For DNFBPs relying on a third party there is not a general requirement that the DNFBP be satisfied that the third party is regulated and supervised and has measures in place to comply with the CDD requirements. • The provisions have just begun applying to the full range of DNFBPs and have not yet been put effectively into practice.

4.2 Monitoring transactions and other issues (R.16)

(applying R.13 to 15 & 21)

4.2.1 Description and Analysis

Applying Recommendation 13

478. Real estate agents, dealers in precious metals and gems were obliged to report all suspicious transactions to the FIU in the same way as financial institutions, according to Art. 7 of the MLA 1999 (see Section 3.7). However, these sectors did not appear adequately aware of these obligations and have not filed any STRs.

479. Dealers in precious metals and stones were also required to comply with the requirement set out in Recommendation 13 when the trading of precious metals and gems exceeds the amount of EUR 15,000 or in cases where the amount is lower than that and the trading is carried out in a number of inter-related trading activities.

480. The broader scope of DNFBPs are now required to report suspicious transactions to the police, according to 17 of the AML/CFT Act 2006, in the range of circumstances set out in Recommendation 16. This includes transactions that could be related to money laundering or terrorist financing. However, as with the obligation for financial institutions, the scope of the reporting could be limited by the fact that insider trading, market manipulation, and arms trafficking are not predicate offences for money laundering in Iceland.

481. It should be noted that Article 17 (3) of the new legislation indicates that the reporting obligation shall not apply to information obtained by legal professionals in the course of ascertaining the legal position of their client, including advice on instituting or avoiding proceedings, or information obtained before, during or after the conclusion of judicial proceedings, if the information is directly related to such proceedings. The same applies to information obtained by parties pursuant to sub-sections (g) to (i) in Paragraph 1 of Article 2 (i.e., auditors, tax consultants, real estate brokers) when they are providing expert advice to a legal professional before, during or after the conclusion of judicial proceedings.

482. With regard to lawyers, it should also be noted that the Act on Professional Lawyers No. 77/1999, article 22 indicates that "a lawyer has the duty of maintaining silence with respect to any matter confided to him in the course of his functions. A lawyer's employee is also under the duty of maintaining silence with respect to such confidential matters he may become aware of in his work." There is a concern that this broad secrecy requirement for lawyers might conflict with the obligation to report, despite the exemption, as provided in Article 21 of the MLA 2006, from professional secrecy when reporting. The private sector also asked that the differences between the two laws be clarified.

Applying Recommendation 14

483. Article 20 of the AML/CFT Act 2006 generally prohibits reporting parties to disclose to the customer or other third person that information has been provided to police subject to STR provisions. However, Article 20 does indicate that attorneys and auditors who advise their customers to refrain from participating in illegal activities are not regarded as having violated the prohibition on disclosure.

484. Article 21 provides protection from criminal or civil damages, as well as an exemption from professional secrecy, when reporting to the police has been made in good faith.

Applying Recommendation 15

485. See section 3.8.1. Article 23 of the AML/CFT Act 2006 requires DNFBPs to establish written internal rules and maintain internal controls designed to prevent their business activities from being used for money laundering and terrorist financing. However, there are not detailed requirements regarding what the internal rules should cover. (See paragraph 367.) To this end they shall ensure, *inter alia*, that their employees receive special training. They must also have systems in place to respond promptly to queries from the police or other competent authorities.

486. They are also required, on the appointment of staff, to establish specific rules on the checks to be performed of the record of an applicant for positions with the undertakings and in what instances.

487. Article 22 of the AML/CFT Act 2006 requires DNFBPs to nominate a specific person the managerial rank to be responsible for notification and ensuring coordinated practices supporting the implementation of the Act. However, it is not required that the compliance officer and other appropriate staff have timely access to CDD, transaction, and other relevant information. There is no requirement to maintain an adequately resourced and independent audit function to test compliance (including sample testing) with AML/CFT procedures, policies and controls. Iceland authorities note that, in accordance with general principles and best practice, functions of internal audit departments of financial undertakings should cover all the activities of the institutions and their obligations in accordance with the legislation applicable to their operations (including AML/CFT issues); however, this is not laid out in law.

488. In addition, the training requirements do not specify that the training programs be on-going so as to be kept informed of new developments, or specify that they should cover ML and FT techniques, methods and trends. (See paragraph 372.)

Applying Recommendation 21

489. Article 26(2) of the AML/CFT Act 2006 requires DNFBPs to pay special attention to those states or regions which do not comply with international recommendations and rules on actions to combat money laundering. The FSA also informs the financial sector about the NCCT list via a circular letter and publication of this letter on the website. (See also section 3.6.1.)

490. Real estate agents, lawyers and dealers in precious metals and gems were covered by similar provisions in the MLA 1999, but at the time of the on-site visit they were not yet adequately aware of this obligation. Although DNFBPs in Iceland are now covered under the new legislation, they would not receive the notices and instructions issued by the FSA if there is a need for special caution in transactions with a state or region. There is no other authority issuing such notices and instructions. However, subsequent to the on-site visit, Icelandic authorities indicated that consideration was being given to which agency will monitor the DNFBP sectors for AML/CFT compliance.

491. There are, however, no provisions dealing with the possibility to apply appropriate counter-measures where a country continues not to apply or insufficiently applies the Recommendations, nor seems there to be any action undertaken by Icelandic authorities to employ such counter-measures.

4.2.2 Recommendations and Comments

492. Iceland should undertake the following actions to fully implement Recommendation 16:

a. Overall, the measures in the new legislation should be fully and effectively implemented.
b. DNFBPs should be made fully aware of their reporting obligations under the new legislation.
c. DNFBPs should be made aware of their duty to give special attention to business relationships and transactions with (legal) persons from countries which do not or insufficiently apply the FATF Recommendations, in line with Recommendation 21.
d. Measures should be taken to ensure that DNFBPs are advised of concerns about weaknesses in the AML/CFT systems of other countries.
e. DNFBPs should be required to have training programs that are on-going so as to be kept informed of new developments.

4.2.3 Compliance with Recommendation 16

	Rating	Summary of factors relevant to s.4.2 underlying overall rating
R.16	**PC**	• The reporting obligation does not cover transactions related to insider trading, market manipulation, arms trafficking, and participation in an organised criminal group (or otherwise cover this fully through conspiracy) as these are not predicate offences for money laundering in Iceland. • There is a concern that this broad secrecy requirement for lawyers might conflict with the obligation to report. • It is not required that the compliance officer and other appropriate staff have timely access to CDD, transaction, and other relevant information. There is no requirement to maintain an adequately resourced and independent audit function to test compliance (including sample testing) with AML/CFT procedures, policies and controls. • In addition, the training requirements do not specify that the training programs be on-going so as to be kept informed of new developments, or specify that they should cover ML and FT techniques, methods and trends. • DNFBPs would not receive the notices and instructions issued by the FSA if there is a need for special caution in transactions with a state or region. • There are no provisions dealing with the possibility to apply appropriate counter-measures where a country continues not to apply or insufficiently applies the Recommendations. • The provisions have just begun applying to the full range of DNFBPs and have not yet been put effectively into practice; it appears that DNFBPs that were covered under the previous AML requirements were not adequately complying with the reporting obligation.

4.3 Regulation, supervision and monitoring (R.24-25)

4.3.1 Description and Analysis

493. Casinos, including Internet casinos, are prohibited in Iceland.

494. There is no system for effective monitoring and ensuring compliance with AML/CFT requirements for DNFBPs. Icelandic authorities have not designed any authority to have the responsibility for the AML/CFT regulatory and supervisory regime for DNFBPs. There is no designed competent authority with adequate powers such as monitoring and applying sanctions.

Lawyers

495. The Ministry of Justice licenses lawyers pursuant to Articles 6-9 of the Act on Professional Lawyers No. 77/1999. Perspective applicants must possess legal competency, have never been declared bankrupt, have an untainted reputation, have completed legal studies with a final examination or a master's examination from the legal faculty of a university recognised in Iceland, and have competed an entrance test. The Ministry of Justice does not conduct any on-going surveillance of the legal profession.

496. The Icelandic Bar Association, which currently has 694 members, has a discipline and supervisory power over attorneys. However, the Bar association currently has no role with regard to AML/CFT oversight. The Association has a Code of Conduct, which applies to all members and contains measures on confidentiality and ethics.

497. Separate from the Bar is a Disciplinary Board, which handles complaints lodged against attorneys. By law, the Icelandic Bar Association appoints two members of this committee; one is appointed by the Icelandic Judges Association, one by the Minister of Justice and one by the Supreme Court. An attorney who has committed a fault can have various disciplinary sanctions imposed upon him by the Disciplinary Board, i.e. disbarment from the association, warning or admonition. Disbarment is resorted to in the cases of anyone, who in the pursuance of his profession as an attorney, deliberately has done wrong or has otherwise behaved dishonestly or who has shown a very grave lack of judgement. The Bar Association indicated that this has only been done three or four times.

Accountants

498. Members of the professional accountancy association number 301 in January 2006. The Ministry of Finance licenses auditors pursuant to the Act on Accountants, No. 18/1997. To qualify as a state authorised public auditor in Iceland, an individual must have completed four years of study of auditing, accounting, taxation, company law and business administration, have three years of relevant work experience and have passed a comprehensive examination conducted by the Ministry of Finance. They must also not be declared bankrupt and pass a series of exams. A large number of accounting firms operate in Iceland, and most of the major international accounting firms have member firms or representative firms in the country.

499. The legal environment concerning accounting and auditing rules is based on the Annual Accounts Act[26] and the Accounting Act [27]. The former sets out rules for disclosure and reporting, reports by management, consolidation of accounts and the continuing development of accounting standards through the creation of an Accounting Standards Board. The latter includes rules on accounting principles and practices and aligns Icelandic accounting legislation with the relevant EEA (EU) legislation.

[26] The Annual Accounts Act No. 144/1994

[27] The Accounting Act No. 145/1994

500. The Ministry of Finance is in the process of revising the Act so as to implement the 8th EU directive on accounting. At the time of the on-site visit, it was not foreseen that the Ministry would play any role in monitoring auditors for AML/CFT compliance.

501. In addition, a person who attends a special course and passes an exam can be registered as a chartered bookkeeper. Registration only verifies that this person has finished the course and does not give any professional rights to do auditing. According to Article 32 (1) of the Accounting Act no. 145, from 1994, holders of 1/5 of the voting rights can on an assembly demand that an auditor, audit company or examiner is elected. An auditor and audit company falls under the scope of Act on Auditors no. 17, from 1997. The Accounting Act indicates in Article 32 (2) that an examiner has to be legally and financially competent. He/she shall also have experience in bookkeeping and trading practices which are necessary with regards to the operation and size of the business. Furthermore, the qualifications of Article 9 of the Auditors Act also apply to examiners. Chartered bookkeepers are not mentioned and they do not have more rights to be elected examiners as any other person who qualifies according Article 32 (2).

502. The Institute of State Authorised Public Auditors (FLE), which has approximately 300 members, is a similar body to the Bar Association but with less discipline and supervisory power. It is also responsible for professional ethics and issuing of auditing guidelines. Membership is voluntary but 95% of auditors belong to the association. Individuals that have qualified as state authorised public auditors are admitted as members of FLE, but membership is voluntary. The Institute reviews the quality of every member's work every six years. Surveillance of the industry is conducted by the Institute's Audit Committee, which can take matters up that are brought to its attention and can recommend to the Minister of Finance to revoke an auditor's license, although such a recommendation has never been made. It should be noted that the Institute does not play a supervisory role of accountants who are not licensed as auditors.

503. The Institute was consulted during the process of drafting the revised MLA. The industry appeared aware of the obligations that would come into effect with the new law and appeared ready to implement them.

Real estate agents

504. The Ministry of Justice also license real estate dealers pursuant to the Act on Real Estate No. 99/2004. Requirements for obtaining a license include that a perspective have legal competency, not be declared bankrupt, have a clean criminal record, and pass an exam.

505. Once licensed, a special independent Committee, which consists of 3 people, oversees real estate agents to see if they are following the law and Code of Conduct. Every 3 years, the Committee also examines the financial management of dealers. The committee has also published guidelines, although none that pertain to AML/CFT

Recommendation 25 (Guidance for DNFBPs other than guidance on STRs)

506. Icelandic authorities reported that the FIU has been in contact with the DNFBPs regarding interpretation of the provisions of the new MLA and has provided lectures on MLA for various professional bodies.

507. However, guidelines on AML/CFT requirements to give assistance in implementing and complying with respective AML/CFT requirements have not been issued, such as the description of ML and FT techniques and methods; and any additional measures that these institutions and DNFBP could take to ensure that their AML/CFT measures are effective. After the on-site visit, the evaluation team was informed that the Ministries of Industry and Commerce were in the process of preparing information material (guidelines) for DNFBPs in cooperation with other members of the AML/CFT Consultation Committee.

508. FIU has promoted the issuing and acceptance of guidelines for the individual bodies within DNFBP. At the moment the Bar Association is in the process of making such guidelines and the AML/CFT Consultation Committee has discussed similar measures with other groups.

4.3.2 Recommendations and Comments

509. The Icelandic government should designate an authority, authorities, or SROs responsible for monitoring and ensuring compliance with the requirements of the new MLA. The authority/authorities should be provided adequate powers and sufficient technical resources to perform its/their functions. The authorities and/or SROs should also issue adequate guidance on AML/CFT requirements to all DNFBP sectors. Subsequent to the on-site visit, Icelandic authorities reported that discussions were underway amongst the various government agencies in order to determine the appropriate authority to monitor the DNFBP sector for AML/CFT compliance.

4.3.3 Compliance with Recommendations 24 & 25 (criteria 25.1, DNFBP)

	Rating	Summary of factors relevant to s.4.3 underlying overall rating
R.24	**NC**	• There is no system for effective monitoring and ensuring compliance with AML/CFT requirements for DNFBPs.
R.25	**NC**	• No AML/CFT guidelines have been issued for DNFBPs.

4.4 Other non-financial businesses and professions/ Modern secure transaction techniques (R.20)

4.4.1 Description and Analysis

510. Icelandic authorities have applied certain AML requirements to other non-financial businesses and professions since the MLA was amended in 1999. For example, Article 1 indicates that the act also applied to ship brokering (i.e., the buying and selling of ships), trading in art works about a certain amount, as well as licensed lotteries, raffles, and certain parties permitted to conduct fundraising activities. The AML/CFT Act 2006 continues to include these sectors, and also adds several more: any natural or legal persons engaged in trading of goods of EUR 15,000 or more, as well as natural or legal persons who, in the course of their work, perform the various activities where lawyers are covered (i.e., buying and selling real estate, managing client money, etc.). The law provides as examples tax consultants or other external consultants.

511. Iceland has also taken measures to encourage the development and use of modern and secure techniques for conducting financial transactions that are less vulnerable to money laundering, such as reducing the reliance on cash. The highest banknote issued is small—only 5,000 ISK—which, at the time of the on-site visit was equivalent to EUR 54 or USD 67. Cheques account for less than 1% (from 50% ten years ago). In 2005, debit cards accounted for 62% of the total number of transactions, credit cards for 38%. Iceland is probably the most advanced cashless society in Europe (cash and coins accounting for less than 1% of GDP). Almost all private consumption goes through payment cards.

512. Authorities indicate that Icelanders have fully embraced the use of the Internet as an essential tool to conduct both business and personal transactions. Iceland's established telecommunications and IT infrastructure presents a generally strong foundation to support a thriving e-commerce market. The market for Internet services in Iceland has grown significantly over the past couple of years, fuelled by high rates of Internet access and a high-adoption rate of electronic payment systems.

4.4.2 Recommendations and Comments

513. Iceland is fully compliant with Recommendation 20.

4.4.3 Compliance with Recommendation 20

	Rating	Summary of factors underlying rating
R.20	**C**	Iceland is fully compliant with Recommendation 20.

5. Legal Persons and Arrangements & Non-Profit Organisations

5.1 Legal Persons – Access to beneficial ownership and control information (R.33)

5.1.1 Description and Analysis

General

514. Nearly all forms of legal persons in Iceland must register at the Register of Enterprises, now located within the Tax Directorate of the Ministry of Finance, which will then issue a 10-digit enterprise number. This number is in practice required for doing any type of business in Iceland such as obtaining and maintaining a bank account.

Private limited companies

515. Private Limited Company or "einkahlutafélag" ("ehf."): (approximately 24,600) is by far the most numerous form of legal entity in Iceland, with approximately 25,000 on the register. Requirements are regulated by the Act on Private Limited Companies No. 138/1994, which is based on the relevant EU Directives. The minimum share capital is ISK 500,000. One or more people may be founders of an *ehf*; founders and shareholders may be individuals, registered public and private limited companies, and registered Co-operative Societies. The company's Board of Directors shall consist of at least three persons, unless there are four or fewer shareholders, in which case the Board may consist of one or two persons (Art. 39). The Board of Directors may also choose one or more managers (Art. 41). Managers and at least half of the Directors must be resident in Iceland or other EEA countries (Art. 42). The company must generally hold Board meetings and keep a record of minutes to show what occurs at board meetings which must be signed by those attending the board meetings (Art. 46).

516. To register the company, a notice must be provided to the Register of Enterprises (Fyrirtækjaskrá), at the Tax Directorate of the Ministry of Finance. The Notice must contain: details on the company's articles of association (which includes the company's name and address), the amount of share capital, and the names, identity number of and addresses of the founders, Directors, Managers, and those authorised to sign for the company (Art. 122). Directors and managers must be natural persons. Any changes to these must be notified within one month (Art. 123) to the Register of Enterprises. The information is also recorded in the minutes of a general meeting (directors) (Art. 65) and in a record of minutes for a board meetings (Art. 46). All the information at the Register of Enterprises is publicly available for a small fee.

517. The company's Board of Directors must maintain a share register and maintain it at the company's office (Act 138/1994, Art. 19). All shareholders and the authorities have access thereto and may acquaint themselves with the contents thereof. Share certificates may also be issued. Shareholders can be natural or legal persons; nominee shareholders are allowed, although bearer shares are effectively prohibited. In case of a change of ownership of a share, the name of the new shareholders shall be entered in the register of shares when he or his lawful representative gives notice of the change of ownership and proves his right. A person who has acquired a share cannot exercise his rights unless his name has been recorded in the share register or he has given notice and evidence of his ownership of the share.

518. According to Art. 65 of the Accounts Act No. 3/2006, all limited and private limited companies must publish the shareholders (which can be natural or legal persons) who own 10% or more of the company in their annual public accounts.

Public limited companies

519. Most of the large companies in Iceland are Public Limited Companies or "hlutafélag" (hf), which are regulated according to the Act on Public Limited Companies No. 2/1995. There were approximately 950 as of January 2006. Minimum share capital is ISK 4 million. There must be at least two founders, two shareholders, at least one manager and at least three persons on Board of Directors.

520. To register, a notice must be provided to the Register of Enterprises (Fyrirtækjaskrá) at the Tax Directorate. The Notice must contain: details on the company's articles of association (which includes the company's name and address), the amount of share capital, and the names, identity number of and addresses of the founders, Directors, Managers, and those authorised to sign for the company (Art. 148). Directors and managers must be natural persons. Any changes to these must be notified within one month (Art. 149) to the Register of Enterprises. The information is also recorded in the minutes of a general meeting (directors) (Art. 90) and in a record of minutes for a board meetings (Art. 70). All the information at the Register of Enterprises is publicly available for a small fee.

521. According to Art. 30 of Act No. 2/1995 respecting Public Limited Companies, a register of shares has to be prepared by the Board of Directors when it has been established. This register of shares shall at all times be kept at the office of a Public Limited Company and all shareholders and the authorities have access thereto and may acquaint themselves with the contents thereof. Share certificates must also be issued. Bearer shares are not allowed—according to according to Article 27, "share certificates shall be issued to a named person." However, shareholders can be natural or legal persons, and nominee shareholders are allowed.

522. In case of a change of ownership of a share, the name of the new shareholders shall be entered in the register of shares when he or his lawful representative gives notice of the change of ownership and proves his right. A person who has acquired a share cannot exercise his rights unless his name has been recorded in the share register or he has given notice and evidence of his ownership of the share.

523. According to Art. 65 of the Annual Accounts Act No. 3/2006, all limited and private limited companies must publish the shareholders (which can be natural or legal persons) who own or control 10% or more of the company are in their annual public accounts.

Listed public limited companies

524. Twenty-six public limited companies are also traded on the Icelandic Stock Market as of January 2006. In general, the same rules for public limited companies apply. Also, according to Chapter V of Act. No. 33/2003 on Securities Transactions, changes in ownership of a substantial holding in a limited-liability company which has had one or more classes of its shares listed on a regulated securities market, have to be notified to the registered securities market concerned and to the limited company immediately.

Co-operative companies

525. A co-operative company or "samvinnufélag" (svf.) is a legal entity which has united producers of farm products, fish etc., in marketing their produce and purchasing their supplies. They are regulated according to the Co-operatives Act No 22/1991. Their purpose is to further the interests of the members by economic activities in which the members take part as customers or suppliers or by contributing their labours or making use of the services of the association in some other manner. The members' interest must not be to obtain yield from capital. The number of these entities has decreased in recent years to about 82 in January 2006, which are registered at the Register of Co-operatives at the Tax Directorate. A transposition of an EU directive on European Co-operative Societies is in the legislative pipeline and is expected to be enacted later this year.

Foreign Companies

526. If a foreign company plans to operate in Iceland it can either establish a branch of a limited company or it can establish an independent company (subsidiary) in Iceland. They are required to register with the Register of Enterprises at the Tax Directorate if their activity falls within the scope of the taxation regulations (i.e., if they conduct business for a profit) in Iceland. Requirements for registration are the same as those provided for domestic private and public limited companies, according to the respective acts. Additionally, foreign companies have to provide a certificate of incorporation issued from the Register of their homeland and the latest annual account. There are 58 branches of foreign companies registered in Iceland.

527. In addition, an increasing number of foreign companies operate on the Icelandic stock market and/or do some business through Icelandic banks. In these cases, companies have been registered in a special register which is only available to the banks and some official authorities. In these cases, the bank with which the foreign company intends to have business sends the application for the registration along with the certificate of incorporation (provided by the foreign company to the bank) to the Register of Enterprises. Thus the burden of performing any "necessary survey" on the foreign company lies on the bank before the application is sent to the Register of Enterprises. There are currently 2,682 companies in this special register.

528. As with other companies, while the registration information is provided for foreign companies, the Icelandic authorities do not have automatic access to beneficial ownership information. In the case of foreign companies, access to beneficial ownership and control information would be even more difficult, since there is only a voluntary burden on banks to check ownership/control, there are no checks by the Register on the validity or ownership/control of the companies, and the fact that the company is registered in a foreign jurisdiction would make this verification even more difficult. The register concerned may, however, require information to be furnished so as to be able to verify whether legal requirements have been fulfilled.

EEIG and European Companies

529. EEC Regulation 2137/85 introduces European Economic Interest Groupings. The EEIG regulation stipulates that the purpose of a grouping shall be to facilitate or develop the economic activities of its members and to improve or increase the results of those activities; its purpose is not to make profits for itself. Its activity shall be related to the economic activities of its members and must not be more than ancillary to those activities. EEC Regulation 2157/2001 regulates a European Company. It stipulates that it will permit the creation and management of companies with a European dimension, free from the obstacles arising from the disparity and the limited territorial application of national company law. Both of these types of entities could be established in Iceland according to the transpositions of the above acts[28] but none has been founded so far.

Private Individuals

530. Private individuals *(approximately 11,200)* are people who are engaged in some kind of independent business who register with the tax authorities for the purpose of VAT, pension fund liabilities, etc. In recent years, the number registered under this arrangement has for taxation reasons decreased with a corresponding increase in the number of Private Limited Liability Companies.

Partnerships

531. General and limited partnerships (approximately 2,350) are a registered form for economic activity. For general partnerships, the owners carry unlimited liability for the partnership and share the profits between themselves. Under limited partnerships, at least one partner's liability is limited. Partnerships are registered with the District Commissioner's office if they wish to operate under a special name or logo. Limited partnerships must also register with the Register of Enterprises at the Tax Directorate, as required by the Act on Firms No. 42/1903, if they engage in merchandising, crafts, or manufacture. The

[28] Act 159/1994 and Act 26/2004

Register of Enterprises issues an identification number upon the partnership's providing a certificate from the respective District Commissioner's Office. At the end of 2002, there were 65 limited partnerships registered at the Register of Enterprises.

Foundations

532. Foundations are legal persons in Iceland; the main difference from limited companies is that there is no "owner" of the foundation, or the foundation owns itself. Foundations have a founding charter and/or memorandum of association, are established for a particular purpose, and have fund/capital requirements, and a board of directors. The foundation's capital or assets are separate from the founders' assets and managed by an independent board. Commercial foundations (44) must register with the Foundations Registry, which is now maintained by the Tax Directorate in the Ministry of Finance. Non-commercial foundations (671) do not have a direct obligation to register with the Tax Directorate; however, they generally do so in order to obtain an organisation number, which is generally required to open a bank account. Non-commercial foundations do need to apply to and be approved by the Ministry of Justice.

533. ***Commercial foundations*** ("sjálfseignarstofnun sem stundar atvinnurekstur") are regulated according to Act No. 33/1999 respecting Foundations Engaging in Business Operations. Foundations are defined as "engaging in business operations" if they derive earnings from the sale of goods and services and the like or engage in activities being in general similar to those of other associations or individuals engaging in business operations or if they wield the majority of votes in a Public or Private Limited Company or other companies or in another manner exert control on it

534. These are entities which have been established with a permanent donation (e.g. inheritance) of money or other valuables (e.g. real estate) in order to support a special purpose. Most serve educational or cultural purposes, such as the operation of theatres and commercial schools in Reykjavik. These institutions are registered in a special registry operated by the Tax Revenue Directorate in the Ministry of Finance. There are at present 44 in number.

535. The minimum capital to establish a commercial foundation is ISK 1,000,000. The foundation must notify the name and address of the foundation, the purpose, the amount of establishment funds, and the name, identification number and address of directors, managers, and holders of procuration powers (Art. 38). Managers and members of the Board shall have a clean police record (i.e., not found guilty of any violation of the Penal Code or other Acts pertaining to public and private limited companies, bookkeeping, annual accounts, or bankruptcy)(Art. 15). At least half of the Board members must be resident in Iceland or other European Economic Area countries. Any changes must be notified within one month (Art. 39). Some of this information is available via the Registry's website; all documents regarding the foundation can be examined by the public at the Registry. Alternatively, it is also possible to buy a certificate for ISK 700 containing all the information as above indicated. While this system allows timely access to certain kinds of information, it does not ensure automatic access to up-to-date information on beneficial ownership/control. Although the Register concerned may, require information to be furnished so as to be able to verify whether legal requirements have been fulfilled; it is not clear how timely the access to beneficial ownership/control information would be.

536. "Funds and institutions operating according to a confirmed charter"—i.e., ***non-commercial foundations*** –have been normally established for charitable or cultural purposes and have an old tradition in the Nordic countries with the charters confirmed by the respective kings. Since Act 19/1988 on Funds and Institutions Operating under Ratified Charters changed the structure and requirements of these entities, the number has been reduced. At present the number is 671, and only a few are established per year.

537. The foundation capital must be at least ISK 300,000 (Art. 2); but this amount is indexed and is now 400,000-500,000 ISK. The Charter shall prescribe the establishing capital and its source and for what purpose the fund or institution shall use its resources. The charter shall prescribe how the management of the foundation is selected and who is responsible for the preservation of the assets. The

charter must state the foundation capital and from where it has been derived, the purpose of the foundation, how the resources are to be spent, and who will manage the finances. The Ministry must also approve the charter and any subsequent changes to it. Approval of charters and changes are published in the Law Journal. When the Ministry receives an application, it may check into the criminal register, or in some cases a credit report may be requested from a credit assessment company. In some cases the local Chiefs of Police or Courts may also be contacted for carrying out a general or a specific check, depending on the circumstances of the application, the persons involved, etc.

538. The Board of a foundation must yearly submit its annual financial statements, together with a report stating how the foundation's financial resources were disposed of during that year to the State Auditing Office (Ríkisendurskoðun) (Art. 3), which is under the auspices of the Parliament. The accounts must be submitted before 30 June regarding the previous year and it shall be accompanied by information on the composition of the Board. The Office shall inspect the accounts and publish them in an open registry where all income and expenditures are recorded. Copies must be provided to those who request them. If annual accounts are not received by the Auditing Office within a year or they prove defective, the Minister of Justice can, on a suggestion from the Office, instruct a chief of police to investigate the fund or institutions and seize its assets and documents needed for the investigation. Assets of a foundation may not be sold or otherwise disposed of without the Minister of Justice's consent upon a recommendation by the State Auditing Office.

539. Information in the fund register is open to the public; copies of documents will be provided upon request. The information includes the identification number, the name of the foundations, and the year in which the foundation was established and registered. In general, this system does not provide adequate access to timely information on beneficial ownership/control.

5.1.2 Recommendations and Comments

540. The companies with limited liability (hf, ehf, co-ops) and branches of foreign companies are registered in the Register of Enterprises. That register is open to the public with its information on board members, addresses, and annual financial statements. For those companies listed on the stock market, additional disclosure rules apply. The registration system allows for some information on control to be recorded and made readily available; however, nominee directors are allowed. In addition, the Tax Directorate could play a larger role in verifying beneficial ownership/control for the applications it receives. No information on beneficial ownership is maintained in the government registers. Information regarding beneficial ownership may be available in certain circumstances in the company's registers; however, this is not a requirement, and shareholders may be nominees and other companies. Access to beneficial ownership (i.e., the natural person that ultimately owns or controls the entity) does not appear to be available in a timely fashion, and appears more limited in the case of foreign companies. Access to information on beneficial ownership of legal persons should be made more accurate and up to date.

541. Some information regarding the control of foundations is also generally registered, either with the Tax Directorate (for commercial foundations) or the Ministry of Justice (for non-commercial foundations.) However, the process is mostly limited to verifying the legal aspects of the application, and there are no mechanisms to know beneficial ownership/control beyond the direct managers and board members making the application.

5.1.3 Compliance with Recommendation 33

	Rating	Summary of factors underlying rating
R.33	**PC**	• Access to beneficial ownership does not appear to be available in an adequately timely fashion for Icelandic companies or foundations. • No beneficial ownership information for foreign companies is available. • Even though any change of managers and directors has to be notified to the

		Register, the Tax Directorate in practice does not perform any further inquiry to verify this. • Nominee directors are allowed.

5.2 Legal Arrangements – Access to beneficial ownership and control information (R.34)

5.2.1 Description and Analysis

542. Trusts cannot be set up under Icelandic law, and there are no other legal arrangements similar to trusts that exist in Iceland. Certain foundations may have characteristics of trusts; however, foundations are legal persons in Iceland and are therefore explained in the previous section of this report. However, there are no obstacles for an Icelandic citizen to be a trustee of a foreign trust. The applicable law is the foreign law chosen by the parties or, if none has been chosen, that with which the trust shows the closest connection. If information is considered necessary for Icelandic tax purposes, the tax payer has a requirement to disclose such information to the tax authorities. This may concern information about e.g. beneficiaries.

543. It should be noted that trusts are mentioned in the new AML/CFT Act 2006. The category of "trust and corporate service providers" is included as the category of covered person in article 3 (6), which covers the activity of acting as or arranging for another person to act as a trustee of a trust or similar legal arrangement. The legislation also includes as part of its definition of beneficial owner: "the natural person or persons who are the future owners of 25% or more of the assets of a trust or a similar legal arrangements or who control more than 25% of its assets. Where the individuals that benefit from such trust have yet to be determined, the beneficiary is the person or persons whose interest the fund is set up or operates." However, in this regard, it should be noted that the preparatory works for the law reiterate that trusts are not formed under Icelandic law. The preparatory works explain that the language on trusts is incorporated in the law so as to more closely reflect the wording of the 3rd EU Directive, and especially because "these are parties which could become customers of persons under obligation to report from abroad."

5.2.3 Recommendations and Comments

544. Recommendation 34 is not applicable to Iceland.

5.2.4 Compliance with Recommendations 34

	Rating	Summary of factors underlying rating
R.34	**NA**	

5.3 Non-profit organisations (SR.VIII)

Special Recommendation VIII

5.3.1 Description and Analysis

Scope of the Sector

545. According to Icelandic authorities, "NPO" as defined by the FATF especially applies to two types of entities in Iceland: commercial foundations (of which there are 44) and non-commercial foundations (of which there are 671). See the discussion under Recommendation 33 for a comprehensive description of the legal framework, structure, and registration and disclosure requirements for these types of entities. The main difference is that commercial foundations by definition are those that also engage in "business operations"—i.e., make a profit through the buying and selling of good and/or services.

Domestic Review

546. Iceland has not yet reviewed the adequacy of domestic laws and regulations that relate to non-profit organisations (NPOs) for the purpose of identifying the features and types NPOs of non-profit organisations (NPOs) that are at risk of being misused for terrorist financing by virtue of their activities or characteristics.

547. Authorities are planning a domestic review of the NPO sector and to implement other measures mentioned in the FATF interpretative note. Specifically, the Ministry has started reviewing the legislative side with regard to the Act. No 5/1977 on Fund-Raising in order to improve possibilities of fighting financing of terrorism. Authorities plan to make legislative changes as needed, as Icelandic authorities cannot exclude that this might be a channel for terrorist organisations to pose as legitimate non-profit organisation and divert the gains for financing of terrorism.

548. Iceland does have some access to information on the activities and features of the NPO sector which could identify the features and types of NPOs that are at risk of being misused for terrorist financing. Commercial foundations must submit a range of information on the founders and managers, purpose of the foundation, as well as any changes when registering with the Tax Directorate and the Ministry of Finance. For non-commercial foundations, the charters and changes thereafter must be submitted to the Ministry of Justice. In addition, these organisations generally will also register at the Tax Directorate in order to obtain a business identification number in order to open a bank account, etc. While there is therefore some general information at the entry level for these organisations, neither the Tax Directorate nor the Ministry of Justice comprehensively review the submissions so as to have a thorough understanding of the organisations; it is therefore unclear if there is adequate access to information so as to identify the features and types of NPOs, especially non-commercial foundations, at risk for terrorist financing purposes. A request for information may, however, be made as needed.

Outreach and oversight

549. Iceland has not yet undertaken outreach to the NPO sector with a view to protecting the sector from terrorist financing abuse, for example through raising awareness in the NPO sector about the FT risks. There is not adequate awareness regarding the international activities of Icelandic Foundations.

550. NPOs generally maintain information on the purposes and stated activities, as well as the identity of people who directly control their activities such as senior officers and board members. For example, commercial foundations must notify the Tax Directorate of their purpose and stated activities, as well as the name, and ID numbers, and addresses of directors and senior managers upon registration (Act 33/1999, Art. 38) and when changes are made. This information is maintained at the Foundations Registry at the Tax Directorate; some of this information is available via the Registry's website; all the other information on foundations is available free of charge upon request.

551. Non-commercial foundations are not required to maintain information on the purpose and objectives of their stated activities. The identity of the persons who own, control and direct their activities including senior officers, board members and trustees are probably submitted to the Minister of Justice upon application for a charter; however, this is not required by law. Thus, this information would not be publicly available.

552. In general, it is not demonstrated that Iceland has taken adequate measures to promote effective supervision or monitoring of those NPOs which account for: (i) a significant portion of the financial resources under control of the sector; and (ii) a substantial share of the sector's international activities.

Sanctions

553. For commercial foundations, the Finance Minister or its Commercial Foundations Registry may subject directors, managers, auditors, inspectors to daily or weekly fines when they neglect duties under the Act or decisions of the Minister of Foundation Registry until such time as the decision are complied with (Art 42). Fines or imprisonment for up to two years may also be imposed for deliberately violating the Act or deliberately giving incorrect statements or otherwise creating incorrect ideas about the circumstances of a foundation or other factors pertaining to it. However, penalties have never been imposed for these violations. There is no authority to freeze accounts or remove board members or directors. While the Registry may reject applications which are not adequate, there is no authority to de-register foundations for later violations. In general, there is not an adequate sanction regime against non-complying commercial foundations.

554. For non-commercial foundations, the legislation (Act. 19/1988) does not have the same detail of rules that are applicable to the commercial foundations. Nor does Act 19/1988 contain the same range of sanctions. In the cases where no annual financial statements have been submitted for a year or if the accounts prove to be deficient, the Minister of Justice may direct a police commissioner to investigate the finances of the foundation and take documents and assets into his keeping (Art. 4). However, this power has never been used. In addition, if the foundation's structure has changed so much that it is no longer possible to achieve its objectives, or if its board cannot be appointed in accordance with the provision of the Charter, then the Minister of Justice may amend the charter (Art. 6). Under the same conditions, the Minister of Justice may also combine foundations or abolish them in which case the assets shall be channelled into causes that are related to its original objectives. There are no other sanctions such as the ability to de-register, remove managers/directors, or apply fines.

555. Icelandic authorities indicate that the matter has already been discussed with the Ministry of Justice, and it has been agreed to introduce a proactive supervision of this sector by the Ministry of Justice. Authorities plan to publish the results of that supervision in future annual reports of the AML/CFT Consultative Committee.

License/registration

556. As indicated above, commercial foundations must register with the Tax Directorate at the Ministry of Finance and subsequently notify within one month of any changes to the information. The information in the registry is available to the public for a small fee.

557. For non-commercial foundations, regulated by the Act on Funds and Institutions Operating under Ratified Charters (No. 19/1988) there is a similar registration requirement—applications must be submitted to and approved by the Ministry of Justice, which maintains a register of these entities. In addition, while there is no direct requirement to register with the Registry of Enterprises at the Tax Directorate, most non-commercial foundations do so in order to obtain the business identification number ("*kennitala*"), which is generally needed to open a bank account. The Fund Register is open to the public; however it only contains information on the identification number, the name of the foundation, and the year in which it was established and registered.

Transaction records

558. Commercial foundations fall under the scope of "societies, funds or institutions engaged in business activity or in the procurement or trusteeship of funds", and therefore fall under the scope of the Accounting Act No. 145/1994 (Art. 1 (7)). They are therefore required to keep detailed accounts and all records shall be kept in a safe place for at least 7 years. The Accounting Act stipulates the main rules of proper bookkeeping and the complicated rules of the Tax Code must also be complied with. For example "accounts shall be kept so that transactions and the use of funds may be traced in an accessible manner." Icelandic authorities indicated that so far they have deemed it not necessary to carry out checks on how the accounts are kept.

559. Non-commercial foundations also fall under the scope of the Accounting Act, with the requirements as indicated in the above paragraph, and are also required to submit annual accounts to the State Auditing Office, according to Act 19/1988, Art. 3. This includes information on how the financial resources were disposed of during the previous year. Investigations have, however, revealed that verification of end-users can be extremely difficult.

560. In addition, the Act on Fund-Raising No. 5/1977 regulates public collections. Before a public collection is to begin, the organisation must notify the local chief of police as to who is in charge of the collection, when, where, and how it will be carried out (Art. 2). If collections are to take place in the streets or door-to-door, a permit from the Ministry of Justice is required. The collected funds must be places in a special bank or giro account, and the accounts must be audited. Within six months after the end of the collection, the accounts shall also be published (Art. 7). A third category, for example mass media such as daily news papers and TV stations carrying out collections for disaster relief or other good causes, does not need any notification or authorisation.

561. While this law contains some transparency for organisations (including foundations) that collect funds, it does not comprehensively cover all NPO transactions. In addition, the law exempts funds collected at a gathering. The Act on fundraising lacks, however, an article to make the preservation of accounts compulsory for 5-7 years. It is being contemplated to insert an article for such a requirement.

Information gathering and investigation

562. There appears to be adequate domestic co-operation, co-ordination and information sharing among the appropriate authorities that hold relevant information on NPOs of potential terrorist financing concern.

563. Information that is obtained regarding the administration and management of a particular NPO may be obtained during the course of information. However, while a range of information is required to be submitted by commercial foundations to the Ministry of Finance upon registration, non-commercial foundations do not have detailed requirements for disclosure or maintaining information on the administration and management of these entities; it is therefore not clear that detailed information on the administration and management of these entities is available during the course of an investigation.

564. A formal mechanism for the prompt sharing of information among all relevant competent authorities with regard to targeting NPOs suspected of terrorist financing has not been established. However, the various agencies such as the National Commissioner of the Icelandic Police, the Register of Enterprises, and other relevant authorities do appear to have good cooperation in general, which could also be applied in cases regarding NPOs. In a given case each of them will notify other authorities involved, when some action is considered to be necessary, investigative, preventative, informative or otherwise. This notification, exchange or sharing of information will take place promptly. Police also have the power to call for assistance from the necessary fields, such as from financial experts, computer or programmatic experts, etc. in a given case when NPOs are suspected of being exploited or used by terrorists.

565. Icelandic authorities indicate that the contact point for receiving international requests for information regarding particular NPOs suspected of aiding or supporting terrorists or making suspicious financial transactions, etc. is the National Commissioner of the Icelandic Police.

5.3.2 Recommendations and Comments

566. Iceland should review the adequacy of the legal framework that relates to NPOs vis-à-vis terrorist financing and ensure that there is adequate access to information so as to identify the features and types of NPOs at risk for terrorist financing purposes. Authorities have indicated that such a review is now underway.

567. Iceland should also reach out to the NPO sector with a view to protecting the sector from terrorist financing abuse. This outreach should include i) raising awareness in the NPO sector about the risks of terrorist abuse and the available measures to protect against such abuse; and ii) promoting transparency, accountability, integrity, and public confidence in the administration and management of all NPOs.

568. In general, Iceland should take more proactive steps to promote effective supervision or monitoring of those NPOs. Authorities have indicated that since the on-site visit, work has commenced to reorganise the foundation registers and consolidate "NPOs" into one register. The purpose is to monitor and separate fundraising and charity activities from commercial activities by "self-owned" organisations, foundations etc, and to protect these NPOs from being abused. Authorities should ensure that detailed information on the administration and management of non-commercial foundations is available during the course of an investigation. Iceland should also implement an effective sanction regime for violations of oversight measures or rules by NPOs or persons acting on behalf of NPOs.

5.3.3 Compliance with Special Recommendation VIII

	Rating	Summary of factors underlying rating
SR.VIII	**NC**	• Iceland has not yet reviewed the adequacy of domestic laws and regulations that relate to non-profit organisations (NPOs) vis-à-vis terrorist financing. • It is unclear if there is adequate access to information so as to identify the features and types of NPOs, especially non-commercial foundations, at risk for terrorist financing purposes. • Iceland has not yet undertaken outreach to the NPO sector. • It is not clear that detailed information on the administration and management of non-commercial foundations is available during the course of an investigation with regard to non-commercial foundations. • Non-commercial foundations are not required to maintain information on the purpose and objectives of their stated activities. • There are not adequate measures in place to sanction violations of oversight measures or rules by NPOs or persons acting on behalf of NPOs, especially with regard to non-commercial foundations. • Iceland has not identified specific points of contacts and procedures to respond to international requests for information regarding particular NPOs that are suspected of terrorist financing or other forms of terrorist support.

6. National and International Co-operation

6.1 National co-operation and coordination (R.31 & 32)

6.1.1 Description and Analysis (R.31 and R.32 (criteria 32.1 only))

Recommendation 31

569. Icelandic authorities have a number of formal and informal mechanisms in place to enhance the level of national cooperation and coordination amongst competent authorities. Examples of the various arrangements are: the AML/CFT Consultation Committee which was established to develop the new AML/CFT Act. Included within this group are: the police, the FIU, the Financial Supervisory Authority, the Icelandic Central Bank, the prosecutor's office, representatives from the Bankers and Security Dealers Association, as well as the Ministries of Commerce and Justice. Although originally formed for the purposes of developing new AML legislation, Icelandic authorities have decided that this group should continue in existence to review all legislative matters pertaining to AML/CFT and implementation of the new AML/CFT legislation. The aim is to formalise both the co-operation between the governmental and DNFBP sectors. The committee will publish an annual report on the progress in this field.

570. The level of cooperation between law enforcement authorities within Iceland appears very good. There does not appear to be any formal information sharing protocols in place, i.e. memoranda of understanding (MOUs), as there is a strong reliance on personal contacts and relationships amongst the personnel of the various agencies. There does not appear to be any barrier to communication and cooperation between law enforcement authorities within the country.

571. At the present time there also appears to be a good level of cooperation between the FSA and the law enforcement community. To this end, the FSA holds meetings with law enforcement representatives several times throughout the year. The relationship between the FSA and the FIU is also being improved; the FSA has hired an individual (effective June 2006) who will be dedicated full to AML/CFT matters and part of his responsibility will be to improve relations with the FIU.

Additional Elements

572. There is some consultation that occurs between competent authorities, the financial sector and DNFBPs concerning AML/CFT matters. Based on information gathered during the assessment, it appears that the consultative process has primarily occurred between competent authorities, the financial sector and several DNFBPs, such as; lawyers and accountants. Real estate agents and precious metal/stone dealers have had very little input into the process to this point.

Recommendation 32[29] (reviewing the effectiveness of AML/CFT systems)

573. Iceland has not yet reviewed the effectiveness of the AML/CFT systems in place.

6.1.2. Recommendations and Comments (R.31 and R.32 (criteria 32.1 only))

574. The current informal operational mechanisms for cooperation among law enforcement, the FIU and supervisors appear effective. While a consultation committee has been formed to develop new AML/CFT legislation, the Icelandic authorities are encouraged to continue this policy coordination now that the legislation has been approved. This will be important for example, in order to issue any appropriate regulations, guidelines, and assess the need for further developments in the future.

[29] See Section 7.1 for the compliance rating for this Recommendation.

6.1.3 Compliance with Recommendation 31

	Rating	Summary of factors underlying rating
R.31	**C**	

6.2 The Conventions and UN Special Resolutions (R.35 & SR.I)

Recommendation 35

6.2.1 Description and Analysis

Vienna Convention

575. Iceland ratified the UN Convention against Illicit Traffic in Narcotic Drugs and Psychotropic Substances (the Vienna Convention) on 2 September 1997. Act No. 10/1997 amended the General Penal Code and other relevant Acts of Law in order to implement the provisions of the Convention. Iceland has implemented the large majority of the convention's provisions; however, conspiracy to commit ML offences is not fully covered.

Palermo Convention

576. Iceland signed UN Convention against Transnational Organized Crime (the Palermo Convention), on 13 December 2000. Iceland has not yet ratified the Convention but is preparing to do so. Iceland has already implemented some of the convention's provisions that are applicable to the FATF recommendations. These include a wide range of serious crimes covered as money laundering predicate offences, the intentional elements of the ML offence, STR requirements, establishment of an FIU, extradition for ML, measures to provide legal assistance, and measures to freeze, seize, and confiscate proceeds of crime.

577. However, other key provisions of the conventions are not yet implemented. Article 5(1)(a), is not adequately covered: Participation in organised criminal group is not criminalised; nor is conspiracy to commit money laundering and other crimes fully covered so as to otherwise adequately criminalise "participation" in the crimes commitment by organised criminal groups. It is unclear whether self-laundering (as required by Article 6(2)(e)) is an offence in Iceland. There do not appear to be effective, proportionate, and dissuasive sanctions for ML. Finally, Article 18(1)(b) of the Convention, which requires countries to implement efficient measures to identify customers in whose interest accounts are opened is insufficiently implemented. Iceland's implementation of Recommendation 5 does not include adequate measures to ascertain the identity of beneficial owners.

CFT Convention

578. Iceland ratified the UN International Convention for the Suppression of the Financing of Terrorism (the Terrorist Financing Convention) on 15 April 2002. Act No. 99/2002 amends the Penal Code in order to implement the convention. Icelandic legislation implements the large majority of the convention's provisions relevant to the FATF Recommendations. Financing of a terrorist act directly is not specifically covered by Iceland's terrorist financing offence Sec. 100(b), although it appears most cases would be covered by other provisions. Also, the scope of "terrorist act" does not fully cover all the acts defined in Article 2 (1). Finally, Article 18(1)(b) of the Convention, which requires countries to implement efficient measures to identify customers in whose interest accounts are opened is insufficiently implemented. Iceland's implementation of Recommendation 5 does not include adequate measures to ascertain the identity of beneficial owners.

Additional elements

579. Iceland is party to several regional agreements and conventions which facilitate extradition and mutual legal assistance, mainly Council of Europe Conventions, the Schengen Convention and agreements with the other Nordic countries. For example, Iceland has ratified the 1990 Council of Europe Convention on Laundering, Search, Seizure and Confiscation of the Proceeds from Crime (the Strasbourg Convention) on 21 October 1997.

580. Furthermore, Iceland has ratified the following Council of Europe Conventions:

- The Council of Europe Convention on Extradition and the two additional protocols.
- The Council of Europe Convention on Mutual Assistance in Criminal Matters and the additional protocol.
- The Council of Europe Convention on the International Validity of Criminal Judgements.
- The Council of Europe Convention on the Transfer of Sentenced Persons and the additional protocol.
- The Council of Europe Criminal Law Convention on Corruption.

Special Recommendation I

CFT Convention

581. Iceland ratified the UN International Convention for the Suppression of the Financing of Terrorism (the Terrorist Financing Convention) on 15 April 2002. By Act No. 99/2002 the Penal Code was amended in order to fulfil the obligations of Iceland under the International Convention for the Suppression of Terrorist Bombings of 15 December 1997 and the International Convention for the Suppression of the Financing of Terrorism of 9 December 1999. With the amendment three provisions relating to the financing of terrorism, i.e. Articles 100 (a), 100 (b) and 100 (c), were added to the Penal Code.

582. Icelandic legislation implements the large majority of the convention's provisions relevant to the FATF Recommendations. Financing of a terrorist act directly is not specifically covered by Iceland's terrorist financing offence Sec. 100(b), although it appears most cases would be covered by other provisions. Also, the scope of "terrorist act" does not fully cover all the acts defined in Article 2 (1). Finally, Article 18(1)(b) of the Convention, which requires countries to implement efficient measures to identify customers in whose interest accounts are opened is insufficiently implemented. Iceland's implementation of Recommendation 5 does not include adequate measures to ascertain the identity of beneficial owners.

S/RES/1267(1999) and S/RES/1373(2001)

583. *S/RES/1267(1999):* Iceland generally implements the provisions of S/RES/1267; however, there are no formal procedures for authorising access to frozen resources when deemed necessary for basic expenses, the payment of certain types of fees, etc pursuant to S/RES/1452(2002).

584. *S/RES/1373(2001):* Iceland does not have an adequate mechanism to implement S/RES/1373 for a variety of reasons. The Public Announcement's definition of terrorism and all subsequent obligations are limited to certain violent acts in the Penal Code—it does not fully cover all persons who commit or attempt to commit terrorist acts.

585. While the Announcement covers entities that are owned by terrorists etc, it does not specifically cover funds of entities that are controlled directly or indirectly by such persons. Nor does it cover funds or other assets derived or generated from funds or other assets owned or controlled directly or indirectly by designated persons, terrorists, those who finance terrorists, or terrorist organisations. The freezing obligation in Law 87/1998 allows only for the FSA to forward lists pursuant to international obligations. As a practical matter, the only lists that can be enforced are those from the 1267 designation committee.

586. There is not a comprehensive mechanism in place to examine and give effect to actions initiated under the freezing mechanisms of other jurisdictions.

587. S/RES/1373 also requires countries to fully implement the CFT Convention. As indicated above, Iceland has not fully implemented the CFT Convention. Financing of a terrorist act directly is not specifically covered by Iceland's terrorist financing offence Sec. 100(b), although it appears most cases would be covered by other provisions. Also, the scope of "terrorist act" does not fully cover all the acts defined in Article 2 (1). Finally, Article 18(1)(b) of the Convention, which requires countries to implement efficient measures to identify customers in whose interest accounts are opened is insufficiently implemented. Iceland's implementation of Recommendation 5 does not include adequate measures to ascertain the identity of beneficial owners.

6.2.2 Recommendations and Comments

588. Iceland should more fully implement the CFT Convention. The definition "terrorist act" should be broadened to fully cover all of the acts defined in Article 2 (1) of the Convention. More comprehensive measures for identifying beneficial owners should also be adopted. Iceland should also institute adequate comprehensive conspiracy provisions for money laundering.

589. Iceland should ratify the Palermo convention and fully implement all of its provisions. Finally, Iceland should also more fully and effectively implement the provisions required by S/RES/1267 and S/RES/1373.

6.2.3 Compliance with Recommendation 35 and Special Recommendation I

	Rating	Summary of factors underlying rating
R.35	**PC**	Vienna Convention • Conspiracy to commit ML offences is not fully covered. CFT Convention • The scope of "terrorist act" does not fully cover all the acts defined in Article 2 (1), and there is a concern that the financing of a terrorist act as defined in the legislation. • Iceland's implementation of Recommendation 5 does not include adequate measures to ascertain the identity of beneficial owners. Palermo Convention: • Iceland has not ratified the Palermo Convention. • Key elements of the Convention are not yet implemented: Participation in organised criminal group is not criminalised; nor is conspiracy to commit money laundering and other crimes fully covered so as to otherwise adequately criminalise "participation" in the crimes commitment by organised criminal groups. • It is unclear whether self-laundering (as required by Article 6(2)(e)) is covered. • There do not appear to be effective, proportionate, and dissuasive sanctions for ML. • Iceland's implementation of Recommendation 5 does not include adequate measures to ascertain the identity of beneficial owners.
SR.I	**PC**	CFT Convention • The scope of "terrorist act" does not fully cover all the acts defined in Article 2 (1), and there is a concern that the financing of a terrorist act as defined in the legislation is not fully covered. Iceland's implementation of Recommendation 5 does not include adequate measures to ascertain the identity of beneficial owners.

		S/RES/1267 • There are no formal procedures for authorising access to frozen resources when deemed necessary for basic expenses, the payment of certain types of fees, etc pursuant to S/RES/1452(2002). S/RES/1373 • Iceland does not have an adequate mechanism to implement S/RES/1373. There is not a comprehensive mechanism in place to examine and give effect to actions initiated under the freezing mechanisms of other jurisdictions. • The Public Announcement's definition of terrorism and all subsequent obligations are limited to certain violent acts in the Penal Code—it does not fully cover all persons who commit or attempt to commit terrorist acts. • The Public Announcement does not specifically cover funds of entities that are *controlled directly or indirectly* by such persons. Nor does it cover funds or other assets derived or generated from funds or other assets owned or controlled directly or indirectly by designated persons, terrorists, those who finance terrorism, or terrorist organisations. • The direct obligation to freeze funds pursuant to designations in the context of S/RES/1373 is contained Sec 16(a) of the revised Law 87/1998 which does not apply to entities not supervised by the FSA, such as money exchange and money transfer and non financial business and professionals • Iceland has not fully implemented the CFT Convention as required by S/RES/1373.

6.3 Mutual Legal Assistance (R.36-38, SR.V, R.32)

6.3.1 Description and Analysis

Recommendation 36 and SR.V (Criterion V.1)

590. Iceland is party to the 1959 European Convention on Mutual Assistance in Criminal Matters, the 1957 Convention on Extradition and the 1970 Convention on the International Validity of Criminal Judgements. In addition, Iceland is party to several regional agreements and conventions which facilitate extradition and mutual legal assistance, as the Schengen Convention, the Eurojust project and some agreements with other Nordic countries. Iceland's mutual legal assistance measures apply equally to money laundering (R. 36) and terrorist financing matters (SR. V).

591. Icelandic authorities can comply with requests for mutual legal assistance coming from any country on the basis of reciprocity even if no specific agreement exists between Iceland and the requesting country. Iceland has not entered into any bilateral agreement for legal assistance and international co-operation.

592. The conditions for assisting foreign states for the purpose of criminal investigations and proceedings are laid down in the Act on Extradition of Criminals and other Assistance in Criminal Proceedings n. 13/1984 (as amended in 2001). The relevant provisions are found in Art. 20-23(b) allow for a wide range of mutual legal assistance in AML/CFT investigations and prosecutions as well as for enforcement of criminal judgements and confiscation orders.

593. In general, a request may not be granted if the acts to which it refers, or "comparable acts", are not punishable under Icelandic law ("dual criminality") or cannot constitute ground for extradition, which include those offences of a political nature, the risk of persecution, or if humanitarian reasons argue against it (Art. 5-7).

594. There are exceptions to these conditions for Nordic and Schengen countries. For Nordic countries (Denmark, Finland, Norway, and Sweden) dual criminality is not necessary except for requests involving political or military offences. Assistance would still not be granted in the cases of where there is a risk of persecution or humanitarian reasons. However, in this case dual criminality exceptionally applies. For States participating in Schengen, the extradition requirement is not necessary—i.e., assistance can be granted in requests involving offences of a political nature, where there is the risk of persecution, or humanitarian reasons.

Scope of information provided

595. Pursuant to Art. 22, in order to gather evidence for use in criminal proceedings in another State, the provisions in the Code of Criminal Procedure shall be applied in the same way as in comparable domestic proceedings. This includes the powers for Icelandic law enforcement authorities to use compulsory measures for the production of records, for the search of persons and premises as well as for the seizure of evidence. This would include all types of records such as transaction and customer identification records from financial institutions. the production, search and seizure of information, documents, or evidence (including financial records) from financial institutions, or other natural or legal persons; the taking of evidence or statements from persons; effecting service of judicial documents; and the identification, freezing, seizure, or confiscation of assets laundered or intended to be laundered, the proceeds of ML and assets used for or intended to be used for FT, as well as the instrumentalities of such offences, and assets of corresponding value. (For a fuller description of assistance relating to asset seizure and confiscation see the discussion under Recommendation 38.)

596. As a minor point, legal provisions on mutual legal assistance would not encourage or facilitate the voluntary appearance of witnesses or persons providing information to the requesting country, as this seems to be out of the scope of Act 13/1984.

Procedure for processing requests and timeliness of responses

597. Requests must include the type of offence, place and time of its commission, and shall be sent to the Ministry of Justice except in the case of Nordic countries, where communication flows directly through the National Police Directorates.

598. If the request pertains to an offender who has been sentenced to imprisonment, the Iceland law requires that the foreign decision be taken by foreign courts in conformity with domestic legislation. Representatives from the Ministry of Justice explained that in practice they only ascertain if all the relevant information on the case is provided, otherwise additional clarifications are sought. If these are not supplied, the request will be refused.

599. The Ministry then forwards the request to the office of the Director of Public Prosecutions (also called the "Prosecutor General") which investigates the case and collects the requested evidence. The results are transmitted back to the Ministry along with the prosecutor's opinion – that is not binding – and incorporated in the answer to be send to the requesting country.

600. Among the others, the Act entails specific provisions on the witnesses to be acquired abroad from sentenced person subjected to deprivation of liberty. By an agreement with foreign authorities, notifications and case documents relating to criminal investigations or proceedings may be sent directly to the persons involved staying in Iceland.

601. Requests for co-operation and legal assistance are handled by a specific department within the Ministry of Justice, named Police and Judicial Affairs, which is comprised of four people. Icelandic officials indicated that the average time to answer a request, when any further enquiries or information from the requesting country are not necessary, is two weeks, and as of the date of the on-site visit, there were no pending requests. The department receives approximately two or three requests of assistance per year concerning economic crimes and as far as they can remember no request has ever been refused. Total requests are around 10-20 per year and they are mainly coming from the Nordic as well as Balkan countries. From 2002 no request has been refused for not fulfilling the dual criminality requirement. Apart from that, no evidence was available on the effectiveness of the assistance provided.

Conditions and restrictions

602. Mutual legal assistance is not subject to unreasonable, disproportionate or unduly restrictive conditions. A conviction is not required for providing assistance; nor is the commencement of a judicial proceeding required. In fact, beside the basic information on the offence committed, the only requisite upon which co-operation may be denied is dual criminality. No special restrictions are in place for offences concerning fiscal matters; fiscal offences and tax fraud are criminalised in Iceland, and major tax frauds can constitute predicate offence for money laundering as well. Bank secrecy or confidentiality may not be used as a ground for not granting mutual legal assistance requests.

603. Since it is not clear if self-laundering is covered, and conspiracy to commit money laundering is not fully criminalised by Iceland, it is unclear how effectively Iceland can provide assistance relating to these cases. However, authorities explained that assistance involving self-laundering could be executed and cited an example of assistance provided in a case involving a Polish citizen already prosecuted in Iceland for the same facts as the request was related to.

604. The limitations on the scope of "acts of terrorism" as defined in Iceland also present some concerns about Iceland's ability to effectively provide assistance in cases involving the financing of acts not defined as terrorist acts in Iceland.

Avoiding conflicts of jurisdiction

605. When a case is prosecuted in more than one country, in order to avoid conflicts of jurisdiction, Iceland applies the principles outlined in the European Convention on the Transfer of Proceedings in Criminal Matters on a case by case basis, since the Convention has not been ratified.

Additional elements

606. As a general principle direct contacts between law enforcement counterparts should be based on an international agreement, at least if coercive measures are involved. However, in practice, assistance is given based on the principles in the European Convention on Mutual Assistance in Criminal Matters as incorporated in Act 13/1984. Whether the request for legal assistance involves Nordic countries, informal procedures always apply.

Recommendation 37 (dual criminality relating to mutual legal assistance) and SR.V (criterion V.2)

607. According to the Extradition of Criminals and other Assistance in Criminal Proceedings Act No. 13/1984, dual criminality is generally always required. The only exception is for Nordic countries, where dual criminality is required only for requests involving political offences. It should be noted that the Act refers to powers to gather and provide evidence pursuant to the Code of Criminal Procedure, which generally pertains to coercive measures.

608. Act 13/1984 is silent concerning less intrusive and non-compulsory measures. Authorities indicated that these types of requests would be evaluated on a case by case basis; however, it appears that the dual criminality requirement would still apply, even in the case where e.g. company commercial records or other publicly available information are requested. According to the current framework the procedure to be followed is the same as for any other mutual legal assistance request.

609. Although there is a general principle of dual criminality, Iceland has no legal or practical impediment to rendering assistance where both countries criminalise the conduct underlying the offence. As indicated in Art. 22 of Act, a request for mutual legal assistance requires that "the act giving rise to the request, or a comparable act" be punishable under Icelandic law. Therefore, when assessing the feasibility of a request the authorities will look at the underlying facts and substantive profiles of the offence. As a consequence, the manner in which each country categorises or denominates the offence should not pose an impediment to the provision of mutual legal assistance.

Recommendation 38 and SR.V (Criterion V.3)

610. The general requirements for enforcing foreign criminal judgements are found in the International Co-operation on Enforcement of Criminal Judgements Act 56/93, as amended in 1997, which implements the 1970 Council of Europe Convention on the International Validity of Criminal Judgements. The provisions of this act also apply to agreements made with non-European states.

611. This law allows Iceland to enforce a confiscation order from a foreign court upon the condition that the assets could also be confiscated in Iceland if the case had occurred there (Art. 18). The general principles indicated in Art. 1 specifies that a bilateral or multilateral treaty or convention must apply to both states. If so, Iceland may enforce or execute penalties from foreign judgments or decisions, regarding fines, dispossession of freedom, obtaining confiscation, or decisions from a foreign administrative body. Art. 2 references some conventions that Iceland is a party to, including the 1990 Council of Europe Convention on Laundering, Search Seizure and Confiscation of the Proceeds from Crime, the 1970 European Convention on the International Validity of Criminal Judgements, and the 1988 UN Vienna Convention. Art. 3 also allows for the use of the act's provisions in specific circumstances even if there is no common convention between Iceland and the requesting State., although no case law was available on this at the time of the visit.

612. Domestic measures that give effect to foreign requests for search, freezing, seizing and forfeiture apply equally to money laundering and terrorist financing cases. The conditions that foreign confiscation order must meet are the same as for the execution of a domestic measure as laid down in Sec. 69 of the

Penal Code. Investigative and other judicial powers may be applied for securing and recovering proceeds, assets and instrumentalities used or intended fur use in money laundering and terrorist financing as well as property of corresponding value. (See discussion of Recommendation 3).

613. The procedure for evaluating the requests in this field is the same as for any other case of mutual legal assistance. Among the conditions for refusal laid out in Art. 6-8, some are the common exceptions due to the dual criminality requirement and the political or military nature of the offence, whereas others are more specific. Art. 6 and 7 prevent Icelandic authorities from affording any co-operation when the foreign application is based on European penal judgment is not a final decision, it is against fundamental principles of the Icelandic law, it has already been executed in Iceland or in a third state with respect to the same offence or the person has been acquitted on the account of that offence or when the criminal conduct did not occur in the State requesting the enforcement of penalties. Article 6 also does not allow foreign judgments to be executed if the person is not domiciled in Iceland.

614. The main principle is that the Director of Public Prosecutions (DPP) shall bring the case to a District Court (Art. 10). The court does not review the criminal liability of the person judged (Art. 11). The role of the court at this stage of proceedings is to establish whether the request is to be denied because the conditions of Art. 6 are not met, there is valid reason to believe that judgement has been passed or that the sentence imposed was heavier than it should have been due to the race, nationality, religious belief or political persuasion of the person sentenced, or that the penalty has lapsed due to the limitations provision of the Penal Code. The court does not make a fresh examination of whether or not the person sentenced meets the conditions regarding criminal responsibility regarding the offence. If the court considers that authorisation exists for the execution of the sentence in Iceland, it determines, under Sections 13-15 of the act, a new punishment for the offence which would be imposed under Icelandic law for comparable offences.

615. However, if the foreign request concerns properties of a third person (i.e. other than the person judged) the DPP is due to open a case against this part before an Icelandic court. If the case concerns collection of fines or confiscation of property, and upon the consent of the third person involved, a simplified procedure can be followed whereby the request takes place through an agreement with the third party and the foreign authority.

616. When a request for seizing a suspect's property for the settlement of fine, damages, costs, or confiscation, comes from another Nordic country, the legal framework is different, namely the "common Nordic legislation on co-operation between Iceland, Denmark, Finland, Norway or Sweden concerning the carrying out of sentences, etc. (Act No. 69/1963)". Authorities purported the view that this law follows the same general conditions set out in Act 13/1984 except for the dual criminality requirement and the informal procedure for transmitting the requests. Beyond this no specific information was supplied to the evaluation team.

617. Nevertheless, no practical experience has been developed so far on this issue.

Coordinating seizure/confiscation and sharing assets

618. Iceland does not have any specific agreement or MOU for co-ordinating seizure and confiscation actions with other countries. However, informal arrangements exist. In international cases, searches and seizures are normally co-ordinated through preparatory meetings before action is taken and a support team is appointed for collecting documents and information. In a domestic case Icelandic, investigators will usually participate in the most relevant actions abroad; as will foreign investigators in Iceland if they are involved in a local case. In addition, in the European domain Iceland is taking part to the Eurojust network through appointment of contact point prosecutors, with a view to strengthen the fight against serious crimes by facilitating the exchange of relevant information. Co-operation in this field can also be arranged within the Schengen Agreement framework as well as through Interpol and Europol channels.

619. At this time Icelandic authorities are not considering establishing an asset forfeiture fund.

620. Iceland has not considered authorising the sharing of confiscated assets between them when confiscation is directly or indirectly a result of co-ordinated law enforcement action. Pursuant to Sec. 69 of the Penal Code, all confiscated assets accrue to the State Treasury. This principle is reiterated in Art. 32.3 of Act 56/1993. This article also indicates that the Ministry of Justice may decide, upon a request from the State demanding enforcement of a judgment, that a confiscated object is handed over to that State. However, Icelandic authorities have clarified that "object" cannot include confiscated assets and funds.

Additional elements

621. Iceland only recognises criminal confiscation; therefore, it is not possible to enforce a foreign civil forfeiture order.

Recommendation 32[30] (Statistics)

622. Icelandic authorities do not maintain precise statistics on MLA requests relating to ML and FT, including the nature of the request, whether it was granted or refused, and the time required to respond. However, the evaluation team was told that approx. 10-20 mutual legal assistance requests per year are received by the Ministry of Justice. Although the Ministry of Justice has a registration system in place for cases and requests, this does not make possible to collect such specific data since it does not indicate the crime(s) concerned by the requests.

6.3.2 Recommendations and Comments

623. Overall, Iceland has a generally broad legal framework for granting international co-operation. Requests for mutual legal assistance from Nordic countries are not subject to the dual criminality requirement (except for political offences) and are treated expeditiously as they are channelled directly between judicial and law enforcement authorities. Icelandic authorities are allowed to assist foreign countries with every measure that is available for domestic investigations and prosecutions. This includes enforcing foreign judgments for identification, freezing and confiscation of assets. However, Iceland should clarify the procedures to allow non-coercive measures to be applied in the absence of dual criminality. In addition, Iceland should enact provisions on mutual legal assistance that would encourage or facilitate the voluntary appearance of witnesses or persons providing information to the requesting country.

624. Experience in this field, especially with countries outside the Nordic community, is still limited as international co-operation has been carried out insofar on a very small scale. Furthermore effectiveness of the current laws cannot be demonstrated due to the lack of quantitative and qualitative data.

625. Iceland should consider establishing an asset forfeiture fund and a mechanism to authorise the sharing of confiscated assets with other countries when confiscation is directly or indirectly a result of co-ordinated law enforcement actions.

6.3.3 Compliance with Recommendations 36 to 38 and Special Recommendation V

	Rating	Summary of factors relevant to s.6.3 underlying overall rating
R.36	**LC**	• Since it is not clear if self-laundering is covered, conspiracy to commit money laundering is not fully criminalised, and not all predicate offences are fully covered, it is unclear how effectively Iceland could provide assistance relating to these cases. • Legal provisions on mutual legal assistance would not encourage or facilitate the voluntary appearance of witnesses or persons providing information to the requesting country, as this seems to be out of the scope of Act 13/1984.

[30] See Section 7.1 for the compliance rating for this Recommendation.

		• The limitations on the scope of "acts of terrorism" as defined in Iceland also present some concerns about Iceland's ability to effectively provide assistance in cases involving the financing of acts not defined as terrorist acts in Iceland**.** • Effectiveness of the current laws cannot be demonstrated due to the lack of quantitative and qualitative data. There is no evidence of how expeditiously requests are answered.
R.37	**PC**	• Dual criminality would still apply to requests for less intrusive and non-compulsory measures such as company commercial records or other publicly available information.
R.38	**LC**	• Since it is not clear if self-laundering is covered, conspiracy to commit money laundering is not fully criminalised, and not all predicate offences are fully covered, it is unclear how effectively Iceland could provide assistance relating to these cases. • Foreign judgments cannot be executed if the person is not domiciled in Iceland. • Iceland has not considered authorising the sharing of confiscated assets when confiscation is directly or indirectly a result of co-ordinated law enforcement action. Icelandic authorities have not considered establishing an asset forfeiture fund.
SR.V	**LC**	• Since dual criminality applies, the limitations on the scope of "acts of terrorism" as defined in Iceland also present some concerns about Iceland's ability to effectively provide assistance in cases involving the financing of acts not defined as terrorist acts in Iceland**.** • Foreign judgments cannot be executed if the person is not domiciled in Iceland.

6.4 Extradition (R.39, 37, & SR.V)

6.4.1 Description and Analysis

Recommendation 39 and SR V (Criterion V.4)

626. Both money laundering and terrorist financing are extraditable offences in Iceland. There are laws and procedures to extradite individuals charged with a money laundering or terrorist financing offence. Extradition rule and procedures are dealt with in Act 13/1984 on Extradition of Criminals and other Assistance in Criminal Proceedings (as amended in 2001), exception for Nordic countries to which the Act on Extradition of Offenders to Denmark, Finland, Norway and Sweden No. 7/1962 applies. Although no extradition treaties are in place in Iceland, this does not prevent it from affording co-operation to foreign States since the current law does not subject extradition to the existence of a treaty.

627. Act 13/1984 allows for extradition if the concerned offence is equivalent in substance to a crime punishable under Icelandic law with imprisonment of one year or more (Art. 3). Therefore, this requirement is satisfied in cases concerning money laundering and financing of terrorism. If the extradition concerns enforcement of a passed sentence, the penalty imposed must be four months imprisonment or more or other forms of detention for an equivalent period.

628. Act 13/1984 generally prohibits extraditing Icelandic nationals (Art. 2). However, Act 7/1962 permits the extradition of Icelandic nationals to the Nordic States if the person has been domiciled for two years prior to the offence in the requesting state or if the offence is punishable under Icelandic law with imprisonment of four years or more. Therefore this would cover extradition for terrorist financing and aggravated and drug-related money laundering, but not other money laundering offences. The non-Icelandic nationals, the legislation also has a lower threshold: extradition will be allowed if the offence has a punishment of more than a fine.

629. Icelandic authorities point out that Iceland has criminal jurisdiction over any person, including Icelandic nationals who have committed abroad certain criminal offences, subject to some conditions pursuant to Sec. 4 and 5 of the Penal Code. These provisions also cover the case where the predicate offence for money laundering and the terrorism offences have been perpetrated outside the Icelandic territory.

630. If a foreign state (other than a Nordic state) should ask for extradition of an Icelandic citizen, the case request is denied immediately. Under the second paragraph of Article 6 of the European Convention on the Extradition of Criminals of 1957, to which Iceland is a party, a state that denies the extradition of its own citizens is required to institute proceedings if the state that requested extradition so desires. A special request must be made to the Icelandic authorities to institute proceedings, and if this is received, then the same procedural rules apply to the case as would apply to comparable cases in Iceland.

631. Current law prohibits extradition in connection with political offences. Exemptions to this principle can be made in international agreements, in which certain offences, typically political in nature, are not considered as such. This applies to all requests for extradition based on Article 1 or 2 of the TF Convention or Article 2 of the International Convention for Suppression of Terrorist Bombing. Special provisions in the Act 7/1962 allow for extradition of non-nationals to Nordic countries also in case of political offences, but dual criminality is then required. Extradition will also be denied if there would be a considerable risk of persecution for the person involved, when such a person has been convicted or acquitted in Iceland for the same offence, or on the ground of humanitarian reasons, like age or health, (Act 13/1984, Art. 4-8) or face the death penalty (Art 11.).

632. Art. 12 of Act 13/1984 requires that extradition requests be made through diplomatic channels "unless other arrangements have been agreed with the state involved." In practice, diplomatic channels are now used only for non-European requests. All cases are then sent to the Ministry of Justice. After a preliminary analysis of the request, the Ministry sends the application to the Director of Public

Prosecutions, which ensures that any further investigation that is deemed necessary will be carried out. At this stage investigations are focused on the formal requirements of the requests. The requesting State must show that there is a reason for extradition in the specific case; additionally, a copy of the relevant domestic legal provisions which are assumed to be breached or a certified copy of the conviction or detention order shall be enclosed.

633. Once the Ministry has decided to grant extradition, the procedure should be as quickly as possible (Art. 18) and the domestic criminal procedure provisions shall apply, as appropriate, to investigations and other matters concerning extradition applications. The person whose extradition is requested may however demand the ruling of the competent Icelandic court to verify the fulfilment of the legal requirements of the procedure. This demand has to be submitted to the General Prosecutor or the Ministry of Justice itself not later than 24 hours after the person has been informed that the extradition has been granted. Within the Schengen agreement the approval for the extradition may extend to punishable act other than that specified in the request. Assets and valuables confiscated in connection with the extradition case are made over to the foreign requesting authority with the necessary provisos in safeguard of the right of third parties.

Additional elements

634. In principle, direct transmission of extradition requests has to be based on an international agreement. However, in practice the Ministry of Justice usually accept a direct request and take the first steps of the procedure while waiting for the formal request. A formal request from the competent authority is nevertheless required.

Recommendation 37 (dual criminality relating to extradition)

635. Iceland has no legal or practical impediment to rendering assistance in extradition requests where both countries criminalise the conduct underlying the offence. Article 3 of Act 13/1984 indicates that a person may only be extradited if the offence involved "or a comparable offence" could be punishable by more that one year's imprisonment under Icelandic law. When assessing the feasibility of a request the authorities will look at the underlying facts and substantive profiles of the offence. As a consequence, the manner in which each country categorises or denominates the offence should not pose an impediment to extradition.

Recommendation 32[31] (Statistics)

636. Icelandic authorities do not maintain precise statistics on extradition requests relating to ML and FT, including the nature of the request, whether it was granted or refused, and the time required to respond. However, Icelandic authorities indicated that they usually receive only five or six extradition requests per year, primarily from Nordic countries, the Netherlands and Baltic States, and no application was pertaining to money laundering or terrorist financing offence to date. Only two requests were declined so far as they were related to minor offences.

6.4.2 Recommendations and Comments

637. Iceland has a generally comprehensive framework for extradition of non-Icelandic nationals, and for extradition requests from Nordic countries involving more serious crimes (i.e. with a punishment of four years or more), Icelandic nationals as well. However, the lack of statistics and cases in the courts makes it difficult to determine how effective the legislation is in practice.

638. Iceland should collect and maintain statistics on i) the number of requests for extradition; ii) the offence the request was related to; iii) whether the request was granted or refused; iv) the amount of time required to answer.

[31] See Section 7.1 for the compliance rating for this Recommendation.

6.4.3 Compliance with Recommendations 37 & 39, and Special Recommendation V

	Rating	Summary of factors relevant to s.6.4 underlying overall rating
R.39	**LC**	• Since it is not clear if self-laundering is covered, and conspiracy to commit money laundering and all the required predicate offences are not fully covered, it is not clear how effectively Iceland could extradite relating to these offences.
R.37	**PC**	• (Adequate with respect to extradition/Crit. 37.2)
SR.V	**LC**	• Since dual criminality applies, the limitations on the scope of "acts of terrorism" as defined in Iceland also present some concerns about Iceland's ability to effectively respond to extradition requests in cases involving the financing of acts not defined as terrorist acts in Iceland**.**

6.5 Other Forms of International Co-operation (R.40, SR.V & R.32)

6.5.1 Description and Analysis

Recommendation 40 and SR.V (criterion V.5)

General principles

639. In general law enforcement, the FIU, and supervisors can engage in a wide range of international co-operation. Icelandic authorities attempt to render assistance to foreign authorities in as expeditious manner as possible, and information concerning money laundering and predicate offences maybe exchanged upon request, provide that it is in accordance with Icelandic law. Competent authorities within Iceland are permitted to conduct inquiries on behalf of their foreign counterparts. An example of this would include; inquiries made by Icelandic law enforcement on behalf of a foreign law enforcement agency which occurs frequently.

640. There does not appear to be any undue restrictions and/or conditions outside of the "normal caveats" which are placed on information exchanged between Icelandic competent authorities and their foreign counterparts. Information requests by foreign authorities are not refused on the basis that they may involve fiscal matters.

641. As a matter of general practice, foreign agencies which request information from Icelandic authorities must disclose the nature and purpose of their inquiries. If Icelandic authorities are not satisfied with a request from foreign competent authorities, they reserve the right to ask for clarification and additional information to determine if they can or will assist.

642. Iceland appears to have adequate safeguards and controls to ensure that information received by competent authorities is used only in an authorised manner. For example, Iceland has legislation based on EU Directives concerning the protection of personal information. There is also the Data Protection Authority, which is a special agency which enforces the laws, regulations and protection of this information.

643. The only issue that the evaluation team noted was that the complete lack of statistical data (i.e. the number of requests for information received and responded to, the number refused, and the time required to respond) made it difficult to demonstrate the effectiveness of the system.

644. **Law enforcement:** The law enforcement community in Iceland is able to provide international cooperation to their foreign counterparts through a number of fora, including the Schengen Group, Interpol, and Europol and Eurojust channels, as well as direct police to police contact.

645. **FIU:** As a member of the Egmont Group, Iceland's FIU shares information and practices with other international FIUs. The Icelandic FIU is authorised to conduct whatever inquiries are necessary in response to requests from foreign counterparts. Precise statistics on international cooperation (i.e. the number received and responded to, and the time for responding) are not kept. The FIU estimated that there have been approximately 10 requests per year.

646. **Supervisors:** The FSA may also share information with other FSAs within the EEA, however the exchange of information pertaining to supervisory related matters is subject to strict caveats, such as; the obligation to keep this type of information secret. This obligation can only be removed by obtaining the consent of the FSA that provided the information. The FSA has signed MoUs with several foreign financial supervisory authorities regarding the supervision of financial undertakings on a consolidated basis.

647. There are provisions for the FSA to share information with counterparts outside the EEA. However, if the sharing of information is to occur, it must respect the same conditions which apply to the

EEA members; most importantly, they have to respect that the information is to remain secret. In order for the secrecy veil to be lifted, consent has been obtained from the originating agency.

Additional Elements

648. The FIU can obtain information from other competent authorities within Iceland on behalf of their foreign counterparts. There does not appear to be anything which would inhibit this unless, it is contrary to Iceland law.

Recommendation 32[32] (Statistics)

649. Icelandic authorities do not maintain statistics on the number of requests for assistance made or received by law enforcement authorities, the FIU, or supervisors.

6.5.2 Recommendations and Comments

650. Icelandic authorities should maintain statistics on the number of requests for assistance made or received by law enforcement authorities, the FIU, and supervisors including whether the request was granted or refused.

6.5.3 Compliance with Recommendation 40 and Special Recommendation V

	Rating	Summary of factors relevant to s.6.5 underlying overall rating
R.40	**LC**	Given the complete lack of statistical data, the evaluation team was not able to determine that the mechanisms for international cooperation are fully effective.
SR.V	**LC**	(Provisions appear adequate with regard to Rec. 40)

[32] See Section 7.1 for the compliance rating for this Recommendation.

7. Other Issues

7.1 Resources and statistics

651. The text of the description, analysis and recommendations for improvement that relate to Recommendations 30 and 32 is contained in all the relevant sections of the report i.e. all of section 2, parts of sections 3 and 4, and in section 6. There is a single rating for each of these Recommendations, even though the Recommendations are addressed in several sections. Section 7.1 of the report contains the boxes showing the rating and the factors underlying the rating.

	Rating	Summary of factors relevant to Recommendations 30 and 32 and underlying overall rating
R.30	**PC**	<u>The FIU</u> • The number of dedicated staff is not sufficient: the FIU remains a "one person entity" which inhibits its ability to function in an effective manner. • Furthermore, the FIU does not have a sufficient budget or budgetary control. This restricts the unit's ability to make long-term strategic plans, to hire additional resources, to fund training and to buy analytical equipment and software. <u>Law enforcement</u> • There appears to be very little formal training provided to law enforcement personnel, both upon engagement as well as on an ongoing basis regarding AML and CFT investigations. <u>FSA</u> • Considering the number of entities that the FSA is responsible for supervising, its number of staff seems inadequate. It was the view of the evaluation team that adequate staff had not been provided for AML/CFT supervision. • It did not appear that there was yet adequate training on AML/CFT issues.
R.32	**NC**	• Iceland has not reviewed the effectiveness of its systems for combating money laundering and terrorist financing on a regular basis. • There are no comprehensive statistics on the number of STRs analysed and disseminated. • There are no statistics on ML or FT investigations. • Statistics for money laundering prosecutions and convictions were produced; however, there is no system for recording these figures and making them easily available. • No statistics on the number of cases and the amounts of property frozen, seized, and confiscated relating to (i) ML, (ii) FT, and (iii) criminal proceeds. • No statistics on mutual legal assistance and extradition requests (including requests relating to freezing, seizing and confiscation) that are made or received, relating to ML, the predicate offences and FT, including the nature of the request, whether it was granted or refused, and the time required to respond. • No statistics on formal requests for assistance made or received by the FIU, including whether the request was granted or refused; or spontaneous referrals made by the FIU to foreign authorities. • No comprehensive statistics regarding on-site examinations conducted by supervisors relating to or including AML/CFT and any sanctions applied.

TABLES

Table 1: Ratings of Compliance with FATF Recommendations
Table 2: Recommended Action Plan to improve the AML/CFT system
Table 3: Authorities' Response to the Evaluation (if necessary)

Table 1. Ratings of Compliance with FATF Recommendations

The rating of compliance vis-à-vis the FATF Recommendations should be made according to the four levels of compliance mentioned in the 2004 Methodology (Compliant (C), Largely Compliant (LC), Partially Compliant (PC), Non-Compliant (NC)), or could, in exceptional cases, be marked as not applicable (NA).

Compliant	The Recommendation is fully observed with respect to all essential criteria.
Largely compliant	There are only minor shortcomings, with a large majority of the essential criteria being fully met.
Partially compliant	The country has taken some substantive action and complies with some of the essential criteria.
Non-compliant	There are major shortcomings, with a large majority of the essential criteria not being met.
Not applicable	A requirement or part of a requirement does not apply, due to the structural, legal or institutional features of a country e.g. a particular type of financial institution does not exist in that country.

Forty Recommendations	Rating	Summary of factors underlying rating
Legal systems		
1. ML offence	LC	• Arms trafficking insider trading and market manipulation are not crimes in the Penal Code. Therefore, these actions cannot constitute predicate offences for money laundering. • Participation in an organised criminal group or racketeering is not separately criminalised and not a ML predicate offence; ancillary offences do not appear otherwise to cover adequately "participation" in the profit-generating crimes of organised criminal groups—conspiracy is not fully covered. • It is unclear whether self-laundering is adequately criminalised. • The offence is not effectively implemented, as witnessed by the limited number of indictments and convictions.
2. ML offence – mental element and corporate liability	PC	• Penalties appears to be too low, especially in comparison with penalties for similar types of offences (e.g. enrichment offences (6 years)) and do not seem to be effective, proportionate and dissuasive. • Actual penalties applied have been low, even in cases involving narcotics trafficking where a penalty of up to 12 years is available. • Criminal liability of legal persons is very narrow. • The offence is not effectively implemented, as witnessed by the limited number of indictments and convictions.
3. Confiscation and provisional measures	LC	• The high burden of proof lying on prosecutors inhibits effective implementation of the confiscation provisions. • The lack of any data or other information on results does not allow the examiners to be satisfied that the confiscation provisions are effective. • There are some indications in the whole system that confiscation

		of criminal property is treated as a low priority issue.
Preventive measures		
4. Secrecy laws consistent with the Recs.	C	

5. Customer due diligence	PC	• CDD measures are limited to customer identification requirements and not the full range of measures has been effectively implemented (just been introduced in the new MLA).
		• Undertaking CDD measures is not required when carrying out occasional transactions that are wire transfers in circumstances covered by the Interpretative Note to SR VII.
		• There is no general requirement to identify beneficial owners for all customers. Financial institutions are not required to determine actively if the customer is acting on behalf of someone else.
		• There is no supervision of money remittance or money transfer occurring outside of banks and therefore no means to verify if CDD measures are effectively applied.
		• No clear requirements regarding the need to take reasonable measures to understand the ownership and control structure regarding legal persons, nor to verify that the natural person purporting to act on behalf of a legal person or legal arrangement is so authorised;
		• The possibilities for financial institutions to apply no CDD measures are overly broad. There is no assessment to limit the application of such measures to those countries that Icelandic authorities (or financial institutions) are satisfied are in compliance with and have effectively implemented the FATF Recommendations.
		• No requirement to terminate the business relationship and to consider making a suspicious transaction report when the identification cannot be performed properly after the business relationship has commenced.
		• There are no general requirements to apply CDD measures (other than on-going due diligence) to existing customers on the basis of materiality and risk.
		• A series of obligations have just come into force and therefore have not yet been effectively implemented:
		  • conducting CDD when there is a suspicion of terrorist financing or when there are doubts about the veracity or adequacy of previously obtained customer identification data;
		  • the requirements on the verification of the identity of a legal person or arrangement;
		  • CDD requirements regarding the beneficial owner of legal persons, including the requirement to determine the natural persons who ultimately own or control the legal person;
		  • the obligation to obtain information on the purpose and intended nature of the business relationship;
		  • enhanced CDD legislation for higher risk categories of customers, business relationships or transactions;
		  • the requirement to stop the financial institution from opening an account, commence business relations or performing the transaction when it is unable to identify the beneficial owner satisfactorily.

6. Politically exposed persons	NC	• Iceland has not implemented any AML/CDD measures regarding

		the establishment and maintenance of customer relationships with politically exposed persons (PEPs). Provisions in the new MLA will enter into force in 2007.
7. Correspondent banking	PC	• There are no requirements applicable to banking relationships with institutions in EEA countries. • There is no requirement to ascertain that the respondent institution's AML/CFT controls are adequate and effective and, regarding payable through accounts, to be satisfied that the respondent has performed all normal CDD obligations. Regarding the latter, this is limited to the obligation to identify/verify the customer and to perform ongoing due diligence. • Measures regulating correspondent relationships have just been adopted and are not yet effectively implemented.
8. New technologies & non face-to-face business	LC	• The requirement for financial institutions to have policies in place or take such measures as may be needed to prevent the misuse of technological developments in ML or TF schemes is only partially covered. • The requirement to acquire additional information on the customer "when needed" is an open provision which needs further regulation or guidelines to make it effective.
9. Third parties and introducers	PC	• Certain requirements concerning reliance on third parties in practice are unenforceable, in case of a third party outside Iceland, since the obligations are placed on the third party to provide information upon request. • Financial institutions are not required to take adequate steps to satisfy themselves that copies of the relevant documentation will be made available from the third party upon request without delay. • There is no requirement that the financial institution must be satisfied that the third party is regulated and supervised and has measures in place to comply with the CDD requirements. In determining in which countries the third party that meets the conditions can be based, competent authorities do not take into account information available on whether those countries adequately apply the FATF Recommendations.
10. Record keeping	C	
11. Unusual transactions	LC	• The requirement to examine as far as possible the background and purpose of the transaction is not dealt with explicitly in the legislation and only partly covered in the explanatory notes. • The monitoring requirements for insurance and securities intermediaries are new and not yet fully implemented.
12. DNFBP – R.5, 6, 8-11	PC	• Similar deficiencies for CDD that apply to financial institutions (See ratings boxes for Recommendation 5) also apply to DNFBPs. • At the time of the on-site visit, real estate agents and traders in precious metals and gems did not appear adequately aware of existing AML requirements. • There are no requirements for PEPs in force—the requirements in the new law will enter into force until 1 January 2007. There will not be a requirement to obtain senior management approval to continue the business relationship, where a customer has already been accepted and the customer or beneficial owner is subsequently found to be, or subsequently becomes a PEP. • The requirement to have policies in place or take such measures as may be needed to prevent the misuse of technological developments in ML or TF schemes is only partially covered.

		The requirement to acquire additional information on the customer "when needed" is an open a provision which needs further regulation or guidelines to make it effective. • Certain rules for reliance on 3rd party introducers are unenforceable. For DNFBPs relying on a third party there is not a general requirement that the DNFBP be satisfied that the third party is regulated and supervised and has measures in place to comply with the CDD requirements. • The provisions have just begun applying to the full range of DNFBPs and have not yet been put effectively into practice.
13. Suspicious transaction reporting	PC	• The reporting obligation does not cover transactions related to insider trading/marked manipulation, arms trafficking, participation in an organised criminal group (or otherwise fully cover this through conspiracy) as these are not predicate offences for money laundering in Iceland. • The clear obligation to report an STR related to terrorist financing has just been adopted in June 2006; its effectiveness cannot yet be assessed. • There are some concerns about the effectiveness of the system: the insurance and securities sectors have not filed an STR; exchange offices have not filed STRs (and are not subject to supervision). • There has been little guidance given to reporting entities on the form and manner of reporting, and there have been few results shown from the increased reporting.
14. Protection & no tipping-off	C	
15. Internal controls, compliance & audit	PC	• Neither the MLA 1999 nor the AML/CFT Act 2006 includes rules on the subjects that the internal controls should cover. • There is no requirement that the AML compliance officer and other appropriate staff have timely access to CDD, transaction, and other relevant information. • There is no specific requirement to maintain an adequately resourced and independent audit function to test compliance (including sample testing) with AML/CFT procedures, policies and controls. • The training requirements do not specify that the training programs be on-going so as to be kept informed of new developments, or specify that they should cover ML and FT techniques, methods and trends. • There are some preliminary concerns about how effectively internal controls have been implemented. For instance, there is no legal obligation to implement internal controls to ensure that full CDD is performed. • The requirement for all financial institutions to have a compliance officer at the managerial level is new and not yet fully implemented.
16. DNFBP – R.13-15 & 21	PC	• The reporting obligation does not cover transactions related to insider trading, market manipulation, arms trafficking, and participation in an organised criminal group, as these are not predicate offences for money laundering in Iceland. • There is a concern that this broad secrecy requirement for lawyers might conflict with the obligation to report. • It is not required that the compliance officer and other appropriate staff have timely access to CDD, transaction, and other relevant information. There is no requirement to maintain an adequately

		resourced and independent audit function to test compliance (including sample testing) with AML/CFT procedures, policies and controls. • In addition, the training requirements do not specify that the training programs be on-going so as to be kept informed of new developments, or specify that they should cover ML and FT techniques, methods and trends. • DNFBPs would not receive the notices and instructions issued by the FSA if there is a need for special caution in transactions with a state or region. • There are no provisions dealing with the possibility to apply appropriate counter-measures where a country continues not to apply or insufficiently applies the Recommendations. • The provisions have just begun applying to the full range of DNFBPs and have not yet been put effectively into practice.
17. Sanctions	PC	• It is not clear in the MLA 1999 whether sanctions can be applied to the directors and senior management of the FI that was responsible for the violation by the FI. Under the AML/CFT Act 2006, criminal sanctions would not be available for directors or senior management of financial institutions. • There are concerns about the effectiveness of these criminal sanctions since no such sanction has ever been applied for a violation of any version of the money laundering act (dating back to 1993). • The range of administrative sanctions is not sufficiently broad. There are no administrative penalties which can be imposed against directors and controlling owners of financial institutions directly for AML/CFT breaches, only indirectly by not meeting fit and proper criteria. Sanctions for other senior managers appear more limited. The available sanctions do not include the possibility to directly bar persons from the sector, unless they are convicted of an offence. There is not the general possibility to restrict or revoke a license for AML/CFT violations. • Administrative sanctions for AML/CFT have not yet been effectively applied.
18. Shell banks	C	
19. Other forms of reporting	C	
20. Other NFBP & secure transaction techniques	C	
21. Special attention for higher risk countries	LC	• The requirement to examine as far as possible the background and purpose of such transactions is not dealt with explicitly in the legislation and only partly covered in the explanatory notes. • No provisions regulating application of counter-measures.

22. Foreign branches & subsidiaries	PC	• There are no requirements for branch/subsidiaries in EEA countries (the vast majority of foreign activities of Icelandic financial institutions)—without any assessment of the particular AML/CFT risk of that country—to:
		  • apply AML/CFT rules consistent with the Icelandic standard.
		  • pay particular attention that this principle is observed with respect to their branches and subsidiaries in countries within the EEA which do not or insufficiently apply the FATF Recommendations.
		  • inform the FSA if its foreign branch or subsidiary is unable to

		observe appropriate AML/CFT measures because this is prohibited by the laws or regulations of the host country. • There is no requirement that foreign branches or subsidiaries (either within or outside EEA countries) observe Icelandic standards for AML/CFT other than for CDD. • Where the AML/CFT standards differ, there is no requirement to apply the higher AML/CFT standards. • The obligations that do exist are new and have not yet been put effectively into practice; there has not yet been adequate focus on the issue within the FSA.
23. Regulation, supervision and monitoring	PC	• The AML Regulation in place at the time of the on-site visit did not cover insurance/securities intermediaries. • While fit and proper tests apply for directors and board members, they do not apply to other senior management. • There is no general requirement for money or value transfer services to be licensed or registered. • Money value transfer services and money exchange services are not subject to any system for monitoring and ensuring compliance with the AML/CFT requirements. • At on-site inspections, it is normal procedure to not make spot checks of how institutions carry out the mandatory customer identification checks. • At the time of the on-site visit, financial institutions were not subject to adequate supervision of compliance with CFT requirements. • There are concerns about how effectively the financial sector has been supervised regarding AML/CFT; while the FSA indicated that AML/CFT assessments of financial institutions are part of regular visits, the very limited findings – and number of warnings – indicates that the focus on AML/CTF has been inadequate.
24. DNFBP - regulation, supervision and monitoring	NC	• There is no system for effective monitoring and ensuring compliance with AML/CFT requirements for DNFBPs.
25. Guidelines & Feedback	NC	• Competent authorities have not established guidelines that will assist financial institutions or DNFBPs to implement and comply with STR requirements. • The activity initiated by the authorities has so far been very limited in order to provide feedback. There is only basic specific feedback and no substantive general feedback such as statistics on the number of disclosures and results, information on techniques, methods and trends, or sanitised case examples.
Institutional and other measures		
26. The FIU	PC	• Overall, the FIU does not appear to be effectively addressing AML/CFT issues. • At the time of the on-site visit, the FIU did not have sufficient structural or operational independence. • Insufficient human and financial resources to effectively perform FIU functions. • The FIU staffing, activities, and results have not increased despite a large increase in the financial sector, drug trafficking crimes, and STRs. • Limited AML/CFT training provided to FIU personnel.

		• There has been no written guidance or forms to reporting entities. • No annual public reports concerning FIU activities, typologies or AML/CFT trends analysis have yet been issued. • There is no standardised or uniform process for reporting STRs.
27. Law enforcement authorities	LC	• Overall it did not appear that investigation and prosecution authorities adequately pursued money laundering cases. • AML/CFT training is inadequate, and there is no mechanism in place to ensure that those who investigate/prosecute ML remain current in their knowledge and experience.
28. Powers of competent authorities	C	
29. Supervisors	LC	• No supervisory powers exist for financial institutions not under FSA's supervision, such as foreign exchange companies or foreign remittance dealers that may operate outside of banks. • While there is a range of sanctions available, the range is not sufficiently broad. There are no administrative penalties which can be imposed against directors and controlling owners of financial institutions directly for AML/CFT breaches, only indirectly by not meeting fit and proper criteria. Available sanctions for other senior management appear more limited. The available sanctions do not include the possibility to directly bar persons from the sector, unless they are convicted of an offence. In addition, there is not the general possibility to restrict or revoke a license for AML/CFT violations.
30. Resources, integrity and training	PC	<u>The FIU</u> • The number of dedicated staff is not sufficient: the FIU remains a "one person entity" which inhibits its ability to function in an effective manner. • Furthermore, the FIU does not have sufficient budget or budgetary control. This restricts the unit's ability to make long-term strategic plans, to hire additional resources, to fund training and to buy analytical equipment and software. <u>Law enforcement</u> • There appears to be very little formal training provided to law enforcement personnel, both upon engagement as well as on an ongoing basis regarding AML and CFT investigations. <u>FSA</u> • Considering the number of entities that the FSA is responsible for supervising, its number of staff seems inadequate. It was the view of the evaluation team that adequate staff had not been provided for AML/CFT supervision. • It did not appear that there was yet adequate training on AML/CFT issues.
31. National co-operation	C	
32. Statistics	NC	• Iceland has not reviewed the effectiveness of its systems for combating money laundering and terrorist financing on a regular basis. • There are no comprehensive statistics on the number of STRs analysed and disseminated. • There are no statistics on ML or FT investigations. • Statistics for money laundering prosecutions and convictions were produced; however, there is no system for recording these figures and making them easily available.

		• No statistics on the number of cases and the amounts of property frozen, seized, and confiscated relating to (i) ML, (ii) FT, and (iii) criminal proceeds. • No statistics on mutual legal assistance and extradition requests (including requests relating to freezing, seizing and confiscation) that are made or received, relating to ML, the predicate offences and FT, including the nature of the request, whether it was granted or refused, and the time required to respond. • No statistics on formal requests for assistance made or received by the FIU, including whether the request was granted or refused; or spontaneous referrals made by the FIU to foreign authorities. • No comprehensive statistics regarding on-site examinations conducted by supervisors relating to or including AML/CFT and any sanctions applied.
33. Legal persons – beneficial owners	PC	• Access to beneficial ownership does not appear to be available in an adequately timely fashion for Icelandic companies or foundations. • No beneficial ownership information for foreign companies is available. • Even though any change of managers and directors has to be notified to the Register, the Tax Directorate in practice does not perform any further inquiry to verify this. • Nominee directors are allowed.
34. Legal arrangements – beneficial owners	NA	
International Co-operation		
35. Conventions	PC	<u>Vienna Convention</u> • Conspiracy to commit ML offences is not fully covered. <u>CFT Convention</u> • The scope of "terrorist act" does not fully cover all the acts defined in Article 2 (1), and there is a concern that the financing of a terrorist act as defined in the legislation. • Iceland's implementation of Recommendation 5 does not include adequate measures to ascertain the identity of beneficial owners. <u>Palermo Convention:</u> • Iceland has not ratified the Palermo Convention. • Key elements of the Convention are not yet implemented: Participation in organised criminal group is not criminalised; nor is conspiracy to commit money laundering and other crimes fully covered so as to otherwise adequately criminalise "participation" in the crimes commitment by organised criminal groups. • It is unclear whether self-laundering (as required by Article 6(2)(e)) is covered. There do not appear to be effective, proportionate, and dissuasive sanctions for ML. • Iceland's implementation of Recommendation 5 does not include adequate measures to ascertain the identity of beneficial owners.
36. Mutual legal assistance (MLA)	LC	• Since it is not clear if self-laundering is covered, conspiracy to commit money laundering is not fully criminalised, and not all predicate offences are fully covered, it is unclear how effectively Iceland could provide assistance relating to these cases. • Legal provisions on mutual legal assistance would not encourage or facilitate the voluntary appearance of witnesses or persons providing information to the requesting country, as this seems to

		be out of the scope of Act 13/1984. • The limitations on the scope of "acts of terrorism" as defined in Iceland also present some concerns about Iceland's ability to effectively provide assistance in cases involving the financing of acts not defined as terrorist acts in Iceland. • Effectiveness of the current laws cannot be demonstrated due to the lack of quantitative and qualitative data. There is no evidence of how expeditiously requests are answered.
37. Dual criminality	PC	• Dual criminality would still apply to requests for less intrusive and non-compulsory measures such as company commercial records or other publicly available information.
38. MLA on confiscation and freezing	LC	• Since it is not clear if self-laundering is covered, conspiracy to commit money laundering is not fully criminalised, and not all predicate offences are fully covered, it is unclear how effectively Iceland could provide assistance relating to these cases. • Foreign judgments cannot be executed if the person is not domiciled in Iceland. • Iceland has not considered authorising the sharing of confiscated assets when confiscation is directly or indirectly a result of co-ordinated law enforcement action. Icelandic authorities have not considered establishing an asset forfeiture fund.
39. Extradition	LC	• Since it is not clear if self-laundering is covered, and conspiracy to commit money laundering and all the required predicate offences are not fully covered, it is not clear how effectively Iceland could extradite relating to these offences.
40. Other forms of co-operation	LC	• Given the complete lack of statistical data, the evaluation team was not able to determine that the mechanisms for international cooperation are fully effective.
Nine Special Recommendations	**Rating**	**Summary of factors underlying rating**
SR.I Implement UN instruments	PC	<u>CFT Convention</u> • The scope of "terrorist act" does not fully cover all the acts defined in Article 2 (1), and there is a concern that the financing of a terrorist act as defined in the legislation is not fully covered. Iceland's implementation of Recommendation 5 does not include adequate measures to ascertain the identity of beneficial owners. <u>S/RES/1267</u> • There are no formal procedures for authorising access to frozen resources when deemed necessary for basic expenses, the payment of certain types of fees, etc pursuant to S/RES/1452(2002). <u>S/RES/1373</u> • Iceland does not have an adequate mechanism to implement S/RES/1373. There is not a comprehensive mechanism in place to examine and give effect to actions initiated under the freezing mechanisms of other jurisdictions. • The Public Announcement's definition of terrorism and all subsequent obligations are limited to certain violent acts in the Penal Code—it does not fully cover all persons who commit or attempt to commit terrorist acts. • The Public Announcement does not specifically cover funds of entities that are *controlled directly or indirectly* by such persons. Nor does it cover funds or other assets derived or generated from

		funds or other assets owned or controlled directly or indirectly by designated persons, terrorists, those who finance terrorism, or terrorist organisations. • The direct obligation to freeze funds pursuant to designations in the context of S/RES/1373 is contained Sec 16(a) of the revised Law 87/1998 which does not apply to entities not supervised by the FSA, such as money exchange and money transfer and non financial business and professionals • Iceland has not fully implemented the CFT Convention as required by S/RES/1373.
SR.II Criminalise terrorist financing	LC	• Financing of a terrorist act directly is not specifically covered by Sec. 100(b), although it appears most cases would be covered by other provisions. • The definition of "acts of terrorism" does not fully cover all those activities Article 2, par.1 of the CFT Convention; the financing of acts not specifically designated as terrorist acts in the Penal Code (but within the Annexes of the Convention) would not be criminal acts in Iceland. • The need to show that the act was committed for the purpose of intimidation/coercion, and the need to show that the act could damage a state or international establishment further limits the scope of FT offences and their effectiveness.
SR.III Freeze and confiscate terrorist assets	NC	• Overall, Iceland does not have effective laws and procedures to give effect to freezing designations in the context of S/RES/1373. • There is not a national mechanism to designate persons in the context of S/RES/1373, nor a comprehensive mechanism in place to examine and give effect to actions initiated under the freezing mechanisms of other jurisdictions. • The Public Announcement's definition of terrorism and all subsequent obligations are limited to certain violent acts in the Penal Code, which do not fully cover all persons who commit or attempt to commit terrorist acts. • There is not a mechanism to enforce the freezing obligation for designations in the context of S/RES/1373, if any were made, for entities that are not supervised by FSA, such as money exchange and money transfer and non-financial business and professionals. • The freezing obligation in Law 87/1998 allows only for the FSA to forward lists pursuant to international obligations. As a practical matter, the only lists that can be enforced are those from the 1267 designation committee. • The Announcement implementing S/RES/1373 does not cover fully freezing funds associated with terrorism, etc; nor does it not specifically cover funds of entities that are *controlled directly or indirectly* by such persons, nor funds or other assets derived or generated from funds or other assets owned or controlled directly or indirectly by designated persons, terrorists, those who finance terrorist, or terrorist organisations. • It is not required that action take place without delay and without prior notice to the persons involved. • There are no formal procedures at national level for evaluating de-listing requests, for releasing funds or other assets of persons or entities erroneously subject to the freezing and for authorising access to frozen resources when deemed necessary for basic expenses, the payment of certain types of fees, etc pursuant to S/RES/1452(2002).

		• No specific measures to protect the rights of bona fide third parties consistent with Article 8 of the CFT Convention. • Even though the freezing obligation is already in place for financial institutions concerning persons and entities on the lists distributed by the FSA, no practical indications have been released to clarify related duties and responsibilities.
SR.IV Suspicious transaction reporting	LC	• The clear obligation to report an STR related to terrorist financing was adopted in June 2006; its effectiveness cannot be assessed yet. • Some concerns raised above in Recommendation 13 about the effectiveness of the reporting system apply equally to SR IV.
SR.V International co-operation	LC	• Since dual criminality applies, the limitations on the scope of "acts of terrorism" as defined in Iceland also present some concerns about Iceland's ability to effectively provide assistance in legal assistance and extradition cases involving the financing of acts not defined as terrorist acts in Iceland. • Foreign judgments cannot be executed if the person is not domiciled in Iceland.
SR VI AML requirements for money/value transfer services	NC	• There are currently no requirements to license or register natural and legal persons that perform money or value transfer services (MVT operators). • There is no authority that maintains a list of names and addresses of such operators. • The deficiencies regarding the extent of CDD and other AML/CFT requirements apply also to MVT operators. • MVT operators are not required to maintain a current list of their agents which must be made available to the designated competent authorities. • The evaluation team had serious concerns regarding supervision, since there is no mechanism for monitoring and ensuring compliance with the FATF Recommendations, including the practical inability to apply sanctions for AML/CFT deficiencies. • Sanctions for failure to comply with the other obligations of SR VI would not be available.
SR VII Wire transfer rules	NC	• Iceland has not implemented any requirement regarding obtaining and maintaining information with wire transfers.
SR.VIII Non-profit organisations	NC	• Iceland has not yet reviewed the adequacy of domestic laws and regulations that relate to non-profit organisations (NPOs) vis-à-vis terrorist financing. • It is unclear if there is adequate access to information so as to identify the features and types of NPOs, especially non-commercial foundations, at risk for terrorist financing purposes. • Iceland has not yet undertaken outreach to the NPO sector. • It is not clear that detailed information on the administration and management of non-commercial foundations is available during the course of an investigation with regard to non-commercial foundations. • Non-commercial foundations are not required to maintain information on the purpose and objectives of their stated activities. • There are not adequate measures in place to sanction violations of oversight measures or rules by NPOs or persons acting on behalf of NPOs, especially with regard to non-commercial foundations. • Iceland has not identified specific points of contacts and procedures to respond to international requests for information

		regarding particular NPOs that are suspected of terrorist financing or other forms of terrorist support.
SR.IX Cross Border Declaration & Disclosure	PC	• The assessment team did not view that the current system for detecting and preventing cross border movements of currency or bearer negotiable instruments related to money laundering or terrorist financing is effective. No currency declaration had yet been made. • The requirement to declare bearer negotiable instruments does not appear adequately addressed in the law or in guidance to the public. • The system authorises, but does not require, the customs to create separate customs clearance channels, and therefore the mechanism to declare does not apply everywhere. • There is no practical mechanism in place for declaring outgoing currency movements. • There are no specific criminal sanctions available for persons who carry out a physical cross-border transportation of currency or bearer negotiable instruments that are related to terrorist financing or money laundering contrary to the obligations under SR IX. • There are no specific requirements that at a minimum, information on the amount of currency declared or otherwise detected, and the identification data of the bearer(s) shall be retained for use by the appropriate authorities in instances when: (a) a declaration which exceeds the prescribed threshold is made; (b) where there is a false declaration/disclosure; or (c) where there is a suspicion of money laundering or terrorist financing.

Table 2: Recommended Action Plan to Improve the AML/CFT System

AML/CFT System	Recommended Action (listed in order of priority)
1. General	
2. Legal System and Related Institutional Measures	
2.1 Criminalisation of Money Laundering (R.1 & 2)	• Iceland should fully cover all the necessary predicate offences for money laundering, and conspiracy should be fully criminalised. Review domestic laws, and if necessary, adjust them to ensure that self-laundering is fully criminalised. • Consider lowering the standard of proof to demonstrate the mens rea in the money laundering offence by allowing prosecutors and lower courts to adopt a full range of mental element including every degree of knowledge. • Specific training on money laundering investigations jointly with clear guidance by prosecutors on evidence requirements under Sec. 264 should be delivered to officials from law enforcement authorities. • Raise the criminal penalties for money laundering, to be in line with those of other profit-generating offences in Iceland. • Criminal liability of legal persons for money laundering offence should be expanded and extended to any predicate offence.
2.2 Criminalisation of Terrorist Financing (SR.I)	• Review the legislation to ensure that the financing of terrorist acts directly is included in the FT offence. • Broaden the definition of terrorist act to include all those activities referred to by Article 2 (1)(a) and (b) of the CFT Convention. • Remove the purpose elements—i.e., the need to demonstrate that the act occurred for the purpose of intimidating/coercing of a government, etc, and the need that the act also to be able to damage a State or international establishment in order for acts under the Convention to be valid FT offences.
2.3 Confiscation, freezing and seizing of proceeds of crime (R.3)	• Provisions on confiscation should be strengthened especially when the offender is not in possession of the assets, which are held by a third party. • Consider measures that require confiscation of property held by a perpetrator convicted of a serious offence generating profit, unless the offender can prove that the property was legally obtained (reversal of burden of proof). • Consider reducing the burden of proof when executing a forfeiture order after conviction, e.g. by adopting "a balance of probabilities approach" or other standard lower than the criminal standard. • Give higher priority to confiscation of criminal property.
2.4 Freezing of funds used for terrorist financing (SR.III)	• Establish a central authority at national level to examine, integrate and update the received lists of persons and entities suspected to be linked to international terrorism before sending them to the financial sector. • A domestic mechanism to enact S/RES/1373(2001) should be implemented to be able to designate terrorists at a national

	level as well as to give effect to designations and requests for freezing assets from other countries. • Adopt procedures for evaluating de-listing requests, for releasing funds or other assets of persons or entities erroneously subject to the freezing and for authorising access to frozen resources pursuant to S/RES/1452(2002). • Release practical guidance to the financial institutions concerning their responsibilities under the freezing regime as well as for the reporting of suspicious transactions that may be linked to terrorist financing. • The direct obligation to freeze funds of persons and entities designated in the context of S/RES/1373 applies only to financial institutions supervised by FSA. This should be broadened to apply to all financial institutions and DNFBPs.
2.5 The Financial Intelligence Unit and its functions (R.26)	• Improve the structural and operational independence of the FIU by fully implementing the new Regulation 626/2006. • Secure an increased level financial and human resources to enhance its ability to effectively perform the functions of an FIU. • Develop written guidance and direction to reporting entities concerning the manner of reporting STRs. • Develop a standardised STR reporting format for all reporting entities. • Initiate proactive analysis of STRs and police data to enhance the effectiveness of targeting entities involved in suspected ML and FT. • Increase international cooperation between the FIU and other international partners through more active participation in the Egmont Group. • Produce annual reports on trends and typologies (as required in the new regulation 626/2006). • Develop educational programs for the public on AML/CFT issues. • Pursue training and educational opportunities for FIU personnel, the financial sector and other police agencies. (The training issues could be pursued through the Training Working Group of the Egmont Group). • The FIU should consider taking measures regarding the "disaster recovery" of their database. Consideration should be given to having the system automatically back-up the information at regular intervals with the back-up information being stored off site.
2.6 Law enforcement, prosecution and other competent authorities (R.27 & 28)	• Take a more proactive approach to investigating and prosecuting money laundering. • More frequent and in-depth training should also be provided to law enforcement and prosecution personnel.
2.7 Cross Border Declaration & Disclosure	• Implement a system to comprehensively address the remaining requirements in SR IX. There should be a system that applies more explicitly to bearer negotiable instruments. • Provide additional guidance so as to better inform arriving and departing passengers about their obligations to make a declaration. • Implement procedures for declaring or disclosing outgoing movements of currency or bearer negotiable instruments. • Adopt criminal sanctions for persons who transport currency

	that is related to money laundering or terrorist financing. • Authorities should ensure that, at a minimum, information on the amount of currency declared or otherwise detected, and the identification data of the bearer(s) is retained for use by the appropriate authorities in instances when: (a) a declaration which exceeds the prescribed threshold is made; (b) where there is a false declaration/disclosure; or (c) where there is a suspicion of money laundering or terrorist financing. • Consider the implementation of new investigative techniques and methods similar to those outlined in the Best Practices Paper for SR IX, e.g. canine units specifically trained to detect currency. • Customs officials should also consider working more closely with the Icelandic FIU and other law enforcement authorities to develop typologies, analyse trends and develop protocols for the sharing of information amongst themselves to more effectively combat cross border ML and FT issues.
3. Preventive Measures: Financial Institutions	
3.1 Risk of money laundering or terrorist financing	
3.2 Customer due diligence, including enhanced or reduced measures (R.5 to 8)	*Recommendation 5:* Iceland should implement the following elements from Recommendation 5 which have not been fully addressed: • Money exchange and money or value transfer should be fully and effectively brought under AML/CFT regulation and especially under customer due diligence requirements. • Financial institutions should be required to undertake CDD measures when carrying out occasional transactions that are wire transfer in circumstances covered by the Interpretative Note to SR VII. • The provisions regarding obtaining information concerning the legal person or arrangement should be extended to information concerning the directors and provisions regulating the power to bind the legal person or arrangement. • There should be a more general requirement to identify beneficial owners for all customers. The financial institution should be required to actively determine if the customer is acting for someone else and it should take reasonable steps to obtain sufficient identification data to verify the identity of the third person. Furthermore, reasonable measures should be taken to understand the ownership and control structure of the legal person. It should be made clear what is expected from the sector. • There should be some consideration/assessment made based on which there is a satisfaction about compliance with the Recommendations by countries which are currently seen as compliant without any doubt. • Rules regulating the CDD treatment of existing customers should be introduced. Several new requirements just introduced with the new AML/CFT Act on 22 June 2006 should be now be effectively put into practice:

	• The requirement to undertake CDD measures in cases where there is a suspicion of terrorist financing and in cases where there are doubts about the veracity or adequacy of previously obtained customer identification data. • Rules on the verification of the identity of legal persons. • The requirements regarding identification and verification of the beneficial owner for legal persons, including the obligation to determine the natural persons who ultimately own or control the legal person. • The obligation to obtain information on the purpose and intended nature of the business relationship. • Performing enhanced due diligence on higher risk categories of customers, business relationships or transactions. • In case of applying simplified or reduced due diligence there has been introduced a basic identification regime instead of no customer identification regime at all, but practice has to pick it up in an effective manner. • When regulating the identification and verification of beneficial owners, a requirement to stop the financial institution from opening an account, commence business relations or performing transactions when it is unable to identify the beneficial owner satisfactorily. • The requirement to terminate the business relationship and to consider making a suspicious transaction report when identification of the customer cannot be performed properly after the relationship has commenced. *Recommendations 6-8:* • Implement the necessary requirements pertaining to PEPs. • With regard to correspondent banking, financially institutions should be required to determine that the respondent institution's AML/CFT controls are adequate and effective, and regarding payable through accounts, to be satisfied that the respondent has performed all normal CDD obligations. • Iceland should clarify the requirement to establish policies and procedures to address any specific risks associated with non-face to face business relationships or transactions.
3.3 Third parties and introduced business (R.9)	• Clarify that the financial institution is required to take adequate steps to satisfy itself that copies of the relevant information will be made available upon request without delay. • Some kind of risk assessment should take place to establish that third parties from outside Iceland actually meet the mentioned conditions.
3.4 Financial institution secrecy or confidentiality (R.4)	
3.5 Record keeping and wire transfer rules (R.10 & SR.VII)	• Iceland should issue the regulation to implement the requirements of Special Recommendation VII as planned.
3.6 Monitoring of transactions and relationships (R.11 & 21)	• The scope of the requirement to pay special attention to all complex, unusual large transactions or unusual patterns of transactions that have no apparent or visible economic or lawful purpose should be now be put effectively into practice for insurance and securities intermediaries, as obligations for these entities are new.

	• The requirement to examine the background and purpose of the transaction needs to be clearly and effectively implemented. • Regarding Recommendation 21, it is recommended to implement provisions dealing with the application of appropriate counter-measures where countries continue not to apply or insufficiently apply the Recommendations.
3.7 Suspicious transaction reports and other reporting (R.13-14, 19, 25 & SR.IV)	• Iceland should ensure that non-bank financial institutions, including money exchange and MVTS providers, are properly supervised so as to comply with their reporting obligations. • Steps should also be taken to refocus reporting in general to concentrate more on the nature of the transaction. • Comprehensive guidelines should be given to the financial sector which should be direct and broad and based on the different typologies, trends and techniques that focus more attention on the nature of transactions themselves. • Additional guidelines that are more tailored to particular types of financial institutions should also be issued. • The FIU should also deliver more specific feedback to reporting entities, particularly concerning the status of STRs and the outcome of specific cases.
3.8 Internal controls, compliance, audit and foreign branches (R.15 & 22)	• Reporting FIs should be obligated to implement satisfactory internal controls with respect to audit functions for AML/CFT. • It should be clarified that the compliance officer should have timely access to CDD and other records, and that financial institutions should provide on-going training programs. • Iceland should also implement comprehensive obligations for all foreign branches and subsidiaries to observe full AML/CFT measures consistent with Icelandic requirements and the FATF Recommendations to the extent that host country laws and regulations permits and that the branches and subsidiaries should apply the higher standard, where the AML/CFT standards differ. Iceland should also implement a requirement that a financial institution inform the FSA if its foreign branch or subsidiary in an EEA country is unable to observe appropriate AML/CFT measures because this is prohibited by the laws or regulations of the host country.
3.9 Shell banks (R.18)	
3.10 The supervisory and oversight system - competent authorities and SROs. Role, functions, duties and powers (including sanctions) (R.23, 29, 17 & 25)	• *Recommendation 17:* The range of administrative sanctions should be broadened for directors and senior management of financial institutions, to include the more direct possibility to bar persons from the sector, to be able to more broadly replace or restrict the powers of managers, directors, or controlling owners for AML/CFT breaches. • There should be the possibility to restrict or revoke a license for AML/CFT violations. • *Recommendation 23:* In general, the FSA should give more attention to AML/CFT matters. • While fit and proper tests apply for directors and board members, they should also apply to other senior management. • There should be a general requirement for money or value transfer services to be licensed or registered. Money value transfer services and money exchange services that operate outside of banks should also be made subject to a system for

	monitoring and ensuring compliance with the AML/CFT requirements. • Iceland should now ensure that AML/CFT assessments of Reporting FIs occur more regularly, particularly in high risk institutions. • *Recommendation 25:* The FSA and other authorities should complete and issue comprehensive AML/CFT guidance for the whole private sector covered by the obligations. • *Recommendation 29:* Icelandic authorities should give adequate powers to a designated authority to adequately supervise unlicensed financial institutions such as foreign exchange companies or foreign remittance dealers that may operate outside of banks. • *Recommendation 30:* The FSA should be given additional resources to be allocated for AML/CFT supervision. • The FSA should consider creating a well staffed stand alone AML/CFT unit or at least a team of examiners specialising in AML/CFT measures that check FIs compliance with AML/CFT on an on-going basis for all supervised entities.
3.11 Money value transfer services (SR.VI)	• Iceland should implement the measures in SR.VI. • Iceland should require all money or value transfer services (MVT operators) to be licensed or registered, maintain a list of such operators, and adopt a mechanism to adequately monitor and ensure compliance with the FATF Recommendations.
4. Preventive Measures: Non-Financial Businesses and Professions	
4.1 Customer due diligence and record-keeping (R.12)	• Iceland should adopt and fully implement the full range of CDD measures, as discussed in section 3.2 and 3.3 of this report, so as to also apply to DNFBPs. Iceland should fully implement the new measures that apply to DNFBPs.

4.2 Suspicious transaction reporting (R.16)	• Iceland should undertake the following actions to fully implement Recommendation 16:
	  • Overall, the measures in the new legislation should be fully and effectively implemented.
	  • DNFBPs should be made fully aware of their reporting obligations under the new legislation.
	  • DNFBPs should be made aware of their duty to give special attention to business relationships and transactions with (legal) persons from countries which do not or insufficiently apply the FATF Recommendations, in line with Recommendation 21.
	  • Measures should be taken to ensure that DNFBPs are advised of concerns about weaknesses in the AML/CFT systems of other countries.
	  • DNFBPs should be required to have training programs that are on-going so as to be kept informed of new developments.

4.3 Regulation, supervision and monitoring (R.24-25)	• Designate an authority, authorities, or SROs responsible for monitoring and ensuring compliance with the requirements of the AML/CFT Act 2006. • The authority/authorities should be provided adequate powers and sufficient technical resources to perform its/their functions. • The authorities and/or SROs should also issue adequate

	guidance on AML/CFT requirements to all DNFBP sectors.
4.4 Other non-financial businesses and professions (R.20)	
5. Legal Persons and Arrangements & Non-Profit Organisations	
5.1 Legal Persons – Access to beneficial ownership and control information (R.33)	• Access to information on beneficial ownership of legal persons should be made more accurate and up to date. • The Tax Directorate could play a larger role in verifying beneficial ownership/control for the applications it receives.
5.2 Legal Arrangements – Access to beneficial ownership and control information (R.34)	
5.3 Non-profit organisations (SR.VIII)	• Review the adequacy of the legal framework that relates to NPOs vis-à-vis terrorist financing and ensure that there is adequate access to information so as to identify the features and types of NPOs at risk for terrorist financing purposes. • Reach out to the NPO sector with a view to protecting the sector from terrorist financing abuse. This outreach should include i) raising awareness in the NPO sector about the risks of terrorist abuse and the available measures to protect against such abuse; and ii) promoting transparency, accountability, integrity, and public confidence in the administration and management of all NPOs. • In general, take more proactive steps to promote effective supervision or monitoring of those NPOs. • Authorities should ensure that detailed information on the administration and management of non-commercial foundations is available during the course of an investigation. • Implement an effective sanction regime for violations of oversight measures or rules by NPOs or persons acting on behalf of NPOs.
6. National and International Co-operation	
6.1 National co-operation and coordination (R.31)	• Continue the AML/CFT policy coordination now that the AML/CFT legislation has entered into force.
6.2 The Conventions and UN Special Resolutions (R.35 & SR.I)	• Iceland should more fully implement the CFT Convention. • The definition "terrorist act" should be broadened to fully cover all of the acts defined in Article 2 (1) of the Convention. • More comprehensive measures for identifying beneficial owners should also be adopted. • Iceland should also institute adequate comprehensive conspiracy provisions for money laundering.
6.3 Mutual Legal Assistance (R.36-38 & SR.V)	• Enact provisions on mutual legal assistance that would encourage or facilitate the voluntary appearance of witnesses or persons providing information to the requesting country. • Clarify the procedures to allow non-coercive measures to be applied in the absence of dual criminality. • Consider establishing an asset forfeiture fund. • Consider a mechanism to authorise the sharing of confiscated assets with other countries when confiscation is directly or indirectly a result of co-ordinated law enforcement actions.
6.4 Extradition (R.39, 37 & SR.V)	

6.5 Other Forms of Co-operation (R.40 & SR.V)	• In order to demonstrate the regime's effectiveness, maintain statistics on the number of requests for assistance made or received by law enforcement authorities, the FIU, and supervisors including whether the request was granted or refused.
7. Other Issues	
7.1 Resources and statistics (R. 30 & 32)	• Increase the human and budgetary resources for the FIU • Provide additional training to law enforcement, both upon engagement as well as on an ongoing basis regarding AML and CFT investigations. • Consider additional staff for the FSA. • Increase training on AML/CFT issues for the FSA.

ANNEXES

Annex 1: Details of all bodies met on the on-site mission - Ministries, other government authorities or bodies, and private sector representatives.

I. Ministries and interagency committees

- Ministries of Industry and Commerce
- Ministry of Finance
  - Tax Directorate (Registry of Enterprises)
- Ministry of Justice
  - General Penal Code (GPC) Review Committee
- Ministry of Foreign Affairs
- National Statistics Office (National Register)
- AML/CFT Consultation Committee

II. Criminal justice and operational agencies

- National Commissioner of Police
  - Economic Crime Unit
  - Financial Intelligence Unit (FIU)
  - Directorate of Customs
- Director of Public Prosecutions Office (DPP)
- Reykjavik Police
- Keflavik Airport Police

III. Financial sector—government

- Financial Supervisory Authority
- Central Bank of Iceland
- Icelandic Stock Exchange

IV. Financial sector—associations and private sector entities

- Bankers and Securities Dealers Association of Iceland
- The Association of Icelandic Insurance Companies
- Money exchange business

V. DNFBPs–-SROs and associations

- Icelandic Bar Association
- Institute of State Authorised Public Auditors
- Association of Dealers in Real Estate

Annex 2: List of laws, regulations and other material received

Accounting Act No. 145/1994

Act concerning the implementation of instructions by the UN Security Council, No. 5/1969

Act No. 13/1984 on Extradition of Criminals and Other Assistance in Criminal Proceedings

Act No. 138/1994 respecting Private Limited Companies

Act No. 159/1994 on the European Economic Interest Grouping

Act No. 161/2002 on Financial Undertakings

Act No. 2/1995 respecting Public Limited Companies

Act No. 56/1993 on International Co-operation for Enforcement of Criminal Judgments

Act No. 80/1993 on Measures to Counteract Money Laundering (as amended in 1999)

Act No. 87/1998 on official supervision of financial operations

Act on European Companies No. 26/2004

Act on Funds and Institutions Operating under Ratified Charters, No. 19/1988

Act on Insurance No. 60/1994 (updated 01/11/2000)

Act on lotteries No. 38/2005

Act on Professional Lawyers No. 77/1998

Act on the Protection of Privacy as regards the Processing of Personal Data No. 77/2000

Act respecting Foundations Engaging in Business Operations No. 33/1999

Act. No. 64/2006 on Measures against Money Laundering and Terrorist Financing (in force 22 June 2006)

Administrative Procedures Act No. 37/1993

Annual Accounts Act, No. 144/1994

Code of Criminal Procedure, Act No. 19/1991

Custom Act No. 88/2005

General Penal Code Act No 19/1994

Government Employees Act, No. 70/1996

Information Act No 50/1996

Public Announcement 349/2002 (of 15 October 2001)

Public Announcement 867/2001 (of 14 November 2001)

Regulation 272/1994 on the role of financial institutions in measures against money laundering

Regulation 322/2001 on management of personal information by the police with amendment No. 926/2004

Regulation 550/2006 on the obligation to report and customer due diligence in measures against money laundering and terrorist financing (in force 27 June 2006)

Regulation 626/2006 on the handling of notifications of alleged money laundering (in force 12 July 2006)

Annex 3: Copies of key laws, regulations and other measures

Money laundering offence: Article 264 of the General Penal Code

Art. 264 [Anyone who accepts or acquires for himself or others gain from an offence according to the present Act shall be subject to fines … [1)] or imprisonment for up to 2 years. The same penalty shall be applicable to a person who stores or moves such gain, assists in the delivery thereof or does in another comparable manner support securing for others the gain of an offence. In case of a reiterated offence or one of a major character the penalty may become … [1)] imprisonment for up to 4 years.

Penalty may become imprisonment for up to [12 years] [2)] in case of gain resulting from an offence according to Art. 173 a.

In case gain is of a minor character and no special incidents augment the guilt of the offence a Lawsuit shall not be instituted unless public interests so require.

In case an offence be committed through inadvertence this will be subject to fines or [imprisonment for up to 6 months.] [1)] In case the offence from which gain results be subject to no heavier penalty [than imprisonment for up to 1 year] [1)] penalty may be cancelled.] [3)]

[1)] *Act 82/1998, Art. 141.* [2)] *Act 32/2001, Art. 2.* [3)] *Act 10/1997, Art. 4.*

Terrorist financing offence: Articles 100 (a)-(c) of the General Penal Code

[**Art. 100 a.** For acts of terrorism the penalty shall be up to life imprisonment for anyone who for the purpose of causing the public considerable fear or in an illegal manner forces Icelandic or foreign authorities or an international establishment to do or omit something with the object of weakening or damaging the Constitution or the political, economic or sociological foundations of the State or an international establishment, commits one or more of the following offences when the act in the light of its nature or having regard for circumstances at the time and place it is committed can seriously damage a State or an international establishment:-

1. homicide as per Art. 211,

2. physical assault as per Art. 218,

3. deprivation of freedom as per Art. 226,

4. upsets traffic safety as per para. 1, Art. 168,

disturbs public transport equipment et al. as per para. 1, Art. 176 or causes gross damage to properties as per para. 2, Art. 257 and if these violations are committed in such a manner as to endanger human lives or to cause extensive financial loss,

5. hijacking aircraft as per para. 2, Art. 165 or assaults persons present at airport intended for international air traffic as per para. 3, Art. 165,

6. arson as per para. 2, Art. 164 causing explosion, spreading of damaging gases, water flood, shipwreck, railway-, automobile or aircraft accident or accidents of other such vehicles or transport equipment as per para 1, Art. 165, causing general shortage of drinking water or introducing damaging substances to water wells, or water piping as per para. 1, Art. 170 or introducing toxic or other hazardous substances to articles intended for sale or general use as per para. 1, Art. 171.

The same penalty shall apply to a person who for the same purpose threatens to commit the violations listed in para. 1] [1)]

[1)] *Act 99/2002, Art. 2.*

[**Art. 100 b.** Anyone who directly or indirectly supports a person, an association or a group committing or having the purpose of committing acts of terrorism as per Art. 100 a. by contributing funds or granting other financial support, procuring or gathering funds or making funds available in another manner shall be subject to imprisonment for up to 10 years.] [1)]

[1)] *Act 99/2002, Art. 2.*

[**Art. 100 c**. Anyone who by means of his/her word or deed, persuasions, encouragement or in another manner supports punishable activities or a joint aim of an association or a group having committed one or more violations of Art. 100 a. or Art. 100 b. with the activities or the aims comprising the commission of one or more such violations shall be subject to imprisonment for up to 6 years.] [1)]

[1)] *Act 99/2002, Art. 2.*

Act No. 64/2006

on measures against money laundering and terrorist financing

In force 22 June 2006

CHAPTER I

General Provisions

Article 1

Objective

The purpose of this Act is to prevent money laundering and terrorist financing by imposing on parties engaging in activities which may be used for the purposes of money laundering and terrorist financing the obligation to obtain knowledge of their customers and their business activities and report to the competent authorities any knowledge of such illegal activities.

Article 2

Scope

The Act covers the following parties:

a) Financial undertakings pursuant to the definition in the Act on Financial Undertakings;

b) Life insurance companies and pension funds;

c) Insurance brokers and insurance intermediaries pursuant to the legislation on insurance brokerage when they broker life insurance or other savings-related insurance pursuant to Article 23 of the Insurance Act No. 60/1994;

d) Branches of foreign undertakings located in Iceland and falling within the scope of Sub-sections (a) to (c);

e) Natural or legal persons which, by way of business, engage in foreign exchange trading or the transfer of funds and other assets;

f) Attorneys and other legal professionals in the following instances:

i. When they manage or represent their clients in any form of financial or real estate dealings;

ii. When they assist in the organisation or conduct of business for their clients with respect to the purchase and sale of real estate or enterprises, manage cash, securities or other assets of their clients, open or manage commercial bank accounts, savings bank accounts or securities accounts, arrange financing needed for the establishment, operation or management of enterprises or establish, operate or manage custody accounts, enterprises and similar entities;

g) Auditors;

h) Other natural or legal persons when, in the course of their work, they perform the same services as those listed in Sub-section (f), e.g. tax consultants or other external consultants;

i) Brokers of real estate, enterprises or vessels;

j) Natural or legal persons engaged, by way of business, in trading in goods for payment in cash in the amount of EUR 15 000 or more, based on the officially posted exchange rate at any time, whether the transaction is executed in a single operation or in several operations which appear to be linked;

k) Trust and company service providers as defined in Article 3;

l) Legal or natural persons who have been granted an operating licence on the basis of the Lotteries Act, and parties permitted under special legislation to conduct fund-raising activities or lotteries where prizes are paid out in cash;

The Financial Supervisory Authority may decide that parties falling within the scope of Sub-sections (a) to (d) in Paragraph 1 and engaging in financial activities on an occasional or very limited basis, and where there is little risk of money laundering or terrorist financing, should be exempt from the provisions of this Act.

Anyone to whom the provisions of this Act apply is obliged to provide all the assistance necessary to ensure that the provisions of the Act may be enforced.

Article 3

Definitions

For the purpose of this Act the following definitions shall apply:

1. *Money laundering:* shall refer to actions by which a natural or legal person accepts or acquires, for itself or others, gains by means of a violation punishable under the General Penal Code, such as an acquisitive offence or a major tax or narcotics violation, violation of the Customs Act, the Act on Habit forming and Narcotic Substances, the Alcoholic Beverages Act or the Pharmaceuticals Act. The term shall also apply to actions by which a natural or legal person undertakes to keep, conceal or transfer such gains, assist in their delivery, or promote by other comparable means the achievement for others of the gains from such punishable violations.
2. *Terrorist financing:* shall refer to the collection of funds with the intention that they should be used or in the knowledge that they are to be used for the purpose of carrying out an offence which is punishable pursuant to Article 100 of the General Penal Code.
3. *Gain:* shall refer to any kind of profit and assets of any kind, including documents intended to entitle the bearer to access to assets or other rights of a financial value.
4. *Beneficial owner:* shall refer to the natural person or persons who ultimately own or control the natural person and/or legal person in whose name the transaction is effected or who effects the transaction. A beneficial owner may include:
    a) The natural person or persons who ultimately own or control a legal person through direct or indirect ownership of more than a 25% share in the legal person or control more than 25% of the voting rights or are deemed to exercise control by other means of the legal person. However, the provision does not apply to legal persons listed on a regulated market pursuant to the definition in the Act on Stock Exchanges and Regulated OTC Markets.
    b) The natural person or persons who are the future owners of 25% or more of the assets of a trust or a similar legal arrangement or who control more than 25% of its assets. Where the individuals that benefit from such trust have yet to be determined, the beneficiary is the person or persons in whose interest the fund is set up or operates.
5. *Persons under obligation to report:* Persons listed in Paragraph 1 of Article 2.
6. Trust and company service providers: Natural or legal persons providing, by way of business, the following services:
    a) Forming companies or other legal persons;
    b) Acting as, or arranging for another person to act as, director or executive of an undertaking, as partner in a company or serve in a comparable position in another form of legal person.
    c) Providing a domicile or other registered address which is used in a similar manner to contact the undertaking, or other related services;
    d) Acting as, or arranging for another person to act as, a trustee of a trust or a similar legal

arrangement;

e) Acting as, or arranging for another person to act as, a nominee shareholder for another person other than a company listed on a regulated market.

CHAPTER II

Customer due diligence

Article 4

Investigation of the reliability of information concerning customers

Persons under obligation to report pursuant to this Act shall apply customer due diligence measures pursuant to the provisions of this Chapter in the following cases:

a) When establishing a permanent business relationship;

b) When carrying out occasional transactions amounting to EUR 15 000 or more, based on the officially posted exchange rate at any time, whether the transaction is carried out in a single operation or in several operations which appear to be linked;

c) When carrying out foreign exchange transactions amounting to EUR 1,000 or more, based on the officially posted exchange rate at any time, whether the transaction is carried out in a single operation or in several operations which appear to be linked;

d) When there is a suspicion of money laundering or terrorist financing, regardless of any exemption or threshold;

e) When there are doubts about the veracity or adequacy of previously obtained customer identification data.

Article 5

Obtaining of information by persons under obligation to report

Prior to the establishment of a business relationship, or prior to a business transaction, a person under obligation to report shall require the new customer to prove his/her identity as follows:

a) Natural persons: by the presentation of identification documents issued by a public entity;

b) Legal persons: by the submission of a certificate from the register of undertakings of the Directorate of Internal Revenue, or a comparable public agency, with the name, domicile and official registration number or comparable information. Persons under obligation to report shall also require the provision of adequate information concerning any beneficial owner, cf. Article 3. Holders of powers of procuration shall prove their identity in the manner described in Sub-section (a).

Information shall be obtained concerning the purpose of the intended business with the proposed customer.

If a natural person, or the employee of a person under obligation to report, possesses knowledge, or has reason to believe, that certain business is being conducted for the benefit of a third party the customer shall, in accordance with Sub-sections (a) and (b), be required to produce information concerning the identity of the third party.

Persons under obligation to report shall preserve photocopies of personal identification documents and other required documents or adequate information from the documents, for a minimum of five years from the time that the business is concluded.

Article 6

Regular surveillance by persons under obligation to report

Persons under obligation to report shall conduct ongoing monitoring of the business relationship with their customers to ensure that their transactions are consistent with the available information on the customers, e.g. by scrutiny of the transactions undertaken throughout the course of the contractual relationship. Information on customers shall be updated and further information obtained in accordance with this Act as needed.

Article 7

Risk assessment.

Persons under obligation to report are permitted to implement the provisions of Articles 5 and 6 and the provisions of Chapters III and IV on a risk-sensitive basis, where the extent of information gathering and other measures pursuant to this Act in respect of each customer are based on an assessment of the risk of money laundering and terrorist financing. In the event of persons exercising such permission they shall establish rules on the conduct of the risk assessment, and the persons specified in Sub-sections (a) to (d) in Paragraph 1 of Article 2 shall be required to obtain the approval of the Financial Supervisory Authority for the rules, and the parties specified in Sub-sections (e) to (l) in Paragraph 1 of Article 2 shall be required to obtain the approval of the police authorities for the rules.

Article 8

Temporary postponement of information gathering

A new customer shall prove his/her identity pursuant to Article 5 before a contractual relationship is established. However, in order not to interrupt the normal conduct of business this may be postponed until a contractual relationship has been established in cases where little risk is perceived of money laundering or terrorist financing occurring. In such an event the customer shall prove his/her identity as soon as practicable.

A bank account may be opened for a customer even if the conditions of Paragraph 1 have not been met provided that no transactions are carried in respect of the customer until he/she has proven his/her identity pursuant to Article 5.

Notwithstanding the provisions of Paragraph 1, it is permitted, in relation to life insurance business, to allow the verification of the identity of the beneficiary under the policy to take place after the business relationship has been established. In such an event, verification shall take place no later than at the time of payout or before the time the beneficiary intends to exercise rights vested under the policy.

Article 9

Non-compliance with conditions of due diligence

If it has not proven possible to comply with the conditions of Paragraphs 1 and 2 of Article 5, the conduct of a business transaction or establishment of contractual relations with such person shall be prohibited Consideration should also be given to notification of the police pursuant to Article 17.

Paragraph 1 shall not apply to the work of legal professionals who are in the course of ascertaining the legal position of a client or performing their task of defending or representing that client in, or concerning, judicial proceedings, including advice on instituting or avoiding proceedings.

CHAPTER III

Enhanced customer due diligence requirements

Article 10

Distance selling

At the start of a distance selling transaction, the establishment of contracts through the use of telecommunications or comparable methods, where the customer is not present to prove his/her identity, additional information should be obtained about customers if necessary, and it should be required that the first payment should be made in the name of the customer and through an account established by the customer in a credit institution.

In the rules that persons under obligation to report are required to establish concerning internal control of business activities pursuant to Paragraph 1 of Article 23, more detailed provisions shall be established, where appropriate, concerning business using telecommunications and the preservation of data concerning such business.

Article 11

Correspondent banking

In cross-border correspondent banking business with parties from countries outside the European Economic Area, credit institutions which are subject to this Act shall comply with the following conditions:

a) Gather sufficient information about the respondent's business and determine from publicly available information the reputation of the institution and the quality of supervision;

b) Assess the respondent's anti-money laundering and anti-terrorist financing controls;

c) Obtain approval from senior management before establishing new correspondent banking relationships;

d) Document the respective responsibilities of each institution pursuant to this Act, and;

e) With respect to payable-through accounts, be satisfied that the respondent has knowledge of the identity of, and conducts ongoing due diligence on, the customers having direct access to accounts of credit institutions which are subject to this Act and that it is able to provide relevant information concerning the customer upon request.

Article 12

Exposed persons

In respect of contractual relationships or business transactions with politically exposed natural persons residing in another country, persons under obligation to report pursuant to this Act shall comply with the following requirements, in addition to the conditions of Chapter II:

a) Determine whether the customer is a politically exposed person, which includes natural persons who are or have been entrusted with prominent public functions and immediate family members, or persons known to be close associates, of such persons;

b) Obtain senior management approval before entering into business transactions with such customers;

c) Take appropriate measures to verify the source of funds that are involved in the business relationship or transaction;

d) Conduct regular monitoring of the business relationship.

Article 13

Correspondent banking business with shell banks

Credit institutions falling within the scope of this Act are prohibited from entering into or continuing a correspondent banking relationship with a credit institution or another party engaged in similar business activities which is established within a jurisdiction where it has no real business activities or management

and which is not related to a financial consolidation which is subject to regulation. Such institutions are also prohibited from engaging in correspondent banking business with banks which permit such credit institutions to use their accounts.

Article 14

Business anonymity

Parties under obligation to report shall show special caution in the case of products or transactions that might favour anonymity, and shall take measures, if needed, to prevent the use of such business for money laundering or terrorist financing purposes.

CHAPTER IV

Derogations from customer due diligence requirements

Article 15

Parties which are exempt from due diligence concerning customer information

The provisions of Articles 5 and 6 of his Act concerning customer due diligence do not apply to the following parties:

a) Legal persons listed in Sub-sections (a) and (b) in Paragraph 1 of Article 2 and corresponding legal persons possessing an operating licence in the European Economic Area. The same applies to regulated credit or financial institutions from countries outside the European Economic Area which are subject to similar requirements as those stipulated in this Act.

b) Companies listed on a regulated market pursuant to statutory definition of the activities of stock exchanges and regulated over-the-counter markets.

c) Icelandic government authorities.

Before granting an exemption pursuant to Paragraph 1 adequate information shall be obtained concerning the customer in order to ascertain whether the provisions of Sub-sections (a) and (b) apply.

Article 16

Third party information

A party under obligation to report is not required to conduct customer due diligence pursuant to Paragraphs 1 – 2 of Article 5 if corresponding due diligence data is revealed through the agency of a financial undertaking which has been granted an operating licence in Iceland or a corresponding legal person which has been granted an operating licence in the European Economic Area. The same applies to information revealed through the agency of regulated credit or financial institutions from countries outside the European Economic Area which are subject to similar requirements as those stipulated in this Act. The final responsibility as regards customer due diligence pursuant to Paragraphs 1 - 3 of Article 5 rests with the recipient of the information.

A third party providing information pursuant to Paragraph 1 shall, at the request of the recipient of the information, promptly make the information available or forward a copy of the appropriate personal data and other appropriate documents proving the identity of the customer or beneficial owner

CHAPTER V

Reporting obligation and other obligations

Article 17

General obligation to report

Persons under obligation to report are required to have any transactions suspected of being traceable to money laundering or terrorist financing carefully examined and notify the police of any transactions which are considered to have any such links. This applies in particular to transactions which are unusual, large or complex in the light of the normal business of the customer, or which have no apparent economic or visible lawful purpose.

Upon the request of police investigating cases of money laundering or terrorist financing, any information deemed necessary on account of such notification shall be provided by persons under obligation to report.

Paragraph 1 shall not apply to information obtained by legal professionals in the course of ascertaining the legal position of their client, including advice on instituting or avoiding proceedings, or information obtained before, during or after the conclusion of judicial proceedings, if the information is directly related to such proceedings. The same applies to information obtained by parties pursuant to Sub-sections (g) to (i) in Paragraph 1 of Article 2 when they are providing expert advice to a legal professional before, during or after the conclusion of judicial proceedings.

Article 18

Obligation to refrain from business

Parties shall refrain from doing business when there is knowledge or suspicion that the business can be traced to money laundering or terrorist financing. Such business shall be reported to the police and the report shall include information on the time limits within which the person under obligation to report is required to carry out the transaction. If such transaction cannot be prevented, or if its suspension could hinder the prosecution of parties benefiting from it, the police shall be notified of the transaction as soon as it has been completed.

Article 19

Processing of reports etc.

The police shall confirm the receipt of notifications pursuant to Articles 17 and 18 in writing. The police may, in cases of urgency, request that transactions notified in accordance with Articles 17 and 18 are not carried out until the conclusion of the time limit specified in the notification. The police shall promptly inform the reporting party if it is the opinion of the police that obstruction of the transaction is not needed.

Further provisions on the receipt of reports, analysis and dissemination of information on potential money laundering shall be laid down in a regulation issued by the Minister for Justice.

Article 20

Prohibition of disclosure

Persons under obligation to report and their directors and employees and others working in their interest shall ensure that it is not disclosed to the customer concerned or to other third persons that information has been imparted to the police in accordance with Articles 17 and 18 or that a money laundering or terrorist financing investigation is being or may be carried out.

Notwithstanding the provisions of Paragraph 1, the disclosure of the above information is permitted to the following parties:

a) The Financial Supervisory Authority;

b) Within a consolidation as defined in the Annual Accounts Act.

c) Between parties referred to in Sub-sections (f) and (g) in Paragraph 1 of Article 2 who are discharging their duties within the same legal person or same network of enterprises;

d) Between parties referred to in Sub-sections (a) to (g) in Paragraph 1 of Article 2,

provided that the following conditions are met:

1. Both parties belong to the same professional category;
2. The case concerns a natural or legal person who is a customer of both parties;
3. The information concerns transactions relating to both parties;
4. Both parties are subject to equivalent obligations as regards professional secrecy and personal data protection; and
5. The information is used exclusively for the purposes of the prevention of money laundering and terrorist financing.

Information pursuant to Paragraph 2 may only be disclosed to a natural or legal person domiciled outside the European Economic Area if the natural or legal person is subject to similar rules as those laid down in this Act concerning measures against money laundering and terrorist financing.

Parties referred to in Sub-sections (f) and (g) in Paragraph 1 of Article 2 who advise their customers to refrain from participating in illegal activities are not regarded as having violated Paragraph 1 on the prohibition of disclosure.

Article 21

Exemption from the principle of professional secrecy

The disclosure in good faith to the police by a person under obligation to report of information pursuant to this Act shall not constitute a breach of any principle of professional secrecy imposed by law or by other means.

The provision of such information shall not make the natural or legal persons or their employees criminally liable or liable for civil damages.

Article 22

Designation of person responsible

Persons under obligation to report are responsible for compliance with this Act and rules and regulations issued pursuant to this Act. They shall nominate a specific person of managerial rank to be generally responsible for notification pursuant to Articles 17 and 18 and to ensure the development of co-ordinated practices supporting the implementation of this Act. The police shall be informed of the nomination of such responsible person.

Article 23

Internal controls etc.

Persons under obligation to report are required to establish written internal rules and maintain internal controls designed to prevent their business activities from being used for money laundering and terrorist financing. To this end they shall ensure, *inter alia*, that their employees receive special training.

Persons under obligation to report are required to prepare written reports on all suspicious and unusual records that occur in the course of effecting transactions in their business activities. The preservation of such information is subject to the provisions of Paragraph 4 of Article 5.

Persons listed in Paragraph 1 of Article 2 shall have systems in place which enable them to respond promptly to queries from the police or other competent authorities. The preservation of such information, including information on individual customer transactions, is subject to the provisions of Paragraph 4 of Article 5.

Legal persons listed in Paragraph 1 of Article 2 are required, on the appointment of staff, to establish specific rules on the checks to be performed of the record of an applicant for positions with the

undertakings and in what instances a transcript from an applicant's judicial record or other comparable certificates of record and former employment shall be required.

Article 24

Branches and subsidiaries in states outside the European Economic Area

The persons listed in Sub-sections (a) to (c) in Paragraph 1 of Article 2 shall ensure that their branches and subsidiaries in states outside the European Economic Area take equivalent measures as regards due diligence concerning information on their customers as provided for in this Act, or as similar as the legislation of the state in question will permit.

If the legislation of a state outside the EEA where a branch or subsidiary is located does not permit the application of such equivalent due diligence concerning customer information as provided for in this Act, the party in question shall notify the Financial Supervisory Authority. In addition, the party in question shall ensure that the branch or subsidiary in question responds to the risk of money laundering or terrorist financing by other means.

The persons listed in Sub-sections (a) to (c) in Paragraph 1 of Article 2 shall ensure that their branches and subsidiaries in states outside the European Economic Area establish written internal rules similar to those required in Paragraph 1 of Article 23, or as similar as the legislation of the state in question will permit.

CHAPTER VI

Surveillance etc.

Article 25

The Financial Supervisory Authority

The Financial Supervisory Authority shall monitor compliance by the parties specified in Sub-sections (a) to (d) in Paragraph 1 of Article 2 with the provisions of this Act and rules and regulations issued pursuant to this Act. Such monitoring is subject to legislation on public surveillance of financial activities and such special legislation as may apply to the activities of regulated parties.

The Financial Supervisory Authority may exercise the supervisory measures provided for in the Act on Official Supervision of Financial Operations n its supervision pursuant to this Act.

Article 26

Reports from regulatory bodies

In the event that the Financial Supervisory Authority or other professional bodies responsible for the supervision of persons under obligation to report obtain, in the course of their work, knowledge of business linked with money laundering or terrorist financing or information which is suspected to relate to money laundering or terrorist financing this shall be reported to police.

The Financial Supervisory Authority shall issue notices and instructions if there is a need for special caution in business transactions with states or regions which do not comply with international recommendations and rules concerning measures against money laundering. Persons under obligation to report are also required to pay particular attention to states or regions which do not comply with international recommendations and rules on measures against money laundering.

CHAPTER VII

Penalties

Article 27

Penalties

In the event that a person under obligation to report, by intent or gross negligence, neglects to conduct due diligence concerning its customers pursuant to Chapters II and III, or neglects the obligation to report or any other obligations pursuant to Chapter V, or neglects the provision of information or assistance, reports or documents as provided for in this Act or rules issued hereunder, such party shall be subjected to penalties.

If an infringement of this Act is committed in the course of the business operations of a legal person, and for its benefit, the legal person may be fined irrespective of whether the guilt of its responsible manager or employee has been established. If the responsible manager of a legal entity or its staff member has infringed this Act, the legal entity may also be fined if the infringement was for its benefit.

CHAPTER VIII

Miscellaneous Provisions

Article 28

Authorisation for the issue of regulations

The Minister for Commerce may, by a government regulation, issue further provisions on the implementation of this Act, including:

1. Further provisions on exemption from due diligence requirements pursuant to Article 15;
2. Further provisions on the enforcement of the obligation to report pursuant to Article 17;
3. Further provision of what information concerning a remittent must accompany transfers;
4. Special rules concerning notification of transfer to, or for the benefit of, natural or legal persons having links with states or regions which do not have in place adequate rules concerning measures against money laundering and terrorist financing;
5. Special rules concerning the prohibition of or restrictions on the permission of persons under obligation to report to enter into a contractual relationship or effect transfers to natural or legal persons having links with states or regions which do not have in place adequate rules concerning measures against money laundering and terrorist financing;

Article 29

Implementation

This Act incorporates into the domestic legal order the provisions of Council Directive 2005/60/EC on the prevention of the use of the financial system for the purpose of money laundering and terrorist financing.

Article 30

Entry into force

This Act shall enter into force immediately. The provisions of Article 12 shall enter into force on .1 January 2007. On the entry into force of this Act, Act No. 80/1993 on measures to counteract money laundering, as amended, shall be repealed.

Passed by the Althing on 2 June 2006.

(Unofficial Translation from Icelandic)

Regulation 626/2006 on the handling of notifications of alleged money laundering

In force 12 July 2006

SECTION I

Scope, etc.

Article 1

Scope.

These regulations apply to the receipt of notifications and the examination and dissemination of information by the police in cases of alleged money laundering (*cf.* the Act on Measures against Money Laundering and the Financing of Terrorist Activities, No. 64 of 14 June 2006.

Article 2

Definitions.

The following terms are used as defined below in these regulations:

1. *Money Laundering Office*: The unit within the Economic Crime Department of the Office of the National Commissioner of Police where notifications of suspicious commercial practices are received and examined under Articles 17 and 18 of the Act on Measures against Money Laundering and the Financing of Terrorist Activities.
2. *PT database*: A separate database in the money laundering office in which notifications of suspicious commercial transactions are recorded and examined.
3. *Investigation*: The gathering of data and their examination to confirm or eliminate suspicion as to whether commercial transactions are connected with illegal activities or are connected in other ways with conduct that may be in violation of the General Criminal Code.

Article 3

Confidentiality.

All police employees who are involved in investigations under these regulations shall be bound under the Police Act and the Civil Servants' Rights and Obligations Act not to disclose matters of which they become aware as a result of notifications and their investigation.

Article 4

Recording and archiving.

All notifications of suspicious commercial transactions shall be recorded electronically in the PT database. This provision also applies to supplementary information applying to notifications that have already been recorded.

The Money Laundering Office shall have a special fax number, and its fax machine shall be located in a locked file repository. If notifications or further information is received in digital form or as a fax or letter, it shall be placed in a case file. All documents and digital data shall be kept in case files. Case files shall be kept in a locked file repository.

Only staff of the Economic Crime Department who are engaged in the reception and investigation of notifications may have read and write access to the PT database. Access to the database shall be granted in writing by the head of the Economic Crime Department.

The head of the Economic Crime Department and the staff of the Money Laundering Office shall have access to the file repository.

SECTION II

Handling of notifications in cases of suspected money laundering.

Article 5

Sending of notifications.

Notifications of suspicious commercial transactions shall be sent to the Money Laundering Office in the form of letters or fax messages, or in electronic or digital form (on diskettes or compact discs).

Article 6

Recording of notifications; preliminary investigation.

Notifications of suspicious commercial transactions shall be recorded in the PT database as soon as possible.

Records shall include the following information:

1. The name of the person making the notification,
2. the names of the persons and/or enterprises whose interests are involved,
3. the nature and scope of the transactions and
4. the reason why the person making the notification considers that the transactions may be connected with criminal activities, or may be the product of such activities.

Article 7

Investigations.

Investigations shall be carried out on the basis of notifications and, as appropriate, the gathering of information; these shall be the basis of decisions as provided for under Article 8.

Article 8

Decisions.

An investigation under Article 7 may lead to the following:

1. The destruction of the notification of the suspicious commercial transaction.
2. The recording of the notification in the police information system as material to be used in an investigation; reasons for such a decision shall be recorded in writing.
3. A decision to initiate a police investigation.
4. The transaction not being carried out (see Article 10).

Decisions on points 1 or 2 shall be taken by the investigating officer; decisions on points 3 or 4 shall be taken by the prosecution authority. Decisions shall be taken as soon as possible.

Article 9

Beginning of a police investigation.

When an investigation is begun by the Economic Crime Department of the Office of the National Commissioner of Police under item 3 of the first paragraph of Article 8, or when the case has been sent to another police department, a police detective shall make a police report on the case.

Article 10

Blocking of transfers.

When necessity so demands, the prosecution authority may instruct the person making the notification that the transaction of which notification has been given under Articles 17 and 18 of the Act on Money Laundering and the Financing of Terrorist Activities is not to be carried out (*cf.* the first paragraph of Article 19 of the same act). When such a decision is taken, it shall be taken into account whether there is reason to believe that the money will be destroyed or disposed of.

When a transaction is blocked (*cf.* the first paragraph of this Article), the Money Laundering Office shall carry out its investigation quickly so that the blocking of the transfer does not last longer than is necessary; in all cases this shall be done within the period stated in the announcement. This shall not apply, however, when the prosecuting authority decides to initiate an investigation, as part of which it seizes money or takes other measures in accordance with the provisions of the Code of Criminal Procedure.

Article 11

Recording and use of information of significance for the police.

If information received by the Money Laundering Office in connection with a notification of suspicious commercial practices constitutes information of significance for police investigations, such information shall be recorded in the national police data system. The information shall be recorded in such a way as not to indicate by whom the notification was submitted or by whom that person is employed.

Article 12

Information supplied to persons submitting notifications.

Those who submit notifications shall be sent immediate confirmation of receipt of their notifications.

As soon as the Money Laundering Office has taken a decision under Article 8, the person who submitted the notification shall be informed in writing of the decision unless he has stated that it is not necessary to give him such information. If the notification leads to criminal proceedings, the person who submitted it shall be informed of the outcome of the case.

The person who submitted the notification shall be informed if it is destroyed under the second paragraph of Article 14.

Article 13

Maintenance and release of information.

The Money Laundering Office shall keep, and publish each year, information on the number of notifications of suspicious commercial transactions it receives, how notifications are followed up, the number of cases investigated, the number of individuals prosecuted or sentenced for money laundering or the financing of terrorist activities and the value and categories of assets embargoed or seized under the Code of Criminal Procedure or confiscated under the General Criminal Code.

The Money Laundering Office shall release to the parties to whom such notification is obligatory the latest information on methods used in money laundering and the financing of terrorist activities, and on how to identify transactions covered by the Act on Measures against Money Laundering and the Financing of Terrorist Activities.

SECTION III

Destruction of notifications of suspicious commercial transactions.

Article 14

Destruction of materials.

If an investigation under Article 7 eliminates all suspicion of a connection with illegal activities, then all information recorded in the PT database regarding the case shall be deleted.

In cases other than those covered in the first paragraph of this Article, the information shall be deleted not later than 7 years after it was recorded in the PT database, except where new information has been recorded or a police investigation has been initiated against individuals or legal persons who are the subject of the notification.

SECTION IV.

Commencement.

Article 15

These regulations, which are issued under Article 19 of the Act on Measures against Money Laundering and the Financing of Terrorist Activities No. 64 of 14 June 2006, shall take immediate effect.

Ministry of Justice and Ecclesiastical Affairs, 12 July 2006.