

## Executive Summary

1. This report summarises the AML/CFT measures in place in the Kingdom of Bahrain as at the date of the on-site visit (7-22 November 2017). It analyses the level of compliance with the FATF 40 Recommendations and the level of effectiveness of Bahrain's AML/CFT system, and provides recommendations on how the system could be strengthened.

### *Key Findings*

- Overall, Bahrain has a moderate level of understanding of its money laundering and terrorist financing (ML/TF) risks, with the national risk assessment (NRA) process on going at the time of the onsite. The understanding of ML/TF risks is still evolving and will be further developed as the NRA process is concluded.
- Domestic coordination, cooperation and information exchange at the operational level is strong and proactive. There have been a number of initiatives, policies and actions by authorities to address ML/TF risks. However, more generally, the objectives and activities of authorities will need to be strengthened and aligned with the identified ML/TF risks.
- Financial intelligence and other information are accessed and used in investigations for ML/TF and associated offences. During 2012-2017, Bahrain initiated 43 investigations for ML, resulting in nine convictions, and a number of ongoing cases. However, the investigation and prosecution of ML, generally, do not appear to be fully in line with its ML risks.
- Bahrain's terrorism offence (which is cross referenced in the TF offence) includes an exemption that is inconsistent with the TF Convention. This exemption significantly impacts Bahrain's compliance at the technical level, but has not yet had a discernible impact on effectiveness. TF activities are identified and investigated by LEAs, though TF is mostly identified as a result of terrorism investigations. Given the strong domestic coordination in Bahrain, information and intelligence is rapidly exchanged in TF cases.
- Financial institutions in Bahrain immediately implement TFS (both PF and TF) without delay. However, the majority of the DNFBP sector does not implement TFS without delay, and the remaining DNFBPs (as well as all natural and legal persons in Bahrain) do not have legal obligations in relation to TFS.
- Bahrain identified a subset of high risk NPOs for potential terrorism abuse. Yet, restrictive obligations are placed on all NPOs operating in Bahrain, regardless of their identified risk profile. While these measures may be effective at mitigating TF

abuse of the NPO sector, they are not applied on a risk-basis and may unduly or inadvertently restrict NPO's ability to access resources, including financial resources, to carry out their legitimate activities.

- In the financial sector, the application of proportionate mitigating measures by large financial institutions is robust. Progress still needs to be made regarding the understanding and implementation of beneficial ownership obligations. Implementation of preventive measures, including suspicious transaction reporting by the DNFBP sector needs improvements.
- Bahrain has strong controls to prevent criminals from beneficially owning a significant or controlling interest or holding a management function in a financial institution. The CBB has strong elements of a risk based approach to supervision and requires remediation from institutions it supervises. It has imposed a range of sanctions and made referrals for prosecution, though there is scope to increase the use of sanctions as the level of onsite supervision increases.
- International cooperation between Bahraini authorities and foreign counterparts is collaborative and provided upon request and spontaneously, with priority given to terrorism and TF. Mutual Legal Assistance (MLA) requests are mainly used as complementary tools, in addition to more informal cooperation channels.

### *Risks and General Situation*

2. Bahrain is a regional financial and trading hub with a liberal business environment. Bahrain's economy has shown steady growth during in recent years despite the financial meltdown in 2008-2009. Bahrain's real GDP was USD 31.8 billion in 2016, and grew by around 3.3% from that in 2015. Oil comprises 75.6% of the country's budget revenues and 20% of its GDP. Bahrain enjoys a strong, diverse, and competitive economy which promotes business growth. The financial services sector accounted for 16.5% of the real GDP in 2016, and is the largest non-oil contributor to the GDP.

3. Bahrain is exposed to domestic ML/TF risks, and the ML/TF risks associated with cross-border customers and activity. Bahrain is currently undertaking its first formal and comprehensive National Money Laundering and Terrorist Financing Risk Assessment (NRA). The NRA process is organised and led by the National Policy Committee (NPC) and carried out by working groups representing relevant AML/CFT stakeholders in the country, including private sector.

4. As per the draft NRA as at the time of onsite, the most important ML threats are investment fraud, cash courier/cross-border violations including smuggling and immorality and prostitution. The banking sector is considered to be the most targeted sector for ML, with money changers, custodians and real estate being medium risk targets.

5. Bahrain is also exposed to geopolitical risks, most notably in relation to TF. According to the authorities, the risk of terrorism and TF is high. Though the understanding of risk is still being finalised, Bahrain identifies the most prevalent and high risk TF areas as: cash smuggling via land and sea (i.e. foreign funding); NPOs; and fundraising.

## Overall Level of Compliance and Effectiveness

### *Assessment of risk, co-ordination and policy setting (Chapter 2; 10.1, R.1, 2, 33 & 34)*

6. Bahrain is currently undertaking a ML/TF NRA, with most of the relevant authorities contributing to the process. It is moving forward methodically and the NRA process will continue to build on existing sectoral assessments carried out by the Central Bank of Bahrain (CBB) and the Ministry of Industry Commerce and Tourism (MOICT), which has a dual role: registrar of legal persons and DNFBP supervisor for dealers in precious metals and stones, accountants and auditors and real estate agents which are structured as companies (until September 2017 at which point, real estate sector was transferred to a separate authority). Understanding of ML/TF risks is still evolving and will be further developed as the NRA process is concluded. At the time of the onsite a draft NRA report had been prepared.

7. The assessment of risks both in general, and in a range of particular areas, needs to be deepened so as to allow substantiated conclusions on risks, and their relative importance from a national perspective. There should also be more in depth analysis in certain areas, including the threats from, and vulnerabilities to, cross-border flows; legal persons and legal arrangements; and, organised crime. This would enable Bahrain to reach robust conclusions.

8. The Bahrain has a longstanding co-ordination framework, which covers AML/CFT and combatting of PF. Domestic co-operation and information exchange at the operational level is strong and visible and a number of informal exchanges also occur, for example in the context of national security. There is strong domestic coordination by the authorities within the Ministry of Interior (MOI) and the National Security Agency (NSA) in relation to investigations of terrorism and TF offences and to progress investigations once started. This enables intelligence to be shared rapidly in all cases between various units of the MOI involved in these cases and the NSA.

9. The NPC with its subcommittee, the Legislation/Policy Committee, sets and coordinates AML/CFT policy. There is also a separate committee, the National Committee on the Implementation of UNSCRs, which follows up on the implementation of UNSCRs. The NPC develops 3-5 year strategies, which can be updated as needed. However, the existing strategy and action plans do not constitute a comprehensive national policy to address key risks. The absence of agreed and fully articulated ML/TF risks at national level means that the authorities have not been well placed to direct their objectives and policies towards the highest national risks.

### *Financial intelligence, ML investigations, prosecutions and confiscation (Chapter 3; 10.6, 7, 8; R.1, 3, 4, 29–32)*

10. Bahraini Financial Intelligence Directorate (FID) is a law enforcement FIU and is well integrated through electronic systems and direct communication channels with other agencies. Financial intelligence and other information are accessed and used in investigations for ML, TF and associated predicate offences,

including for the development of evidence for associated predicate offences. The FID has access to several databases which enhance its ability to produce financial intelligence of quality using a variety of sources.

11. There is strong and effective co-operation and co-ordination between FID and other law enforcement authorities including national security agencies and supervisors. The FID is supporting the operational needs of law enforcement agencies to a considerable extent; however, more in depth strategic analysis on emerging trends and typologies is needed to better support the work of all the competent authorities.

12. Bahrain has a sound legal framework for the investigation of ML. The initial investigation of ML cases is carried out by the FID and referred to the Public Prosecution Office (PPO) for judicial investigation. The PPO and FID work collaboratively with other relevant competent authorities in the course of ML investigations and prosecutions. In recent years, Bahrain has pursued more complex ML investigations and among the ML cases provided, both small and large-scale ML cases exist, including various types of ML offences. However overall, the assessment team has concerns that Bahrain does not consistently and systematically investigate and prosecute ML in line with its ML risks.

13. A wide range of sanctions are imposed for ML offences for natural and legal persons. In practice, of the 34 individuals convicted of ML during 2012-17, the average sanction applied was four years, with the highest sentence applied being seven years' imprisonment and included fines up to BHD 200 000 (EUR 431 077).

14. Bahrain's legal framework for seizing, freezing and confiscating assets is adequate and has been used to some extent. The disclosure system for incoming and outgoing cross border currency movements and BNIs was significantly strengthened at the time of the onsite. There is, however, no specific policy or guidelines requiring law enforcement agencies to pursue confiscation as a policy objective, though, authorities seem to pursue it as part of a larger proceeds-of-crime approach to combat crime. More generally, confiscation results can be considered modest, taking into account Bahrain's risk profile.

### ***Terrorist and proliferation financing (Chapter 4; 10.9, 10, 11; R. 1, 4, 5-8, 30, 31 & 39.)***

15. Bahrain's terrorism offence includes an exemption which is cross-referenced in its TF offence, and is inconsistent with the TF Convention. This exemption significantly impacts Bahrain's compliance at the technical level, though it does not have a discernible impact on effectiveness, as it has not been used as a defence in court or by authorities to limit their identification or investigation of TF.

16. The authorities have an evolving understanding of TF threats in Bahrain. TF activities are identified and investigated by LEAs, though TF is mostly identified as a result of terrorism investigations. As a result, the assessment team has concerns that Bahrain is not proactively pursuing TF investigations and prosecutions as a preventive measure to identify and financially disrupt terrorists. Sanctions imposed in TF cases are effective, proportionate and dissuasive.

17. Financial institutions in Bahrain immediately implement the relevant UNSCRs related to TFS, as they are legally obliged to comply with UN Chapter VII

designations without the need for additional orders from Bahraini authorities. DNFBPs supervised by the MOICT [real estate agents which are structured as companies (until September 2017 at which point, real estate sector was transferred to a separate authority, RERA under SLRB), DPMS, accountants and auditors] also have a legal obligation to implement TFS upon notification by the MOICT. However, changes to the relevant lists were not communicated without delay by the MOICT prior to the end of the onsite visit, though the MOICT changed its procedures subsequently.

18. The CBB and MOICT verify their respective reporting entities' compliance with UNSCR obligations during onsite and offsite inspections. Understanding and implementation is varied and limited, particularly outside the financial sector. The assessment team also had serious concerns about a case where a financial institution permitted access to an account by a UN 1267 listed individual.

19. In regard to PF, Bahrain has no trading relations with Iran or the DPRK; however given the geographical proximity to Iran, PF exposure risks do exist. Bahrain's customs officials have an advanced understanding of the risks of proliferation and PF, including diversion and sanctions evasion. Case studies exist that demonstrate that the competent authorities are monitoring and ensuring compliance with PF related TFS, including the application of the CBB's most severe administrative penalties, as well as the pursuit of criminal charges. Detailed guidance and outreach on PF by the relevant supervisors will further help mitigate the PF risk.

### *Preventive measures (Chapter 5; IO.4; R.9–23)*

20. Bahrain has a diverse financial industry with banks as the key players. The Financial Crime Module (FC Module) issued by the CBB is recognised as a solid base for understanding and complying with AML/CFT obligations across financial sector. Understanding of ML/TF risks and commensurate mitigating measures across FIs and DNFBPs vary depending on the nature of the sector. Banks, MVTs, insurance and securities have a good understanding of ML risks and in some instances, less understanding of TF risks. The level of understanding of ML/TF risks among DNFBP sector in general needs improvements. Implementation of CDD measures is relatively less robust in the DNFBP sector. Some elements of the CDD process, such as identifying and verifying the identity of beneficial ownership need to be improved across the financial and DNFBP sectors.

21. Banks, money changers and MVTs providers are the largest contributor to STRs with five banks filing nearly 52% of the total STRs filed by the banking sector. This is in line with the overall risk and context of Bahrain. Both the level and quality of reporting done by DNFBPs needs major improvements. Authorities indicated that the quality has improved over last few years and the level of defensive reporting from the sector has reduced, though the assessment team has concerns about very low level of reporting by the DPMS and absence of any reporting by the real estate sector, in particular during the last five years.

### *Supervision (Chapter 6; IO.3; R.14, 26–28, 34, 35)*

22. The CBB supervises the financial sector, including trust service providers, and has strong controls to prevent criminals from beneficially owning a significant

or controlling interest or holding a management function in a FI. The Ministry of Justice (MOJ) has reasonable controls in relation to the fitness and properness at initial licensing of lawyers and thereafter. The MOICT also has reasonable controls at initial registration and thereafter to prevent criminal ownership and control of its supervised entities.

23. The CBB has strong elements of a risk-based approach to supervision and it reviews significant offsite information (including STRs), which informs onsite inspections and the use of other supervisory tools to address risk. The CBB has imposed a range of sanctions and made referrals for prosecution. There is scope to increase the use of sanctions as the level of onsite supervision increases.

24. The MOICT has put in place a framework for, and a largely risk based approach to supervision (it too reviews STRs and, in addition, auditors' reports on the quality of AML/CFT controls). The MOICT has also risk graded each DNFBP it supervises and uses both onsite and offsite monitoring tools, though further enhancements are needed to ensure a more comprehensive risk based approach.

### *Transparency and beneficial ownership (Chapter 7; IO.5; R.24, 25)*

25. Bahrain is yet to conduct a comprehensive assessment of the ML/TF risks posed by legal persons created in the country.

26. Bahrain has a centralised registry for companies, partnerships and individual establishments (Sijilat system). Basic and legal ownership information is accurately and adequately kept. The registry is frequently updated, searchable on different parameters and user friendly.

27. The registry includes information on authorised signatories, board of directors and shareholders. The registry also separately captures names of all shareholders who own 5% and above in a company's shares as well as names of ultimate natural person who is the beneficial owner of the shares (however it lacks reference to those who may control a legal person through means other than ownership). The beneficial ownership is relatively easily traced through the Sijilat system where no foreign ownership or control is involved.

28. The MOICT has a dual role in Bahrain's AML/CFT regime: as DNFBP supervisor and as registrar of legal persons and needs further resources to fulfil its mandate effectively.

29. Information related to Waqfs is available through a court order in the Sharia Courts and Waqfs councils, which supervise and manage Waqfs to preserve their state. With regard to trusts, authorities have access, upon request, to all information relating to trust service providers, available with the CBB. No specific instances of abuse of trusts or Waqfs had come to the notice of authorities thus far.

### *International co-operation (Chapter 8; IO.2; R.36–40)*

30. International cooperation is an important element for Bahrain, given its role as a financial and business centre. Bahrain sends and responds to MLA requests for both ML and predicate offences and uses informal cooperation mechanisms for a variety of purposes, including TF. Formal bilateral agreements are signed at the request of counterparts, although no agreements or MOUs are required under

Bahraini law to provide MLA or exchange information. Bahrain takes a collaborative approach towards requests and it has not refused an international cooperation request because of a lack of reciprocity.

31. The number of outgoing MLA requests is not fully in line with the ML/TF risk profile of Bahrain. However, the FID exchanges information related to ML/TF through other channels. The FID is active on outgoing exchange of information requests particularly for ML cases. The CBB has the authority to, and has exchanged supervisory information with its international counterparts when relevant to AML/CFT.

32. Extradition requests are fulfilled by Bahrain in a timely manner, given that: i) no complaints with regard to extradition were noted by counterparts; and ii) the fact that by law, the average time to process extraditions cannot exceed 30 days (which could be extended to a maximum of 60 days), unless a reason is given by the requesting state. The number of both incoming and outgoing extradition requests is significant considering Bahrain's size and context.

### *Priority Actions*

- Bahrain should finalise its NRA, including by utilising information from outside Bahrain; utilising more statistics and ensuring that the statistics used are robust; further analysing external risks and the risks of organised crime; and reviewing the DNFBP sectors in more detail. Assessment of TF risk should improve in depth and coverage.
- Bahrain should develop and implement national AML/CFT policies based on the findings of the ML/TF risk assessment and provide a clear strategy as well as action plans to address the risks identified.
- Bahrain should prioritise the investigation and prosecution of all types of ML in accordance with the country's risks, in particular cross-border risks.
- Bahrain should develop policy guidelines and strategies on seizures and confiscation in order to ensure a consistent approach across LEAs. Bahrain should also take measures to adequately track trends and results obtained in this regard.
- Bahrain should urgently amend its terrorism offence (which is cross-referenced in its TF offence) to remove the exemption as it is inconsistent with the TF Convention.
- Bahrain should seek to routinely identify and investigate TF as a distinct criminal activity instead of investigating TF primarily as part of terrorism cases.
- Bahrain should implement mitigation measures that are commensurate to the risks identified through its review of the NPO sector and understanding of the TF risks in the sector. A targeted risk based approach, outreach and guidance on how to identify, prevent and report TF, with a focus on those NPOs assessed as higher risk for potential TF abuse would help avoid restricting and disrupting legitimate NPO activities.

- Bahrain should further develop the understanding of the ML/TF risks being faced by the financial sector and DNFBPs, in particular by communicating the findings of NRA once finalised and through proactive engagement.

## Effectiveness & Technical Compliance Ratings

### Effectiveness Ratings (High, Substantial, Moderate, Low)

<b>IO.1 - Risk, policy and coordination</b>	<b>IO.2 - International cooperation</b>	<b>IO.3 - Supervision</b>	<b>IO.4 - Preventive measures</b>	<b>IO.5 - Legal persons and arrangements</b>	<b>IO.6 - Financial intelligence</b>
<b>Moderate</b>	<b>Substantial</b>	<b>Substantial</b>	<b>Moderate</b>	<b>Moderate</b>	<b>Substantial</b>
<b>IO.7 - ML investigation &amp; prosecution</b>	<b>IO.8 - Confiscation</b>	<b>IO.9 - TF investigation &amp; prosecution</b>	<b>IO.10 - TF preventive measures &amp; financial sanctions</b>	<b>IO.11 - PF financial sanctions</b>	
<b>Moderate</b>	<b>Moderate</b>	<b>Moderate</b>	<b>Moderate</b>	<b>Moderate</b>	

### Technical Compliance Ratings (C - compliant, LC - largely compliant, PC - partially compliant, NC - non compliant)

<b>R.1 - assessing risk &amp; applying risk-based approach</b>	<b>R.2 - national cooperation and coordination</b>	<b>R.3 - money laundering offence</b>	<b>R.4 - confiscation &amp; provisional measures</b>	<b>R.5 - terrorist financing offence</b>	<b>R.6 - targeted financial sanctions - terrorism &amp; terrorist financing</b>
<b>PC</b>	<b>LC</b>	<b>LC</b>	<b>C</b>	<b>PC</b>	<b>PC</b>
<b>R.7 - targeted financial sanctions - proliferation</b>	<b>R.8 - non-profit organisations</b>	<b>R.9 - financial institution secrecy laws</b>	<b>R.10 - Customer due diligence</b>	<b>R.11 - Record keeping</b>	<b>R.12 - Politically exposed persons</b>
<b>PC</b>	<b>LC</b>	<b>C</b>	<b>LC</b>	<b>C</b>	<b>LC</b>
<b>R.13 - Correspondent banking</b>	<b>R.14 - Money or value transfer services</b>	<b>R.15 - New technologies</b>	<b>R.16 - Wire transfers</b>	<b>R.17 - Reliance on third parties</b>	<b>R.18 - Internal controls and foreign branches and subsidiaries</b>
<b>LC</b>	<b>LC</b>	<b>C</b>	<b>LC</b>	<b>C</b>	<b>LC</b>
<b>R.19 - Higher-risk countries</b>	<b>R.20 - Reporting of suspicious transactions</b>	<b>R.21 - Tipping-off and confidentiality</b>	<b>R.22 - DNFBPs: Customer due diligence</b>	<b>R.23 - DNFBPs: Other measures</b>	<b>R.24 - Transparency &amp; BO of legal persons</b>
<b>LC</b>	<b>LC</b>	<b>LC</b>	<b>PC</b>	<b>PC</b>	<b>LC</b>
<b>R.25 - Transparency &amp; BO of legal arrangements</b>	<b>R.26 - Regulation and supervision of financial institutions</b>	<b>R.27 - Powers of supervision</b>	<b>R.28 - Regulation and supervision of DNFBPs</b>	<b>R.29 - Financial intelligence units</b>	<b>R.30 - Responsibilities of law enforcement and investigative authorities</b>
<b>LC</b>	<b>LC</b>	<b>LC</b>	<b>LC</b>	<b>C</b>	<b>C</b>
<b>R.31 - Powers of law enforcement and investigative authorities</b>	<b>R.32 - Cash couriers</b>	<b>R.33 - Statistics</b>	<b>R.34 - Guidance and feedback</b>	<b>R.35 - Sanctions</b>	<b>R.36 - International instruments</b>
<b>C</b>	<b>LC</b>	<b>LC</b>	<b>LC</b>	<b>LC</b>	<b>LC</b>
<b>R.37 - Mutual legal assistance</b>	<b>R.38 - Mutual legal assistance: freezing and confiscation</b>	<b>R.39 - Extradition</b>	<b>R.40 - Other forms of international cooperation</b>		
<b>LC</b>	<b>LC</b>	<b>LC</b>	<b>LC</b>		

