



Anti-money laundering and counter-terrorist financing measures - Malaysia

2. National AML/CFT policies and coordination

Effectiveness and technical compliance



Citing reference:

FATF and APG (2015), "National AML/CFT Policies and Coordination" in *Anti-money laundering and counter-terrorist financing measures - Malaysia*, Fourth Round Mutual Evaluation Report, FATF, Paris and APG, Sydney
www.fatf-gafi.org/publications/mutualevaluations/documents/mer-malaysia-2015.html

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2. NATIONAL AML/CTF POLICIES AND COORDINATION

Key Findings

Malaysia has assessed its ML and TF risks through a number of assessments prior to and since the two NRAs (one completed in 2012 and the other in 2013) and other targeted and sectoral assessments. The most recent NRA (2013) identified five high threat/crime areas: fraud, goods smuggling, drugs, tax evasion and corruption. The NRAs did not sufficiently take account of foreign sourced threats, TF and the interconnectedness of specific crimes and financial sectors but these are considered moderate limitations in light of risks identification activities prior to and since the NRAs were completed which further enhance Malaysia's understanding of its ML/TF risks. The assessments of institutional strengths and vulnerabilities were reasonable, but could be enhanced including through the assessment of more institutions.

Understanding of ML/TF risks has increased substantially since the first NRA in 2012 but is still evolving. The NRA process enhanced the country's understanding of risks and while the assessment process was reasonable, moderate improvements in the methodology, scope and depth of analysis can be made in the future. Assessment of TF risks associated with the increasing threat of terrorism activities e.g. domestic recruitment and self-financed operations was still developing at the time of the onsite visit. A White Paper addressing the threat posed by ISIL was tabled in Parliament in November 2014. Malaysia has plans to update the last NRA, including further assessment of TF risks.

The framework for national coordination and cooperation through the AML/CFT National Coordination Committee (NCC) is very strong with only minor improvements needed. The inclusion of PF in 2012 into the NCC's mandate and relevant agencies supports good outcomes.

Given the timing and dissemination of the 2013, NRA, broad-based analysis of the results and updating of national strategies, priorities and action plans, including the revision of the risk-based elements of the sectoral guidelines, is continuing. The Interim Strategic Plans (October 2014) has started the process of further recalibrating the AML/CFT regime in line with the risks identified in the NRAs.

The financial and DNFBP sectors have not yet fully integrated the NRA findings in their internal risk identification, assessment and mitigation measures. Awareness of assessed risks by the non-bank and DNFBP sectors appears generally low (See IO 4). A planned red flags and typologies exercise should assist in this process but could be broadened beyond FIs. The sectoral Guidelines include a risk-based approach to compliance that is closely aligned with the revised FATF Recommendations and which provides a sound legal basis for more precisely implementing the applicable NRA findings.

2.1 Background and Context

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(a) Overview of AML/CFT Strategy

2.1. Malaysia's AML/CFT regime is based on a well-coordinated and integrated inter-agency strategy and reflects its understanding of ML/TF risks. The government's priorities and objectives are part of wider policy objectives of modernising the economy, governance and responses to human security issues. A number of related policy objectives complement the AML/CFT strategy including enhanced financial inclusion, and contributions to regional global AML/CFT efforts (e.g. APG, ASEAN, the Egmont Group and the World Bank). Malaysia was granted FATF observer status in October 2014.

(b) The Institutional Framework

2.2. Malaysia's institutional framework for AML/CFT is well developed as set out in s. 1.3 above.

(c) Coordination and Cooperation Arrangements

2.3. Malaysia has effective mechanisms of coordination and cooperation for the development of AML/CFT and PF policies and activities. It established the NCC in 2000 with a membership now comprising 16 public sector agencies with a role in AML/CFT matters and predicate crimes. The NCC's main function is to coordinate inter-agency and national AML/CFT activities and there is clear political commitment and support for the NCC and AML/CFT efforts generally as evidenced by the involvement of the Economic Council (chaired by the Prime Minister) and the Prime Minister's Department in AML/CFT issues. In 2012, the NCC expanded to cover PF.

(d) Country's assessment of Risk

Timeline and process for assessing risk

2.4. The activities of the NCC have been focused on measures to combat ML/TF risk since its inception in 2000. The NCC's role in mitigating ML/TF was reflected in Malaysia's 2007 MER. Prior to the 2012 NRA some agencies undertook threat and vulnerability assessments on specific topics, including some at the national level¹. The results helped inform national AML/CFT policy and measures to mitigate identified ML/TF risks, but this was not consolidated until the first NRA in 2012.

2.5. The first NRA (December 2012) was mainly based on data collected on crime and sectoral self-assessments, ML threats linked to certain predicate crimes and vulnerabilities inherent in FIs and DNFBPs.

2.6. A key outcome of the 2012 NRA was improvements of data capture capabilities mainly through the Centralized Data Management Framework that came into effect in January 2013 for the NCC agencies. The framework formalised the compilation of data on financial intelligence; investigations; prosecutions; forfeiture (criminal and civil); international cooperation; supervision; ML/TF typologies cases and AML/CFT training. Financial intelligence, investigation, prosecution and supervisory statistics are collected every 4 months.

2.7. Following the 2012 NRA, the NCC revised and expanded the NRA methodology that, inter alia, expanded the scope of the country's vulnerabilities, ML predicates, TF, NPO vulnerabilities, and legal persons and arrangements. It also expanded the scope of information obtained, including from foreign counterpart

1 Other threat and risk assessments included e.g. Government Transformation Programme consultations identifying seven areas for prioritized action including corruption; continues monitoring and actions against threat of drug abuse threat since 1983; BNM's 2009 assessment and subsequent reform of the MSB sector; inclusion of tax offences as a predicate offence in 2010 resulting from analysis of STRs and CTRs; and strengthening of LEAs including establishment of specialized AML/CFT units

agencies, expert views, perception surveys (from LEAs and the private sector) and published reports. The 2013 NRA findings were finalised in December 2013 and presented to the Economic Council in June 2014. It was further reviewed by the NCC in July 2014 based on feedback from the EC. The process of dissemination to RIs started in July 2014.

2.8. NRAs enhanced Malaysia's understanding of its ML/TF risks and support the framework for implementing broad-based reforms to the existing AML/CFT regime including recalibration of strategies, priorities, policies and action plans to mitigate ML/TF risks. In September 2014 each of the NCC agencies were requested to draft action plans based on the NRA results. The interim strategic plan (ISP) outlines specific actions to be taken by NCC member agencies.

Methodology, scope and depth of analysis of the NRA

2.9. The NRA methodology was based on the combination of threats and vulnerabilities using the following formula:

Risk= threats + vulnerabilities

Threats= domestic and foreign crimes + impact from those crimes

Vulnerabilities= country (economic, legal, and geographical) and sectoral (FIs, DNFBPs, NPOs and legal persons)) **vulnerabilities + likelihood**

Strengths

2.10. The rating of risks provides a useful basis for applying countermeasures proportionate to the level of risk. The NRA identified five high-risk crime categories (fraud, smuggling, drug trafficking, tax crimes and corruption/bribery) as priority areas of focus. The dissemination of the 2013 NRA to the RIs articulated the various risk categories and their ratings, as well as vulnerability areas that can inform development of proportional risk mitigation controls.

2.11. As indicated above, the framework for data capture improved the quantity and quality of information available for the 2013 and future NRAs. The NRA included data from the FIU, LEAs, independent and external reports, perception surveys from LEAs and RIs, and experts' views. The range of stakeholders involved was also expanded.

2.12. Malaysia's engagement with international partners in seeking to capture data of risks of ML/TF arising in foreign jurisdictions is a valuable component of the NRA process but the few responses received from foreign jurisdictions was a limitation. Malaysia made effective use of Egmont channels and bilateral outreach to obtain risk information from surveys and open source materials.

2.13. Although domestic and foreign terrorism and related TF threats were not fully covered in the NRAs, Malaysian authorities provided general and specific information on the country's increasing exposure to such risks which included use of the country as a source of funds or recruits for terrorist groups active in other countries. The authorities have taken account of other risk assessments. For instance, a White Paper on the security threat posed by ISIL to Malaysia was tabled before Parliament on November 26, 2014.

2.14. Assessments of ML and TF risks prior to, during and following the two NRAs provided an ongoing basis for the NCC and individual agencies to prioritise their policies and activities towards risk mitigation. These risk mitigation activities are discussed throughout the report, and a number of key responses to the assessment of TF risk are summarised in the box below. Malaysia has committed to update the NRA at least every two to three years with more frequent reviews in response to emerging risks, as indicated by the case study below. Each NCC member agency will conduct risk assessments on an ongoing basis as per the NCC's October 2014 ISP.

Box 2.1. Case study: Assessing and responding to TF risk

Malaysia's assessment of TF risk predates the NRA process and includes activities to assess methods and trends of cross-border terrorism groups (Jemaah Islamiya, Abu Sayaf, LTTE, etc.), vulnerabilities of MVTS and money changers, risks in the NPO sector, and institutional vulnerabilities (prosecutions, etc.). Malaysia's assessment of TF has been evolving and responding to the changing nature of the TF risks. The 2014 White Paper on ISIL and associated TF risks reflects the iterative approach taken by Malaysia to assess risks. Policies and activities responding to the findings on terrorism and TF risks demonstrate that the authorities adapt flexibility to the changing environment and include:

- The intensity and scope of controls on the NPO sector (particular the tight controls on charitable collections from 2012 and targeted RoS and Special Branch activities (see IO10)
- The intensity and scope of regulation/supervision of the MSB sector during 2011-2013 (see IO3)
- Targeted outreach to FIs, DNFBPs and NPOs on the details of TF risk (see IO4)
- Focus on the use of targeted financial sanctions against terrorism (see IO10)
- RMP's focus on TF investigations since 2012 (see IO9)
- Interventions to arrest facilitators and shut down fundraising websites in 2014 (see IO9)

Areas for improvement of the NRA for assessing risks in the future

2.15. While assessors consider the NRA has provided a reasonable basis to assess many of the risks, this section identifies a number of moderate improvements to the methodology of the NRA which Malaysia should consider as it works on future iterations of the NRA process. The NRA results disseminated are generally high-level. Future NRAs would benefit from further details to guide RIs. In addition, deeper analysis of foreign sourced threats including those connected with cross-border trade and financial flows, and the Labuan offshore sectors, would be useful. A good example of this has been work to assess flows from China as part of FIED's analysis. The above threats were not adequately addressed in the NRA but are material in the context of Malaysia.

2.16. Existing assessments of domestic and foreign terrorism and related TF threats were not sufficiently consolidated in the NRA, but further assessment of these risks has continued since late 2013 which has enhanced Malaysia's understanding of TF risk such that post NRA is considered to be high by the authorities.

2.17. The interconnectedness and correlation of threats/crimes and their ratings do not appear to have been adequately assessed. In particular, the interconnectedness of organised crime (rated medium risk) and high risk rated crimes e.g. smuggling and drug trafficking; and reported links between organized crime and low risk rated crimes such as counterfeiting and piracy.

2.18. The assessment of domestic corruption as high risk was well supported but not the potential linkages with other domestic and cross-border crimes such as illegal logging/environmental crimes. Environmental crime is one of the areas where authorities sought targeted responses on risk from countries in the region, but did not receive responses. The work of Malaysia's well-functioning Anti-Corruption Commission (MACC) reflects the priority to mitigate this crime in the country.

2.19. Assessment of strengths and vulnerabilities in the institutional frameworks of AML/CFT stakeholder agencies beyond the legal framework could be improved in the NRA, including through the assessment of more institutions. Outside of the NRA, supervisors have conducted an assessment of vulnerabilities for each regulated sector, including through their ongoing supervisory activities to help benchmark approaches to

regulation and supervision. Some of the institutional vulnerabilities identified in the NRA are covered under the ISP as measures to be implemented.

2.20. With respect to sectoral vulnerabilities, further consideration could have been given to vulnerabilities (e.g. contagion risks) associated with the prevalence of financial groups spanning multiple sectors and the business linkages between the domestic and offshore FIs.

2.2 Technical Compliance (R.1, R.2, R.33)

2.21. R. 1 – Assessing Risks and applying a Risk-Based Approach – **Malaysia is rated largely compliant**

2.22. R. 2 – National Cooperation and Coordination - **Malaysia is rated compliant**

2.23. R. 33 – Statistics - **Malaysia is rated compliant**

2.3 Effectiveness: Immediate Outcome 1 (Risk, Policy and Coordination)

(a) *Understanding of ML/TF Risks*

Risks, context and materiality

2.24. Prior to the 2012 NRA some agencies undertook threat and vulnerability assessments on specific topics, including some at the national level. Malaysia's understanding of ML/TF risks has improved substantially since it started the process of systematic assessments, which culminated in a NRA in December 2012, and an expanded NRA in December 2013. The last NRA indicates that the country is exposed to a range of ML risk associated with high threat areas including fraud, smuggling, illicit drugs, tax crimes and corruption. With the exception of TF and, to an extent organised crime, the NRA appropriately highlights the findings of these crime areas as priority risk areas for attention (see the analysis of the NRA in s.2.1(d) above). Understanding the interconnectivity of risks, e.g. in relation to organised crime, corruption and domestic and foreign crimes appears to be limited requiring moderate improvements. For example, while corruption risk is rated as high, its linkages to other lower rated crimes (e.g. illegal logging) do not appear to have been sufficiently assessed and understood.

2.25. Terrorism and TF is considered as medium risk in the 2013 NRA, but in practice, the authorities consider it has high risk partly due to post NRA developments. Malaysia has faced a number of threats related to terrorist financing, including from Al Qaida, Jemaah Islamiya, the Liberation Tigers of Tamil Ealam (LTTE), Abu Sayef Group, and others. Recently significant threats related to the financing of ISIL recruits have emerged. Malaysia has porous national borders, rendering the country susceptible to the smuggling of cash and weapons and the relatively easy movement of people. Since 2004, some 156 Malaysians and a number of foreign nationals have been arrested in Malaysia for adherence to terrorist groups.

2.26. Malaysian authorities provided information on terrorism threats and the country's increasing vulnerability of being used as a source of TF or recruits for terrorist groups active in other countries, including ISIL. Malaysian officials estimated that in 2014 more than 75 Malaysians had joined or attempted to join ISIL. The authorities indicated that most of the cases detected so far involve low income, unsophisticated individuals but recent reported cases involve recruitment and financing operations using the internet. This suggests the emergence of more organized and sophisticated operations and that the understanding of this risk is still evolving in pace with TF methods. In November 2014, SB arrested those suspected of recruiting Malaysians via Facebook to send to Syria.

2.27. Malaysian authorities indicated that there is no evidence linking the proceeds of criminal activities such as kidnapping, extortion, robbery, smuggling, fraud and drug trafficking to terrorist groups, despite the prevalence of these activities in 'hot spots' associated with terrorism risks (Southern Philippines and

Southern Thailand). There have been incidents of kidnapping in Malaysia's territory, i.e. Sabah, by the Abu Sayyaf group for ransom to further terrorism activities in their home country. Malaysia collaborates with the relevant regional authorities to share risk information to address these threats.

2.28. In the past, Malaysia, through its cooperation with international partners, has had the experience of investigating terrorist groups that have raised monies in support of their causes on a larger scale. Malaysia has identified fundraising through contributions made by terrorist group members through a collection of *infaq*² of approximately 5% of monthly income in cash.

2.29. Malaysia has also focused on the use of the internet by terrorism-affiliated entities to channel logistical assistance to militant groups, recruitment, and funding terrorist activities. Between February 2013 and late 2014, SB has arrested 45 suspected militants of whom 22 have been charged, including three connected to Tadzim Al-Qaeda. The authorities contend that most of the cases detected so far involve low income unsophisticated individuals but recent reported cases involve recruitment and financing operations using the internet which suggests more organized and sophisticated operations.

2.30. Religious, charitable and political NPOs account for about 40% of NPOs and are considered a high-risk TF area in the NRA. The NRA indicates that a small proportion of NPOs account for the majority of international financial transactions and activities (approximately 1000 of a total of more than 47 000 NPOs) and that relatively few transactions are linked to high risk and conflict countries. NPO receipts during 2013 more than tripled far exceeding payments which had been steady during the previous 8 years. TF risk associated with this sector was rated as medium in the NRA. While awareness of TF risks in the NPO sector has been generally low in the past, oversight and risk mitigation have started to improve but is limited by resources. Outreach of TF has increased including through online portals and an annual conference. All of these factors point to a reducing but still high vulnerability for the NPO sector.

2.31. Malaysia has taken strong regulatory and enforcement measures to control the MSB sectors (remitters and money changers) in response to significant risks, but unauthorized illicit MSBs continue to pose a significant vulnerability, including with respect to TF. Malaysia is a net outbound remitter of funds, with a large presence of migrant workers both legal and illegal. Strengthened controls, enforcement and other supervisory measures are resulting in significant increases in formal channels for remittance which should mitigate the level of risk posed by this sector.

2.32. Malaysia's highly cash-based economy (vulnerability rated as high) and significant informal economy (vulnerability rated as moderate) is considered by the NRA. The NRA indicated that terrorists have used cash couriers in Malaysia in the past including cross-border operations. Malaysia's states that its efforts to increase financial inclusion have reduced the size of the informal economy while national efforts to promote e-money are aimed at reducing the use of cash. The World Bank's Global Findex for 2014 shows that 81% (an increase from 66% in 2011) of the adult population had access to accounts in formal financial institutions.

2.33. Malaysia's assessments and understanding of risk, as well as the assessment team's discussions with RIs and LEAs, indicate that use of informal nominee and front or 'mule' accounts in Malaysia is a challenge for RIs across Malaysia. The mule accounts identified by Malaysian authorities mainly involve individual account holders rather than legal persons. Use of formal nominees is also a feature in the offshore corporate sector. The authorities and private sector recognize this vulnerability and enforcement measures have been taken against those identified as mule account holders.

2.34. Malaysia has a small but important offshore financial centre in Labuan, which was rated as medium risk in the NRA. The assessment and understanding of ML/TF risks associated with Labuan-based businesses is partly based on the size of the sectors and the absence of cash transactions. Nonetheless, since many of the services are not substantially asset-based (e.g. company, trust, foundation and related services), these factors may be insufficient to properly assess and understand their associated ML/TF vulnerabilities and risks.

2 Infaq means spending or disbursement simply to please God without asking for any favour or hoping for a return. It is different from Zakat, which is obligatory on Muslims.

Many of the FIs operating in Labuan are owned or controlled by onshore banks (considered high risk), and a large proportion of business (e.g. loans by offshore banks) are to Malaysian customers. The Labuan offshore sector has exposure to a number of high-risk jurisdictions. These institutional, commercial and cross-border linkages and the associated ML/TF risks do not appear to have been sufficiently assessed and understood, requiring moderate improvements in the assessment and understanding of risk.

2.35. Only one large casino has been licensed in the country and is the single non-financial sector vulnerability rated as high risk in the NRA. This rating was well supported and the inherent ML risks and vulnerabilities are well known. The casino offers a wide range of high-risk services (e.g. those associated with client account and transaction practices), has several cross-border subsidiaries, affiliates and customers (e.g. through junket operations). The risks arising from the casino's foreign operations have yet to be viewed on a consolidated basis.

2.36. Malaysia has a significant Islamic finance sector involving banks, takaful (Islamic insurance) and other intermediaries which are subject to the same AML/CFT legal and regulatory regime as conventional and Islamic finance institutions. Supervisors are of the view that, based on their supervisory experience, there are no material differences in risks when compared to conventional FIs (for example Islamic banks and non-Islamic bank are all rated as high-risk sectors). The NRA and other assessments considered ML and TF risks for all sectors of FIs and did not separately assess ML/TF risk and vulnerabilities in the Islamic finance sector as it did, for example, for the domestic and offshore sector.

2.37. The role of Zakat³ and its potential connection with charitable organisations (NPOs) was another area that has been considered by the authorities, although it was not discussed directly in the NRA. Malaysia has centralised and closely monitors systems for collection and disbursement of Zakat to mitigate risks in the sector (see IO10).

Sectoral understanding of risk (see IO 3 and IO 4)

2.38. Malaysia's understanding of sectoral ML/TF risks was substantially improved by the process and results of the NRA (and recently the ISIL White Paper with respect to TF). The outcomes of the NRA process have commenced to be incorporated into the roles and priorities of the various AML/CFT stakeholders (e.g. the October 2014 Interim Strategic Plan) which should continue to enhance their understanding of risk.

2.39. BNM, in particular the FIED, and the banking sectors have a better understanding of ML risks. Much of this derives from the broad supervisory coverage of banks and other sectors subject to its supervision. During 2014, BNM, SC and LSFA developed an enhanced risk-based framework for AML/CFT supervision that provides for a more detailed assessment of institutional risks than was previously the case, and which is broadly consistent with the FATF requirements.

2.40. Discussions with the private sectors on the results of the NRAs mainly reflected their sectoral risk contributions to the NRA process and to the predicate crimes identified as high risk by the NRAs. Their own understanding of risks, including based on NRAs findings, are assessed under IO.4. The sectoral guidelines issued in 2013 closely follow the risk-based requirements of the FATF Recommendations. The authorities indicated that the development of these guidelines were also informed by the 2012 NRA process and results, including sectoral vulnerability assessments conducted for the 2013 NRA.

(b) Cooperation, Coordination and Policy

Interagency cooperation and coordination

2.41. The national framework for cooperation and coordination on AML/CFT issues is strong and supports

3 Zakat is an obligation on Muslims to give a specific amount of their wealth (with certain conditions and requirements) to prescribed beneficiaries called al-mustahiqqin with the main objective of achieving socioeconomic justice.

the development and effective implementation of policies and activities to combat ML and TF with only minor shortcomings identified. The NCC was established in 2000 with a membership now comprising 16 public sector AML/CFT stakeholders. There is no direct private sector representation on the NCC, but NCC members coordinate with the private sectors, mainly through their respective supervisory agencies. The NRAs engaged the RIs sectors who provided input into the assessment process. The ME process and the NRAs also reinforced the implementation of interagency coordination and cooperation including for setting national strategies and activities. The October 2014 ISP to address key findings of the NRA is one of the recent coordination outputs.

2.42. There is clear political commitment and support for the NCC and AML/CFT matters. The involvement of the Economic Council and the Prime Minister's Department in the NRA is process is evidence of such support.

2.43. There has been close cooperation among the main supervisor agencies, namely the BNM, SC and the LFSA. These agencies contribute to the work of the NCC, coordinated in the drafting of the 2013 sectoral guidelines, and participate in consolidated supervision of financial groups and sectoral awareness raising programs. The DNFBBPs and their SRBs coordinate through the NCC's DNFBBP Taskforce but their activities are not significant.

2.44. Coordination at the operational level is well developed but there are a number of areas requiring improvement. LEAs should more effectively coordinate their efforts to combat horizontal threats/crimes and their associated ML/TF risks identified in the NRAs. These coordination mechanisms should also extend to other agencies (e.g. supervisors) involved with risk mitigation including the reduction of sectoral and institutional vulnerabilities, such as in the NPO sector. The establishment of the Special Taskforce for the enforcement of Government revenue collection, including related ML has enhanced LEA cooperation.

2.45. Malaysia's coordination framework includes a number of specialized taskforces to deal with specific crimes and AML/CFT related issues, e.g. illicit money services businesses and cross-border currency transportation. The NRA highlighted the need to enhance inter-agency cooperation and cooperation by institutionalizing the 'ad hoc' taskforce mechanism drawing on the experience of the AGC's Special Taskforce but this is not part of the ISP. The ISP contemplates the establishment of a more permanent financial working group under the NCC including the financial sector supervisors. Enhanced private sector engagement in the work of the NCC would also enhance public-private sector collaboration.

2.46. There is good cooperation between the main supervisory agencies (BNM, SC and LFSA), the FIU and other LEAs. The ISP further requires that all LEAs attach officers to BNM FIED (FIU) to enhance inter-agency collaboration. For the NPO sector, efforts are being made to enhance cooperation between the RoS, IRB, regulators and other LEAs in order to improve information sharing in support CFT efforts, including development of systems for risk identification, assessment and mitigation.

2.47. Interagency coordination to combat PF is well supported. The inclusion of the Strategic Trade Secretariat (STS) in the NCC has provided a suitable platform for inter-agency cooperation and policy coordination on PF issues. Nonetheless, there is a need to further deepen the engagement between the Special Branch, regulators and other relevant agencies in information sharing and cooperation on combating PF.

Policies and other activities

2.48. The authorities have taken other specific AML/CFT risk mitigating measures in addition to those that are discussed in other parts of the MER. For example, in October 2014 the ISP was formulated to provide a useful framework for reviewing and calibrating national policies, priorities and action plans. The ISP contains 19 action points. Some of these activities are summarized below:

- Each NCC agency to establish an ML/TF risk assessment function.
- Labuan to undertake a more broad-based threat and vulnerability assessment.
- Establish specialized AML units in all LEAs.

- Develop red flags and typologies for high-risk threats between LEAs and FIs.
- Second LEA officers to the BNM FIED.
- LEAs to develop criteria for opening ML investigations.
- Increase ML investigations and prosecutions of high-risk crimes, including drugs.
- Increase international information exchange and MLA.
- Enhance the cross-border currency declaration regime.
- Increase investigations and prosecutions of TF.
- Operationalize the targeted sanctions regime under the Strategic Trade Act.
- Complete the revision of risk-based AML/CFT supervisory framework.
- Establish a permanent financial working group under the NCC.
- Issue specific guidelines to high-risk entities esp. casinos.
- Establish formal cooperation and information sharing mechanisms between the Registrar of Societies and other regulators e.g. through MOUs.
- Revise the Companies Act to require retention of beneficial ownership information.

Box 2.2. Case study: Special Taskforce

The Special Taskforce is an operational level taskforce established in 2011 by the High Level Taskforce on Combating Money Laundering and Related Crimes. It is led by the AGC and uses AML as one of its key tools to systematically target vulnerabilities in key elements of the economy. The Special Taskforce identifies strategic opportunities to collect revenues, investigate related crimes (e.g. illegal remittance) and proposes improvements to systems and procedures.

The Special Taskforce comprises the ACG, RMC, RMP, MACC, IRB, BNM, CCM, CyberSecurity Malaysia, National Audit Department and the Immigration Department. The Special Taskforce is an excellent example of effective interagency cooperation and policy coordination to use AML tools and has achieved notable successes, including administrative recoveries of over RM 2.5 billion (USD 747M)¹. The actions have directly contributed to overall increased levels of tax compliance, which has significantly increased revenue to the government.

1. Exchange rate as of last day of onsite (25 November 2014) used throughout report, 1USD: 3.3474RM

(c) *NRA and risk-based measures*

2.49. The 2013 NRA provided an important but not the only basis for the review and calibration of AML/CFT strategies, policies and action plans, (the ISP is one such measure) building on measures taken based on prior risk and vulnerability assessments. The 2013 sectoral guidelines (regulations) were developed during the 2013 NRA process and are largely based on the requirements of revised FATF Recommendations and other information available to supervisors, including findings of the 2012 NRA. These guidelines will be revised taking into account the results of the 2013 NRA. The ISP calls for a revision and updating of the risk-based supervisory frameworks but not of the sectoral guidelines. It requires the three supervisory agencies to further update their risk-based supervision frameworks which could be expanded to include

the identification and assessment of institutional risks relating to clients, products and services, including TF specific risk factors and use of nominee and “mule” accounts. Revision of the risk-based supervisory framework for all sectors was completed in November 2014.

(d) Activities and objectives of competent authorities

2.50. Malaysia’s ongoing assessments of risk have provided a good basis for competent authorities to prioritise their policies and activities to mitigate key risks. Examples of Malaysia’s responses to identified risks appear throughout the report. For example, IO3 notes enhanced supervisory resources and activities with the casino (since 2014); outreach and supervision of FI branches located in high-risk areas such as border towns (since 2011); and an increased intensity and focus of MSB regulation and supervision (2011-13). The BNM and SC have implemented a risk-based approach to general supervision that includes an AML/CFT compliance element. During 2014, both supervisors as well as the LSFA have developed a new and enhanced risk-based framework for AML/CFT supervision that provides for a more detailed assessment of institutional risks. The ISP contemplates the joint development of red flags and typologies by the LEAs and FIs based on high risk areas identified by the NRA but does not contemplate participation by DNFBPs in this process.

(e) Awareness by FIs and DNFBPs of NRA results

2.51. The results of the 2012 NRA were disseminated through outreach conferences to a large number of RIs and their respective associations. All financial and DNFBP sectors participated in the 2013 NRA by providing data through their respective supervisors, SRBs and the conduct of self-assessments. The results of the NRA were disseminated to RIs from mid-2014 through awareness programs, conferences and publishing the results on relevant AML/CFT websites. Based on discussions with RIs, the 2013 NRA dissemination was useful but did not provide sufficient details to enable RIs them to fine tune their internal risk assessment and mitigation systems because it was too high level for a more detailed assessment of specific risks and their mitigation, as required by the sectoral guidelines. Most RIs interviewed indicated that the NRA adequately reflected their individual sectoral inputs but did not seem to go beyond that in helping them understand the broader sectoral and country risks. This view was also reflected by some of the official AML/CFT agencies interviewed.

2.52. Malaysia’s White Paper on ISIL was published and was planned to be disseminated to RIs to enhance awareness of TF risk. The RMP and other authorities have engaged with the media to raise public awareness on the developing threats posed by ISIL, including groups at risk, activities involved and *modus operandi*.

Overall conclusions on Immediate Outcome 1

2.53. Overall, the level of understanding of ML/TF risks in Malaysia is reasonable and increasing, and Malaysia has a range of AML/CFT policies and activities to mitigate the risks. Assessments of ML and TF risks prior to, during and following the two NRAs provided a strong basis for the NCC and individual agencies to prioritise their policies and activities towards risk mitigation taking into account the evolving nature of risks. The NRA processes were a principal factor in enhancing risk awareness in the country. The assessment team was generally satisfied with the reasonableness of Malaysia’s assessment of ML/TF risks, but some shortcomings in the NRA’s scope, data availability and process were noted. These shortcomings limit the understanding of some of the ML/TF threats and vulnerabilities (e.g. foreign sourced and interconnected threats and vulnerabilities, and institutional strengths and vulnerabilities). Some of the shortcomings in the NRA’s scope and level of detail limits its utility for RIs in calibrating their internal risk identification, assessment and management systems.

2.54. Broad-based and detailed review of national and institutional strategies, policies and action plans has commenced based on the 2012 NRA and other information sources (e.g. supervisory data) with the ISP, but is still to be completed. This reflects the timing of the 2013 NRA results and the ongoing ME. The October 2014 ISP will be further developed once this MER is finalised. The supervisory agencies have revised their risk-based frameworks for AML/CFT supervision. These systems are more advanced for the banking and securities sectors than for other sectors.

2.55. The national AML/CFT coordination and cooperation framework is comprehensive and effective with only minor shortcomings identified. The NCC provides a sound foundation for continued inter-agency coordination and collaboration as was evidenced by the organisation and conduct of the NRA and this ME. The NRA identified a number of areas where inter-agency cooperation could be improved but not all are included in the ISP. The assessment team also identified areas for enhanced inter-agency coordination and cooperation to improve the quality of STRs and oversight of the NPO sector.

2.56. The expansion of the NCC agenda and membership to encompass PF issues provides a sound foundation to develop and implement coordinated policy responses to proliferation financing issues.

2.57. Malaysia demonstrated its commitment to improve a number of the risk-sensitive elements of the system that were not all implemented at the time of the onsite visit. The 2013 NRA was disseminated to RIs but its findings have not been fully taken into account in their risk identification, assessment and mitigation systems, mainly because dissemination was relatively recent. Following the 2013 NRA, the 2013 sectoral guidelines are being reviewed for high-risk entities, e.g. the single casino. The October 2014 ISP, which is partly based on the 2013 NRA, requires the issuance of typologies and the establishment of risk assessment functions by all NCC members, and upgrading of the risk-based supervisory frameworks which has been undertaken.

2.58. **Overall, Malaysia has achieved a substantial level of effectiveness for Immediate Outcome 1.**

2.4 Recommendations on National AML/CFT Policies and Coordination

2.59. In line with its plan for a 2-3 year NRA cycle, commence the next iteration of the NRA and other assessments to address issues of scope and depth of analysis, and enhance understanding of risk, including:

1. Implement the ISP action plan to establish a risk assessment unit in each NCC agency.
2. More in-depth assessment of foreign sourced threats/crimes, terrorism and TF threats, institutional strengths and vulnerabilities, interconnectedness of organised crime and other crime types.
3. Strengthen the risk assessment of Labuan, including interconnectedness with other sectors.
4. Ensure a deepened process of dissemination of risk findings to RIs following and between each iteration of the NRA to support their implementation of risk-based approaches to mitigate risk.

2.60. Review and update national strategies, policies, priorities and action plans to reflect findings of the NRA, beyond the action points in the ISP:

2.61. Enhance interagency coordination and cooperation under the NCC by permanently establishing the NCC financial working group and consider how self-regulatory bodies and the private sector can have a more active input to coordination processes and activities in the NCC. Establishment of the financial working group and other measures were completed after the onsite visit.

2.62. Further disseminate and raise awareness of risks through further development and dissemination of sectoral typologies and ML/TF risks based on the NRA.

2.63. Review and as necessary update the sectoral guidelines in line with the NRA findings by focusing on the risk-based provisions with respect to simplified and enhanced measures.



2. NATIONAL AML/CFT POLICIES AND COORDINATION

Recommendation 1 - Assessing Risks and applying a Risk-Based Approach

a2.1. The previous MER did not assess compliance in relation to understanding and mitigating risk, although it did set out a range of risks and risk mitigation measures.

a2.2. **Criterion 1.1** – Malaysia has identified and assessed its ML/TF risks through the conduct of two National Risk Assessments (NRAs) in 2012 and 2013 and a range of risk assessments prior to and since the NRA, including focused assessments of specific sectors or crimes. The NRA had inputs on threats and vulnerabilities from government sector and risk inputs from reporting institutions (RIs). The first NRA had a relatively simple methodology and did not assess TF risk. In February 2013 the methodology of the NRA was expanded to include an analysis of threat, vulnerability and consequences for ML and TF with a wider range of government and non-government stakeholders and data sources. While the 2013 NRA's methodology was an improvement on the 2012 methodology there are still gaps evident in its design and application. The scope and depth of assessment of TF risks in the 2013 NRA is relatively weak. Additional assessments of TF risk have been undertaken including a White Paper on ISIL published in late 2014. The TF risk findings available to the private sector are limited in detail, particularly compared to those on ML risks.

a2.3. **Criterion 1.2** - Malaysia has designated the AML/CFT National Coordination Committee (NCC) to conduct the national risk assessment and related risk assessment tasks and the work to prepare the NRA has been led by a team from the FIU. The NCC has been able to draw on a wide range of ministries, agencies and non-government players to conduct the risk assessment. Data collection strategies and resources have been adjusted to collect necessary data to support assessment of risks.

a2.4. **Criterion 1.3** - Through the work of committees of the NCC, since 2012 Malaysia has updated the NRA, including improving the methodology to assess risk and included an assessment of TF in 2013. Malaysia has indicated that the full NRA process will be undertaken every three years, with agency-level and thematic assessments produced within that time, as evidenced by the ISIL White Paper.

a2.5. **Criterion 1.4** - Malaysia has a number of mechanisms to provide the findings of the risk assessment to government and non-government stakeholders. The NCC is the chief mechanism for sharing the detailed findings. At the political level the Economic Council (chaired by the Prime Minister) considered and contributed to the NRA. All NCC agencies received the full NRA and discussions during NCC briefings to each agency centred on agency-specific issues, including risk mitigation plans. NRA findings were communicated to the private sector via publication of key findings and information sharing sessions with RIs. While the published NRA lacks details of TF risk, more detailed briefings on TF risks were given to the private sector via briefings and the White Paper on ISIL.

a2.6. **Criterion 1.5** - Malaysia has taken steps to apply a risk-based approach to allocating resources and implementing measures to prevent or mitigate ML/TF risks based on the NRA and other assessments. More intensive resource allocation for intelligence / investigation / prosecution activities against priority risk areas is achieved through a number of multi-agency task forces focusing on certain areas (prevention of white collar crime, online financial fraud, smuggling/ tax evasion). This is undertaken under the NCC and other policy structures. There is a continuing focus on re-allocating resources and reconfiguring task forces or multi-agency mechanisms in response to ongoing experience (e.g. combating aspects of fraud).

a2.7. The frameworks for risk-based supervision of all sectors, including the allocation of supervisory resources, are being adjusted to take into account risk assessment findings. Based on risks identified with MVTS, the legal and regulatory framework covering the sector was overhauled in 2011, with all entities having to relicense resulting in a significant consolidation of the sector.

a2.8. **Criterion 1.6** - Malaysia applies all of the preventive measures required in the FATF Recommendations to all categories of FIs and DNFBPs, with one exception; however the intensity of the measures to be applied varies in certain specific circumstances set out in law and regulation. The one exception is for custodian

NATIONAL AML/CFT POLICIES AND COORDINATION

services in relation to capital markets which is limited to those defined in s.121 of the Capital Market and Services Act 2007 (CMSA) which includes banks, subsidiaries of banks and trust companies. Malaysia assessed that these custodians are low risk for ML/TF purpose due to the financial activity being limited to clients of fund managers which are subjected to AML/CFT requirements. Additionally these custodians' functions under CMSA do not have direct interactions with the client of the fund managers, as their role is limited to the safekeeping of cash and liquid securities. Fund managers are expected to conduct CDD on individual investors who invest with fund managers.

a2.9. **Criterion 1.7 (a)** - In the case of MSBs (MVTs and money changers), based on the findings of the NRA the CDD threshold for money changing transactions was revised downwards and any exemptions from CDD on corporate customers were removed for this sector. It is not clear that this extends to requiring RIs to take enhanced measures or additional assessment where the NRA/other risk assessments identifies high risk situations.

a2.10. **Criterion 1.7 (b)** - RIs are obliged to assess their ML/TF risks and conduct additional assessment as and when required by the supervisor and such instructions have been given to all RIs based on NRA findings.

a2.11. **Criterion 1.8** - Malaysia has put in place a limited number of risk-based simplified measures which are consistent with the findings of the NRA.

a2.12. **Criterion 1.9** - Supervisors and SRBs in Malaysia are taking steps to ensure RIs assess their risks and apply risk-based measures. This includes engagement, outreach and supervisory actions.

a2.13. **Criterion 1.10 (a-d)** - Obligations on RIs to assess ML/TF risks on an ongoing basis and share the findings with the regulatory authorities directly mirror the FATF standard.

a2.14. **Criterion 1.11 (a-c)** - Obligations on RIs for ML/TF risk controls and mitigation directly mirror the FATF standard. RIs are required to conduct independent testing to monitor their policies, controls and procedures for risk assessment and mitigation.

a2.15. **Criterion 1.12** - The limited number of risk-based simplified measures are not permitted in circumstances where there is a suspicion on ML or TF.

Weighting and Conclusion

a2.16. There are some minor gaps in the level of detail in the assessment of TF risk and foreign sourced threats and minor doubts about connection between NRA findings and MSB's enhanced measures for high risk scenarios.

A2

a2.17. **Malaysia is rated largely compliant with R.1.**

Recommendation 2: National cooperation and coordination

a2.18. Malaysia was rated largely compliant with former R.31. The main deficiencies noted were a limited focus on cross-agency coordination of supervisory initiatives specific to AML/CFT, and a need for inter-agency coordination in relation to cross border cash declarations (SR IX).

a2.19. **Criterion 2.1** – The NCC developed and implemented an AML/CFT Strategic Plan for the years 2010-2012 to address the shortcomings of the 2007 MER, to reflect the revised FATF standards and ensure a focused and effective AML/CFT regime. This was achieved by identifying ML/TF risks half yearly, having an annual peer assessment/review of the AML regime to identify and address implementation gaps; and to have a high level NCC meeting at least once a year to review the developments of the AML/CFT regime and set strategic direction.

a2.20. In October 2014 the NCC adopted an Interim National AML/CFT Strategic Plan (ISP) to reflect the findings of NRA and other assessments of ML/TF risks and gaps identified when preparing for the 2014

mutual evaluation. The ISP will be reviewed and updated taking into account risks and other policy decisions. NCC members have taken steps to reflect the national policies, based on the NRA findings, are reflected in their respective agencies policies and strategies.

a2.21. **Criterion 2.2** - The NCC is a coordinating body made up of 16 core government agencies and is the mechanism responsible for the development and implementation of national AML/CFT policies. While SROs which are the licensing body for certain DNFBPs are not directly represented, the FIED engages with the SROs in its role as AML/CFT regulator/supervisor for those DNFBPs.

a2.22. **Criterion 2.3** - Malaysia has demonstrated that there are mechanisms in place (MOUs, Joint Committees, Task Forces, etc.) to ensure that regulators, supervisors, LEAs, prosecutors and the FIU cooperate and coordinate domestically on the development and implementation of AML/CFT policies and activities. This is assisted by the dual functions of a number of supervisors as LEAs and the FIED as FIU, LEA and supervisor. Development and implementation of the amended cross-border reporting regime was derived from such mechanisms.

a2.23. **Criterion 2.4** - Malaysia's competent authorities have commenced cooperation in relation to the financing of proliferation of WMD. The objectives of the NCC have been expanded to include the development and implementation of national strategies, policies and measures to effectively combat financing the proliferation of WMD. The NCC Legal working group was established to agree on the workflows to operationalize the relevant UNSCRs. While not required under the FATF standard, it is noted that the next iteration of the NRA will consider the risks of proliferation financing.

a2.24. **Malaysia is rated compliant with R.2.**

Recommendation 33 – Statistics

a2.25. Malaysia was rated largely compliant with former R.32. Deficiencies related to statistics on supervisory action by BNM, accurate statistics and records of data obtained through the cross border reporting systems were not retained or made available to competent authorities, and statistics were not maintained on the use of search and production powers in relation to ML or TF investigations.

a2.26. **Criterion 33.1** – Malaysia maintains comprehensive AML/CFT related statistics. In June 2012 the NCC enforced a 'Centralized Data Management Framework' which came into effect in January 2013. The framework requires each NCC agency to adopt policies and systems to capture statistical data related to AML/CFT work across a range of relevant categories. These include financial intelligence (reports received and disseminated); investigation (cases investigated; amounts frozen, seized and forfeited); prosecution (cases prosecuted; forfeiture (criminal and civil) and international cooperation (MLA and extradition)); supervision (onsite and offsite examinations; sanctions); ML/TF typologies (sanitised cases based on ML/TF investigations) and AML/CFT training (events conducted and attended). The outputs of the cross-border reporting system are included. Financial Intelligence, investigation, prosecution and supervisory statistics are collected every four months and typologies and training statistics are collected annually.

a2.27. **Malaysia is rated compliant with R.33.**



Table of Acronyms

AGC	Attorney General's Chambers
ALB	Association of Labuan Banks
ALTC	Association of Labuan Trust Companies
AML/CFT	Anti-Money Laundering and Counter Financing of Terrorism
AMLA	Anti-Money Laundering and Anti-Terrorism Financing and Proceeds of Unlawful Activities Act 2001
AMLA	Regulations -Anti-Money Laundering and Anti-Terrorism Financing (Reporting Obligations) Regulations 2006
AMLDD	Anti-Money Laundering Division (IRB)
APG	Asia/Pacific Group on Money Laundering
ARIN-AP	Asset Recovery Interagency Network – Asia Pacific
ASC	Association of Stockbroking Companies Malaysia
ASEAN	Association of Southeast Asian Nations
BHEUU	Legal Affairs Division, Prime Minister's Department
BNI	bearer negotiable instrument
BNM	Bank Negara Malaysia
BO	beneficial owner
BVAEA	Board of Valuers, Appraisers and Estate Agents Malaysia
CA	Companies Act 1965
CADS	cash declaration system (BNM FIED database)
CBA	Central Bank of Malaysia Act 2009
CCID	Commercial Crime Investigation Department, Royal Malaysian Police
CCM	Companies Commission of Malaysia (also known as SSM)
CID	Crime Investigation Division, Royal Malaysian Police
CLBG	Companies Limited by Guarantee
CONG	Compliance Officers Networking Group
CMSA	Capital Market and Services Act 2012
CMSL	Capital Market Services Licence
CPC	Criminal Procedure Code
CT	counter terrorism
CTR	cash threshold report
DDFOPA	Dangerous Drugs (Forfeiture of Property) Act 1988
DFI	development financial institution
DNFBPs	designated non-financial businesses and professions
DPP	Deputy Public Prosecutor
DTA	double taxation agreement
EA	Extradition Act 1992

TABLE OF ACRONYMS

Egmont	The Egmont Group of Financial Intelligence Units
ETP	Economic Transformation Programme
FGJAM	Federation of Goldsmiths and Jewellers Associations of Malaysia
FI	financial institution
FIED	Financial Intelligence and Enforcement Division (The FIU)
FINS	FIED's online reporting system allowing two way secure communication with RIs
FSA	Financial Services Act 2013
GIFCS	The Group of International Finance Centre Supervisors
GTP	Government Transformation Programme
IBC	International Business Company
IBFC	International Business and Finance Centre
IC	Identity Card
IFC	International Financial Centre
IFSA	Islamic Financial Services Act 2013
INTERPOL	International Criminal Police Organisation
IOSCO	International Organisation of Securities Commissions
IRB	Inland Revenue Board
ISA	Internal Security Act 1960
ISIL	Islamic State of Iraq and the Levant
ISP	Interim Strategic Plan
ITA	Income Tax Act 1967
JAT	Jemaah Anshorut Tauhid
Jl	Jemaah Islamiyah
LCA	Labuan Companies Act 1990
LEA	Law Enforcement Agency
LFSA	Labuan Financial Services Authority
LFSAA	Labuan Financial Services Authority Act 2010
LFSSA	Labuan Financial Services and Securities Act 2010
LIBG	Labuan Investment Banks Group
LIIA	Labuan International Insurance Associations
LIFSA	Labuan Islamic Financial Services Act 2010LLP – Limited Liability Partnership
LLPA	Limited Liability Partnership Act 2012
LLPLLPA	Labuan Limited Partnerships and Limited Liability Partnerships Act 2010 LTA - Labuan Trust Act 1996
LTCA	Labuan Trust Companies Act 1990
LTTE	Liberation Tigers of Tamil Ealam
MACC	Malaysian Anti-Corruption Commission
MACCA	Malaysian Anti-Corruption Commission Act 2009
MACMA	Mutual Assistance in Criminal Matters Act 2003

MACS	Malaysian Association of Company Secretaries
MAICSA	Malaysian Institute of Chartered Secretaries and Administrators
MBC	Malaysian Bar Council
MDIC	Malaysia Deposit Insurance Corporation Act 2011
MDTCC	Ministry of Domestic Trade, Cooperatives and Consumerism
MER	Mutual Evaluation Report
MIA	Malaysian Institute of Accountants
MIBA	Malaysian Investment Banking Association
MICPA	Malaysia Institute of Public Accountants
MITI	Ministry of International Trade and Industry
ML/TF	Money Laundering and Terrorism Financing
MoF	Ministry of Finance
MOFA	Ministry of Foreign Affairs
MMoU	Multilateral Memorandum of Understanding
MSB	money services business (comprising MVTs and money changers)
MVTs	money or value transfer service
NCC	National Co-ordination Committee to Counter Money Laundering
NCID	Narcotics Crime Investigation Department, Royal Malaysian Police
NPO	non-profit organisation
NRA	national risk assessment
NTP	National Transformation Policy
OGBS	Offshore Group of Banking Supervisors (now GIFCS)
PEP	politically exposed person
PF	proliferation financing
RBA	risk-based approach
RSF	Risk-Based Supervisory Framework
RI	reporting institutions
RM	Malaysian Ringgit
RMC	Royal Malaysian Customs Department
RMP	Royal Malaysia Police
RMP AMLA Unit	Anti-Money Laundering Unit, Royal Malaysian Police
RoS	Registrar of Societies
SA	Societies Act 1966
SB	Special Branch, Royal Malaysian Police
SC	Securities Commission of Malaysia
SCA	Securities Commission Act 1993
SCONPO	Sub-Committee on Non-Profit Organisations
SOP	standard operating procedure

TABLE OF ACRONYMS

SOSMA	Security Offences (Special Measures) Act 2012
SRB	self-regulatory body
SRO	self-regulatory organisation
STA	Strategic Trace Act 2010
STS	Strategic Trade Secretariat
SuRF	Supervisory Risk-Based Framework
TA	Trustee Act 1949
TC	technical compliance
TCA	Trust Companies Act 1949
TCSP	trust and company service provider
TF	terrorist financing
TFS	targeted financial sanctions
TIA	Trustee (Incorporation) Act 1952
TIEA	Tax Information Exchange Agreement
UBO	ultimate beneficial owner
UNSCR	United Nations Security Council Resolution
VAEAA	Valuers Appraisers and Estate Agents Act 1981
WCO	World Customs Organisation
WMD	weapons of mass destruction