

**Middle East & North
Africa Financial Action
Task Force**



***Mutual Evaluation Report
Of
The Kingdom of Bahrain
On
Anti-Money Laundering and Combating Financing of
Terrorism***

This Detailed Assessment Report on anti-money laundering and combating the financing of terrorism for Bahrain was prepared by the International Monetary Fund. The report assesses compliance with the FATF 40+9 Recommendations and uses the FATF methodology of 2004. The report was adopted as a MENAFATF Mutual Evaluation by the MENAFATF Plenary on November 14th, 2006.

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KINGDOM OF BAHRAIN

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ACRONYMS

AECD	Anti-Economic Crime Directorate
AML/CFT	Anti-Money Laundering and Combating the Financing of Terrorism
AMLU	Anti-Money Laundering Unit (Bahrain's FIU)
BD	Bahraini Dinar
BMA	Bahrain Monetary Agency
BSE	Bahrain Stock Exchange
CCL	Commercial Companies Law
CDD	Customer due diligence
CID	Directorate General of Criminal Investigation
CPC	Criminal Procedure Code
CPR	Central Population Registration (identity card)
DDL	Directorate of Development and Local Societies
DL	Decree Law
DNFBP	Designated nonfinancial businesses and professions
FATF	Financial Action Task Force
FI	Financial institution
FIU	Financial intelligence unit
FSAP	Financial Sector Assessment Program
FSRB	FATF-style Regional Body
FT	Financing of terrorism
GCC	Gulf Cooperation Council
IAIS	International Association of Insurance Supervisors
KYC	Know your customer/client
ML	Money laundering
MLA	Mutual legal assistance
MLRO	Money Laundering Reporting Officer
MO	Ministerial Order
MOI	Ministry of Interior
MOIC	Ministry of Industry and Commerce
MOJ	Ministry of Justice
MSA	Ministry of Social Affairs
NCCT	Non-Cooperative Countries and Territories
NPO	Non-profit organization
PC	Penal Code
PEP	Politically exposed person
ROSC	Report on Observance of Standards and Codes
SER	Securities and Exchange Regulation
SRO	Self-regulating organization
STR	Suspicious transaction report
UN	United Nations
UNSCR	United Nations Security Council Resolution

A. PREFACE

1. An assessment of the anti-money laundering (AML) and combating the financing of terrorism (CFT) regime of Bahrain was based on the 2003 Financial Action Task Force (FATF) Forty Recommendations and the Nine Special Recommendations on Terrorist Financing of 2001. It was prepared using the 2004 AML/CFT Methodology. The assessment was completed between April 17–May 02, 2005. During the mission, the assessment team met with officials and representatives of all relevant government agencies and the private sector.

2. The assessment was conducted by a team of assessors composed of staff of the International Monetary Fund (IMF) and an expert acting under the supervision of IMF. The evaluation team consisted of: Ian Carrington and Tanya Smith (MFD) who addressed designated non-financial businesses and professions, and financial institutions, respectively, Joy Smallwood (LEG) who addressed legal and legislative issues, and Boudewijn Verhelst of the Belgium FIU who addressed financial intelligence and law enforcement issues. The assessors reviewed the institutional framework, the relevant AML/CFT laws, regulations, guidelines and other documents, and the regulatory and supervisory programs in place to deter money laundering (ML) and the financing of terrorism (FT) through financial institutions and Designated Non-Financial Businesses and Professions (DNFBP). The capacity, implementation, and effectiveness of all these systems were also reviewed.

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

B. EXECUTIVE SUMMARY

Legal Systems and Related Institutional Measures

4. ML is criminalized by Article 2.1 of the Decree Law 4/2001 with Respect to the Prevention and Prohibition of the Laundering of Money (“DL 4/2001”). The offence of money laundering extends to any type of property and applies to persons who commit the predicate offence: accordingly, self laundering is an offence. However it is not necessary that a person be convicted of a predicate offence in order to be convicted of a money laundering offence. The intentional element of the money laundering crime may be inferred from objective factual circumstances. Money laundering may also be ascribed to corporate bodies. Corporate bodies may be fined up to BD 1 million (USD 2.65 million). Corporate criminal liability for offenses does not limit civil or administrative liability. Financial institutions may also be separately sanctioned by The Bahrain Monetary Agency (BMA) and the Ministry of Industry and Commerce (MOIC). Natural persons may face a term of imprisonment up to 7 years as well as a BD 1 million fine (USD 2.65 million).

5. While DNFBPs are guided by legislation and implementing regulations, the financial sector is subject to a wider array of legal instruments. Legislation does provide a common framework in the financial sector, but implementing that legislation may be traditional regulations, circulars, or rulebooks. Despite the different names, the Bahraini authorities believe that all three have the force of regulation. However, in this context, it is important to note that the assessment identified an issue vis-à-vis the BMA's legal ability to issue the circulars and rulebooks and their ability to be enforced (if challenged) as a regulation.

6. The financing of terrorism is not currently a criminal offense in Bahrain. A draft law amending the provisions of DL 4/2001 is now in parliamentary committee. If passed, the amendments would create an offence of terrorist financing in Article 3.1 of the amended DL 4/2001. As the amendments currently read, the terrorist financing offence would not be fully compliant with international standards as it does not criminalize providing funds to a terrorist or terrorist organization and only criminalizes terrorist financing when the terrorist act, for which funds were provided, actually takes place. The assessment team provided recommendations to address these deficiencies and also recommended that the offence be drafted in the common law style in order to mirror the drafting of the money laundering offence in the same law. If this is not done DL 4/2001 (soon to be the AML/CFT Law 2001 (amended)) will have two styles of offenses and it may appear that the FT offence is not criminalized.

7. Under the provisions of DL 4/2001 it is possible to confiscate all property directly or indirectly derived from any criminal activity, as well as substitute assets and income yields. Alternatively all other property belonging to the convicted person, his spouse, or minor children is subject to confiscation up to the value equivalent to the laundered assets. *Bona fide* third parties can claim their rights before, during, and after the court proceedings. *Ex parte* seizure is provided for in DL 4/2001 and in the 2002 Code of Criminal Procedure (CPC) during the judicial procedure under the Public Prosecutor.

8. In the absence of a specific terrorist financing offence, both as a stand alone offence or as a predicate to money laundering, confiscation on these grounds is not possible. There is, however, the indirect exception in some cases on the basis of aiding and abetting offenses that occur in a terrorist context.

9. The Anti-Money Laundering Unit (AMLU) performs the typical FIU functions of receiving and processing the disclosures of suspected money laundering and related crimes forwarded by the entities subject to the reporting obligations of DL 4/2001. It also *de facto* receives and processes suspected terrorist related disclosures even though the financing of terrorism is not yet an offence in Bahrain. As a police-type FIU, the AMLU carries out its own investigations, has access to the appropriate information to perform its functions, and executes money laundering related court orders. It can query additional information directly from the disclosing entity, but has to address the court to obtain information and documents from other persons or entities. It can seize suspect assets upon receipt of a court order, but in urgent cases it can do so on its own authority for a maximum period of 3 days (see above).

10. The AMLU does not have a high profile with all reporting entities, especially DNFBPs. This might be related to the fact that reporting entities are also required to submit STRs to their primary regulator, with whom they inevitable have a closer working relationship. The mission recommended that the AMLU take steps to raise awareness about its role and functions and to issue further guidance on the filing of STRs.

11. The Public Prosecutor's Office is headed by a Prosecutor General, assisted by a Senior Advocate General, and is in charge of the (judicial) investigation and prosecution of offenses and as such it receives, investigates, and prosecutes cases forwarded by the AMLU. Furthermore the Public Prosecutor's Office supports the AMLU investigation whenever coercive measures are required, supplies legal advice to the police and supervises telephone tapping. The office also plays an important role in mutual legal assistance and extradition.

Preventive Measures—Financial Institutions

12. The BMA assumed responsibility for all financial institution licensees in 2002. This includes banks, insurance licensees, capital market licensees and money changers. The agency's Compliance Unit is responsible for implementing its AML supervisory program for all bank, insurance, and money changers licensees. The BMA's Capital Markets Division is responsible for the regulation of licensees in the security sector.

13. The BMA issued AML regulations in 2001, but these regulations only covered banks and money changers. Capital market licensees have been subject to AML regulations since 2004 and insurance licensees will become subject to such regulations in May 2005. Since 2001, the BMA has updated its regulations leading up to the issuance of the revised Financial Crimes Module of its Rulebook volumes for banks which became effective on April 5, 2005.

14. The rulebook provides broad coverage of AML supervisory issues and establishes a comprehensive framework for the application of the 40 + 9 Recommendations. Nevertheless, the mission has provided recommendations for the enhancement of the rulebook and other aspects of the supervisory framework in general.

15. The mission emphasized the particular importance of capital market licensees, but also money changers and money brokers, being subject to a supervisory regime comparable to that applicable to banks and insurance companies (when the financial crime module for insurance licensees becomes effective). The mission recommended that measures be taken to strengthen supervision of capital markets licensees in a number of areas including CDD measures, PEPs, introduced business, and the monitoring and reporting of suspicious transactions.

16. The broad challenge that lies ahead for the BMA is that of integrating the provisions of the rulebook and achieving consistency in the AML/CFT supervision for banks, insurance, capital market, and money changer licensees. This will be especially challenging in respect of capital market licensees as they will be regulated by the Capital Markets Division which does not currently have plans to issue regulations on AML/CFT

equivalent to the rulebooks for banks and insurance companies. In responding to these challenges, the BMA will need to increase its AML supervisory resources, in particular bringing insurance and capital markets expertise into the Compliance Unit.

Preventive Measures—Designated Non-Financial Businesses and Professions

17. The schedule to DL 4/2001 lists real property transactions, bullion dealing, legal practice and advocacy, audit and accountancy as activities covered by the legislation. The law does not cover casinos, company and trust service providers, and dealers in precious metals and stones. However casinos are not permitted in Bahrain and the authorities report there are no company and trust service providers. The Ministry of Industry and Commerce (MOIC) (the supervisor for DNFBPs), has determined that approximately 1,700 registrants fall into this category. At the time of the mission MOIC had undertaken 158 visits to DNFBPs for 2005. These visits were a part of the Ministry's regular program to check company registration requirements, but were used as an opportunity to raise AML awareness.

18. The assessment team expressed concern about the Ministry's ability to effectively regulate DNFBPs as its general supervisory powers appear to be specifically related to the Commercial Companies Law (CCL) and may not provide effective AML/CFT supervisory powers. Concern was also expressed about the Ministry's failure to properly consult with the Ministry of Justice in relation to its plans to supervise lawyers as DNFBPs.

Legal Persons and Arrangements & Non-Profit Organizations

19. The MOIC is responsible for the registration of all business in Bahrain. In undertaking its due diligence, the Ministry requires applicants to produce personal identification documents and evidence of beneficial ownership. Due diligence is undertaken on directors, shareholders, and partners of applicants.

20. There are measures in place to prevent the unlawful use of legal persons by money launderers, but these measures cover banking, insurance, money changers, and money brokers. Capital markets licensees are not currently covered.

21. The rulebooks for banks and insurance licensees have differing requirements, with more stringent requirements applied to banks. The bank rulebooks indicate that a "bank must obtain a signed statement from all new customers confirming whether or not the customer is acting on their own behalf or not." The rulebook requirements are further enhanced with the requirement that "where a customer is acting on behalf of third parties, the bank must obtain a signed statement from the beneficial owner(s) that he/they is/are the ultimate beneficiary or beneficial owner of the account/facility, and giving authority to the customer to act on his/their behalf."

22. The insurance rulebook more closely mirrors the requirements of the 2001 Regulation, with one exception. There is no requirement to make enquiries as to the structure of the company so as to sufficiently determine the provider of funds, the

principal owner(s) of the shares and those who have control over the funds; and for corporate customers to update them on significant changes to ownership and/or legal structure. However, the rulebook does require insurance companies to obtain a list of and verify the identity of the main shareholders of a legal entity holding 20% or more of the issued capital. In addition, CDD requirements are applied to beneficiaries of life insurance policies, with the added requirement that the insurance licensee must establish the relationship between the insured party and the beneficiary or beneficiaries.

23. Capital markets licensees are currently subject to Ministerial Order (MO) 7/2001 and Resolution 1/2004. The MO only covers the general topic of client verification and does not address specific issues such as CDD for legal persons or determination of beneficial owners. Resolution 1/2004 provides slightly more detail and requires that information on the “particulars of the company’s owners and its main shareholders” be obtained prior to account opening. It is not clear what action would be taken if the companies owners and main shareholders are themselves companies, trusts, or other legal arrangements.

24. The Ministry of Social Affairs (MSA) regulates non-profit organizations. The legal framework for the supervision of NPOs is established by a number of laws, which have the objective of establishing an environment of sound corporate governance for these organizations. In recent years, the Ministry has undertaken a review of the legal and regulatory framework for NPOs and implemented a number of changes to more directly address the vulnerability of NPOs to abuse for the financing of terrorism.

25. At the time of the mission there were 386 registered societies including 80 charities. The Directorate of Development and Local Societies (DDLs) has a staff of 4 persons to undertake its work. These resources are inadequate to allow the department to undertake reviews of the financial information submitted by societies or to undertake inspections of these organizations. As a result, the legislative changes that were made cannot be effectively implemented.

National and International Co-operation

26. Coordination and cooperation between supervisory agencies could be improved. Regarding coordination, there are numerous ministerial orders, regulations, circulars and rulebooks underpinning the AML/CFT program in Bahrain. The Policy Committee should take a central role in reviewing these instruments in order to ensure that there is a consistency of approach and a coordinated message.

27. Cooperative efforts between the FIU and the supervisory agencies are based on custom and practical considerations, not on specific legal provisions. The AMLU and the BMA, for example, are legally bound to a high degree of confidentiality, and there is no legal framework regulating or coordinating any cooperative relationship between these natural allies. Recognizing that confidentiality remains an important consideration, they should be able to exchange information on non-compliance with DL 4/2001 requirements by the reporting entities. Operational cooperation between law enforcement agencies, such as customs and police, is systematic and frequent.

28. Mutual legal assistance between judicial authorities is generally governed by Article 426–428 of the 2002 Code of Criminal Procedure (“Letters rogatory”). In money laundering related matters Article 8 of the Anti-Money Laundering Law 4/2001 gives the AMLU a specific responsibility in the execution of foreign assistance requests that goes beyond the cooperation at the FIU level. Under both regimes the assistance is broad and virtually unrestricted, not only in money laundering cases but also in FT cases. It does not require dual criminality (also for coercive measures), only that the execution does not violate the public order of Bahrain (Article 427 CPC). The absence of a formal FT offence does not affect the mutual legal assistance capacity as it is not subject to the dual criminality principle.

29. Extradition is possible even without a treaty although Bahrain does not extradite its own nationals. Extradition is subject to the dual criminality principle and reciprocity. As terrorist financing has not yet been criminalized, no extradition is possible on this ground. Extradition can be granted however when the facts can be qualified as aiding and abetting, or other complicity to, extraditable crimes that have happened in a terrorist context.

C. GENERAL

General information on the Kingdom of Bahrain

30. Bahrain is a constitutional monarchy, with a legal system based on a constitution issued in 1973 and subsequently amended in 2002. Bahrain has a bicameral legislature, known as the National Assembly, consisting of 40 elected members who sit in the Chamber of Deputies, and a Consultative Council of the same size appointed by the King.

31. The country’s legal system is based on a mix of common law, Shari'a (Islamic law) and other civil codes, regulations, and traditions. The judiciary is organized into three separate branches: the Civil law courts, the Criminal law courts and the Shari'a law courts. These courts respectively adjudicate all civil and commercial cases, criminal law cases, and all personal status cases involving Muslims. The 2002 Constitution, as amended, also established the Constitutional court to rule on the constitutionality of laws and statutes.

32. The Bahrain Constitution, as amended in 2002, separates the powers of the Executive, the Legislature, and the Judiciary. All Bahrain laws must be promulgated by the legislature. Prior to promulgation all laws are discussed and examined by the National Assembly and openly debated in both the Chamber of Deputies and the Consultative Council. They are then signed into power by HM the King of Bahrain and published in the Bahrain Official Gazette.

General Situation of Money Laundering and Financing of Terrorism

33. The authorities believe that Bahrain has a relatively low level of domestically generated criminal proceeds and therefore believe that the greatest risk of money laundering is related to foreign proceeds that might transit through Bahrain. Bahrain’s

well-developed banking system, along with its geographical location in the Middle East as a transit point along the Gulf and into South Asia make it a potential target for money laundering and terrorist financing activities.

34. Currently there are four money-laundering prosecutions under way. The predicate offenses are fraud, corruption, illegal gambling and pandering. All these cases originated from suspicious transaction reports (STRs) filed by banks; with the alleged launderers trying to place their illegal proceeds into the banking system.

35. The BMA has blocked five bank accounts belonging to 3 persons/organizations. The total amount blocked with respect to suspected terrorist financing is US\$10.3 million (as at February 15, 2005). The AMLU has in addition received 6 STRs from banks with regards to possible terrorist financing links (as at February 15, 2005). Four of these were received from banks about persons listed on the U.S. government's OFAC list who were trying to wire transfer funds to Bahrain. The Bahrain authorities have also stopped a credit card account of a suspected terrorist arrested in the United States, and provided financial information on him to the Financial Crimes Enforcement Network (FinCEN), the U.S. FIU.

36. As the authorities have identified, Bahrain is more likely to be used in the layering stage of money laundering rather than for other stages of the process. Its relatively large financial sector with a network of foreign branches and subsidiaries makes it particularly vulnerable to this risk. From the law enforcement perspective, the attraction of Bahrain as an international business and financial center evokes particular challenges. The traditional law enforcement approach that starts with a criminal and his activities and ends with the proceeds, is becoming increasingly inadequate to take on the effects of the globalization of the money flows into or through Bahrain. As the reporting system is expected to gain momentum, law enforcement, especially the FIU and the Public Prosecutor's office, will have to learn how to deal with a situation where the investigation must start with the detection of suspect money or assets in order to determine the illegal origin in a remote part of the world.

37. The legal answer to this challenge lies in the autonomy of the money laundering offence separated from its predicate criminality. Jurisprudence will need to be created in order to establish possibilities and boundaries of the prosecution and, specifically, whether the courts will require positive identification and/or proof of the predicate offence and, if so, to what extent. The cases that are pending before the court present a predominantly local connotation in relation to the predicate offence, facilitating the burden of proof for the prosecution, but this will become more and more of a luxury as the foreign money flows originating from foreign activity increase.

38. There are domestic factors that are relevant to the AML/CFT picture as well. FT is not yet criminalized. There are inadequate supervisory resources in place for most categories of institutions covered by the AML legislation, which also reduces the effectiveness with which the legal framework can be implemented. The assessment also highlighted weaknesses in national coordination mechanisms, best characterized by the absence of effective communication among major players in the national AML efforts.

Overview of the Financial Sector and DNFBP

39. The financial sector in Bahrain is comprised of banks, securities firms and brokers, insurance companies, money changers, and money brokers. There are currently approximately 360 institutions licensed by the BMA.

40. Licensing, supervision, and regulation of the financial sector is the responsibility of the BMA. In 2002, the BMA was made the consolidated supervisor for all financial institutions. As a result, insurance and capital markets licensees, who had previously been the responsibility of other ministries within the government, came under the BMA's regulatory umbrella. There has been a gradual transition period to accommodate these organizations and to build up the necessary staff and resources within the BMA to undertake the full range of work.

41. Another key element to be addressed during this transitional period is the process of BMA Executive Directors issuing circulars and other regulatory instruments. While substantively, Article 14(d) of the BMA Law allows for the issuance of "special regulations" regarding the "exercise of strict control over banks and other financial firms", Article 15 requires that these regulations be issued by the Chairman of the Board of Directors. Only if the Chairman has secured "the approval of the Board of Directors" may he authorize "the Deputy Chairman, the Director General, or other members of the Agency's staff to exercise some of his powers" such as issuing regulations. While the regulations, including the circulars, have been issued by the Executive Director, Banking Supervision, BMA management and counsel were unable to produce documents that demonstrated that the Board of Directors had agreed to a delegation in this matter. There is no question that the licensees consider circulars mandatory and are complying with the requests being made under them, but it will be important to ensure that the legal requirements identified in the Central Bank Law are fully addressed with respect to the circulars, rulebooks, and other documents taking the form of a "special regulation."

42. For banks, there are three licensing vehicles from which to choose, offered in both conventional and Islamic form. Full commercial banks are permitted to carry out retail and commercial banking activities, in BD, with residents and non-residents of Bahrain. Offshore banking units may carry out retail and commercial banking activities in any foreign currency, but only with non-residents, although they may be permitted to participate in Bahrain-specific domestic projects with appropriate approvals. The third category of banking licensees, the investment bank licensees, is allowed to carry out traditional investment and merchant banking activities, but only with non-residents of Bahrain. The investment banking license also permits loans and advances to be made to non-residents (excluding overdrafts) and deposits may be taken from non-residents, provided they are in a foreign currency and for a minimum value of US\$50,000. Of the licensed banks, 28 are Islamic banks.

43. Total consolidated balance sheet assets of the banking system (including Islamic banks) were \$118.9 billion at year-end 2004. The majority of the assets, approximately \$98 billion, were held by the offshore bank licensees, with three of those licensees

holding more than 50% of the \$98 billion. The Islamic banking assets comprised \$4.8 billion of the \$118.9 billion in the system.

44. The non-bank sector remains relatively small, but a priority within Bahrain is to encourage future growth. There were 56 onshore insurance licensees and 71 offshore insurance licensees as of year-end 2004; 10 offshore licenses have subsequently been cancelled. There are limited statistics available on offshore licensees for 2004, as only 39 companies had provided financial statements. However, as of year-end 2003, domestic insurance sector assets were approximately \$1.8 billion, with gross premiums of \$209 million. General insurance accounts for approximately three-quarters of domestic insurance underwritten, of which motor insurance accounts for more than half. However, gross life premiums have grown significantly over the past two years, and new entrants are coming into the insurance sector to meet expected increases in life products.

45. The capital markets of Bahrain have also experienced strong growth. There are 13 brokers that operate on the Bahrain Stock Exchange. The market capitalization for the BSE grew by over 40% to approximate \$13.5 billion in 2004.

46. Money changers and money brokers are two other licensees that fall under the financial institution designation in Bahrain. Currently, there are 17 licensed money changers and 3 money brokers.

47. All financial institutions must be registered with the Ministry of Industry and Commerce, as well as being licensed by the BMA.

48. DNFBPs listed in the appendix to DL 4/2001 include persons engaged in “legal practice and advocacy”, “audit and accountancy”, and “real property transactions.” Jewelers are not covered by any of the categories in the appendix. However MOIC considers them to be covered by the category “real property transactions” and includes them in their regulation of DNFBPs.

Audit and Accounting

49. The market consists of the big 4 audit firms, and 31 other local firms engaged in accounting or auditing services. All auditors must be registered in the Register of Auditors under Decree 26/1996. Only persons with appropriate academic qualifications may register. The Decree also provides for a disciplinary committee for auditors to be chaired by a judge of the High Civil Court. Audit firms are required also to be registered in the commercial register and have a valid commercial registration.

50. Audit firms in Bahrain also act in the capacity of company formation agents, assisting their clients to establish companies, as well as to make amendments to their clients’ commercial registration.

The Judicial System, Lawyers and Notaries

51. The judicial system in Bahrain is divided into two courts: the criminal courts, known as the “High Criminal Court” and civil courts known as the “High Civil Court”. Separately, there are also family law courts which are governed by Shari’a law. AML/CFT matters are brought before the Supreme Judicial Council. There are currently four AML cases pending before the court.

52. There are three international law firms operating in Bahrain under specific licenses issued by the Director General of Legal Affairs. The majority of law firms are sole practitioner Bahraini advocacies, with a small number of the larger local law firms operating in cooperation with international practices. While law firms are not legally required to register in the Commercial Register because their legitimacy can be drawn from an approval provided by the Ministry of Justice, a number of the firms have, nevertheless, chosen to do so for other practical reasons, such as permitting them to act as company formation agents.

Real Estate

53. The market is characterized by a small number of medium-sized property companies, and a larger number of small estate agents. Medium-size companies own their own property and rent out property, typically on a one year lease with rental payments made on a monthly or quarterly basis. Smaller estate agents work on a commission basis, typically a month or part thereof as commission for concluding a rental. There are a number of companies, all locally-owned by Bahrainis, which specialize in buying and selling property on behalf of owners. At December 31, 2004, 1,177 were included in the companies register under the Category “Real Estate Buying/Selling and Leasing.”

Non-profit Organizations

54. At the time of the assessment, there were 386 registered societies including 80 charities. The largest categories of societies are social societies (65), professional societies (51), foreign societies (43), foreign clubs (32), churches (20), corporations (20) Islamic charities (19) and women’s societies (15). MSA is of the view that most of these societies do not fit the profile of organizations that are likely to send funds abroad. According to the authorities, the category that is most likely to send funds or resources abroad is the Islamic charities. These organizations often sponsor orphans in foreign countries and send funds to support them. The department reports that two societies are known to send resources abroad. In instances of national or international disasters, societies can send funds abroad but must do so through the Red Crescent.

Overview of commercial laws and mechanisms governing legal persons and arrangements

55. Commerce in Bahrain is regulated by the CCL, Decree No. 21 of 2001; the Commercial Register Law, Decree No 1 (Finance) of 1961; the Commercial Law, Decree No. 7 of 1987; and the Commercial Agency Law, Decree No. 8 of 1998. Companies are

created under the CCL on the basis of a Memorandum of Agreement, which must contain, *inter alia*, the company name, address, names of the partners/promoters, the object (activities to be conducted); and capital. The CCL provides specifically for 8 types of companies, which include General Partnership; Limited Partnership; Joint Venture;¹ Shareholding Company; Limited Partnership by shares; Limited Liability; Single Person; and Holding Company.

56. Branches of foreign companies may be registered without the need for local incorporation on the basis of the Memorandum of Association and commercial registration in its country of origin. In such cases, a company resolution to establish the branch, together with a Power of Attorney issued in favor of the resident director and a guarantee from the parent to meet all of the obligations of the company in the Kingdom of Bahrain, are required, and all must be legalized. A branch of a foreign company is required to have a local Bahraini sponsor unless it operates as a regional office.

57. Bearer shares are legally permissible in Bahrain, as per the CCL. However, the MOIC, which is in charge of the corporate registry, indicates that it does not allow companies to issue these instruments. Decree Law 21/2001 does not permit the registration of offshore companies or brass plate companies. All companies must be resident and maintain their headquarters and operations in Bahrain. All companies and businesses registered in Bahrain must maintain proper books of account and supporting documents in accordance with the CCL, Decree 7/1987, and to which the Ministry has the right of inspection and judicial enforcement. However, it is worth noting that over 70 previously licensed “offshore” insurance companies are neither based in Bahrain, nor keep their records there. Ten of these licensees had their licenses revoked in April 2005.

58. The MOIC is responsible for the registration of all business in Bahrain. Businesses are required to be registered in the commercial register within one month of starting business. MOIC reports that, in practice, businesses are required to be registered prior to commencing operations and taking up occupation of premises. This role makes the Ministry an important first line of defense in the fight against money laundering and terrorist financing.

59. In undertaking its due diligence, the MOIC requires applicants to produce personal identification documents and evidence of beneficial ownership. It also reviews financial statements, and a “receipt of capital certificate” from the applicant’s bank indicating that funds deposited in the applicant’s account have been subject to bank’s AML procedures. Directors, shareholders and partners of applicants are assessed for their fitness and propriety.

¹ A proposed amendment to the law will delete this type, and in practice applications are refused.

Overview of strategy to prevent money laundering and terrorist financing

a) AML/CFT Strategies and Priorities

60. The AML/CFT program in Bahrain is largely directed and coordinated by the Anti-Money Laundering Policy Committee. The Policy Committee, with its inter-ministerial membership, is in a unique position to establish, coordinate, and ensure follow through of strategies related to AML/CFT. However, strategy and priority setting currently takes place more within the individual ministries as opposed to the Policy Committee itself.

61. At the time of the assessment, the key priorities of Bahrain, as established by the Policy Committee, were:

- Addressing terrorism and terrorist financing through legislative mechanisms: a new law has been developed to address terrorism, while terrorist financing is being addressed through legislative amendments to existing legislation. The Policy Committee has provided comments on the terrorist financing amendments, but has not been part of the legislative drafting process.
- Integrating all financial sector licensees into the BMA: Prior to 2002, the BMA was responsible for banks, money changers, and money brokers. However, in 2002, the BMA became the supervisor for all financial sector licensees. As a result, efforts continue with respect to integrating the capital markets and insurance licensees into the regulatory and supervisory environment of the BMA and building the appropriate resource base.
- Addressing FATF Special Recommendation IX: Bahrain recognizes that it must address the issue of cash couriers and this is under development within various governmental ministries. At this time, Bahrain appears to be moving toward a disclosure system, but that has not yet been finalized. During the on-site visit, it was not evident that the Policy Committee had a significant role vis-à-vis addressing SR IX. However, the assessment team was subsequently informed that a subcommittee was formed under the Policy Committee to review this issue. It is not clear what ministries are involved in this subcommittee, nor when their findings will become public policy.

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

62. The AML/CFT effort is taken very seriously in Bahrain and the Kingdom has worked very hard over the past few years to implement an extensive AML framework in order to address the risk of money laundering. Spearheaded by the AML Policy Committee, the front line AML effort is spread between various ministries and agencies.

AML Policy Committee

63. The Policy Committee is chaired by the Undersecretary of the Ministry of Finance and National Economy (MFNE) and is comprised of representatives of the government agencies and departments that play leading roles in Bahrain's AML regime. These

include the Ministry of Finance and National Economy, the Ministry of Interior, the BMA, the Bahrain Stock Exchange, the MOIC, the Ministry of Labour, the Ministry of Social Affairs, the Ministry of Foreign Affairs, and the National Security Agency. Meeting at least four times a year, the Policy Committee serves as an important coordination mechanism among these agencies and advisory body to the Council of Ministers on the development of national AML policy. The committee is not served by a full time secretariat and does not have day-to-day operational responsibilities. A recent addition of CFT to the remit of the AML Policy Committee has given added impetus to the AML/CFT effort.

The Anti-Money Laundering Unit (AMLU)

64. The AMLU is Bahrain's financial intelligence unit. It is a part of the Anti-Economic Crime Directorate (AECD) of the Ministry of Interior's General Directorate of Criminal Investigation. The AMLU has both an intelligence and investigative function and is able to seize and freeze assets. It receives suspicious transaction reports (STRs) which can be filed by any of the institutions covered by DL 4/2001.

65. In July 2003, the AMLU was admitted to the Egmont Group of Financial Intelligence Units. Between its inception in June 2001 to February 15, 2005, the AMLU has received a total of 294 STRs, of which 112 have lead to investigations, with 23 of referred to the Public Prosecutor, and a total of 4 cases currently being prosecuted before the courts.

The Courts and the Public Prosecutor's Office

66. The Public Prosecutor's Office is the key component of the AML law enforcement effort. There is a constant interaction between the Public Prosecutor's Office and the FIU. The Public Prosecutor's Office is headed by a Prosecutor General, assisted by a Senior Advocate General, and further consists of a National Advocate-General and 5 District Prosecutors with their deputies. The Public Prosecutor's office has moved from the Ministry of Interior to the Ministry of Justice following the enactment of the new constitution. The Public Prosecutor's Office is in charge of the (judicial) investigation and prosecution of offenses.

67. The role of the Public Prosecutor's Office, with regard to money laundering cases, consists of receiving, investigating and prosecuting the cases forwarded by the AMLU. Furthermore the Public Prosecutor's Office supports the AMLU investigation whenever coercive measures are required. The Public Prosecutor's Office also plays an important role in mutual legal assistance and extradition. In the absence of a specific TF offense, its authority is restricted because it can only act on suspicion of an offence.

The BMA

68. The BMA, as of 2002, is the consolidated supervisor of all financial institutions licensees in Bahrain. Since then, one priority within the BMA has been to ensure that the insurance and capital markets licensees are subject to the same level of regulation and

supervision in the area of AML/CFT as the banks. These efforts are still in transition. The BMA created a Compliance Unit in 2001 to focus specifically on AML/CFT inspection and regulatory issues, including receipt and review of STR filings (along with the AMLU). In addition, a full regulatory AML/CFT framework was just issued for insurance companies. Capital markets licensees are subject to a regulatory framework for AML/CFT that became effective in 2004. In addition, inspections are due to begin for AML/CFT compliance on both insurance and capital markets licensees in 2005.

The Ministry of Industry and Commerce

69. The Ministry of Industry and Commerce (MOIC) has taken on responsibility for supervising DNFBPs. It issued Ministerial Order 23/2002 as a legislative instrument for DNFBPs and also issued AML guidance notes in 2003. The Ministry reports that it has undertaken 178 visits to DNFBPs, which were mainly focused on raising awareness about their obligations under the Bahrain's AML regime. DNFBPs currently covered by the AML legislation are persons engaging in audit and accountancy, legal practice and advocacy, and real estate buying/selling and leasing. The Ministry has prepared an amendment to MO 23/2002 which proposes to widen the coverage of DNFBPs to include: precious metals and precious stones dealers; automobile buying, selling, and leasing; auctions and galleries, and other purveyors of high value goods; and moveable property. In addition, the Minister has the authority to add additional activities.

c) Approach concerning risk

70. For the financial sector, the BMA has introduced the risk-based approach to customer due diligence and ongoing monitoring through its new rulebooks on banking. The BMA's is not yet willing to require banks to conduct risk-sensitive CDD and monitoring, but the BMA is interested in encouraging banks to move in that direction so that risks in the financial institutions are better identified and addressed. Going forward, the BMA expects to make progress on the risk-based approach by working with industry leaders to develop standards and by looking to guidance issued by the international standard setters.

71. Simplified customer due diligence procedures are permitted by the BMA in select situations and enhanced monitoring of certain types of higher risk accounts is introduced in the new rulebooks for banks and insurance companies. If the customer is the BSE, a licensee of the BMA, a Ministry of the Gulf Cooperation Council (GCC), a FATF government, or a company where a GCC government is a majority shareholder, full CDD procedures do not have to be applied. One-off transactions of less than BD 6,000 (USD 15,915) also do not require full CDD. Another category of entities that may be subject to simplified CDD are those companies listed on GCC or FATF state stock exchanges that have equivalent disclosure standards to those of the BSE. In each of these cases simplified CDD is not appropriate if the person opening the accounts knows or has reason to suspect that the applicant is "engaged in money laundering or the financing of terrorism or that the transaction is carried out on behalf of another person engaged in ML or FT" (FC1.11.4).

72. The MOIC reports that its visits to DNFBPs included 20 to institutions/persons considered to be in a higher risk category. This category includes the larger DNFBPs and those that sell very high value goods.

73. The MSA has not, in general, adopted a risk-based approach to its supervision of NPOs. However, to ensure that the 80 charities are subject to an external audit, it meets the cost of an annual audit for these entities.

d) Progress since the last IMF/WB assessment or mutual evaluation

74. Bahrain was subject to an FATF/GCC mutual evaluation in October 2000. The report noted that there was a high level of commitment to fighting money laundering and that a number of initial measures had been implemented in this regard.

Some of the major concerns expressed in the report were:

- The absence of a money laundering offense.
- The lack of confiscation provisions that provide a full range of options for freezing and confiscating the proceeds of crime.
- The absence of regulations and other instruments that would allow regulators to provide detailed AML guidance to institutions for which they have supervisory responsibility.
- The need to strengthen the requirements for the reporting of suspicious transactions and to explicitly provide immunity for person making such reports.
- The need to create a central unit to receive STRs and to develop financial intelligence and investigation expertise.
- The need to verify that Bahrain could provide the full range of mutual legal assistance.

75. Since the mutual evaluation of October 2000, there has been sea change in the approach to AML within Bahrain. It began with the passage of DL 4/2001 regarding Prevention and Prohibition of Money Laundering. Implementing regulations issued by various ministries including the Ministry of Finance, the BMA, and the MOIC swiftly followed. In addition, the FIU was created. The AML Policy committee was also created to bring together all the key ministries and agency involved in the fight against money laundering. These measures have addressed virtually all of the major concerns expressed in the last evaluation.

76. With the revision of the FATF 40 plus Special 9 Recommendations, Bahrain has continued its efforts regarding AML. In addition to upgrading its existing AML framework, Bahrain is now engaged in the process of integrating the financing of terrorism into its laws, regulations, processes, and systems.

D. DETAILED ASSESSMENT

Table 1. Detailed Assessment

Legal System and Related Institutional Measures

Criminalization of Money Laundering (R.1 & 2)
Description and analysis
<p>Both the Vienna and Palermo Conventions have been ratified by DL 17/1989 and Law 4/2004. ML is criminalized by Article 2.1 of DL 4/2001 with Respect to the Prevention and Prohibition of the Laundering of Money. The offence of money laundering extends to any type of property. The English version of Article 2.1 of the DL 4/2001 states:</p> <p>“Anyone who commits the following actions and claims that the source of these funds is legal, shall be deemed to have committed a money laundering crime:</p> <ol style="list-style-type: none"> a. Undertaking any transaction pertaining to criminal proceeds while knowing, believing or being justified in believing that said proceeds are obtained from a criminal activity or from any act considered to be complicit in said activity; b. Hiding the nature of the crime’s proceeds, their source, location or the methods of dealing with said proceeds, and the activity, ownership or any right thereof while knowing, believing or being justified in believing that said proceeds derive from a criminal activity or from any act considered to be collusion in said activity; c. Acquiring, receiving or transferring crime proceeds while knowing, believing or being justified in believing that said proceeds derive from a criminal activity or from any act considered to be collusion in said activity; d. Keeping or holding crime proceeds while knowing, believing or being justified in believing that said proceeds derive from a criminal activity or from any act considered complicit in said activity.” <p>On first reading, the conduct constituting money laundering as described in Article 2.1 of DL 4/2001 is not fully consistent with the provisions of the Vienna and Palermo Conventions (respectively by Article 3, Section 1 b, i and ii and Section 1 c, i and iv; by Article 6, Section 1(a) and (b)) as use or conversion of property are not included as actions which would constitute an offence. After extensive discussions with the Ministry of Justice, however, it seems that this is due to a translation issue whereby Article 2(1)(a) of DL 4/2001 is not “conducting a transaction” but “conducting an operation” which is widely defined in Arabic and would include conversion, even though it is not specifically included in the English translation. As the Arabic version is legally binding, the assessment team accepts that conversion is included in the law although there are no cases to show this interpretation, given the newness of the AML regime.</p> <p>Property is defined to include movable and immovable, tangible and intangible property. Property does not include the concept of corporeal or incorporeal, nor does it specifically cover legal documents or instruments, including those in electronic or digital form, evidencing title. Again, the assessment team was advised by the Ministry of Justice that these would be included in the definition of property as the translation of property begins with “all things that have value” instead of the English translation of “property of every kind.”</p> <p>Criminal activity includes any activity which is a crime whether in Bahrain or in any other State. Proceeds of crime include property that is derived directly or indirectly, in whole or in part, from criminal activity, whether in Bahrain or elsewhere. Interestingly, this would mean that if financing of terrorism occurred in a foreign country which had criminalized FT, and the proceeds passed through Bahrain, a Bahraini money laundering case could be investigated and prosecuted as the predicate offence would have been a crime “elsewhere” which is all that is required by DL 4/2001. Mutual legal assistance could also be rendered on this basis, as dual criminality in Bahrain is only required for extradition.</p> <p>Pursuant to Article 2.3 of DL 4/2001, it is not necessary that a person be convicted of a predicate offence in order to be convicted of a money laundering offence. The intentional element of the money laundering crime</p>

may be inferred from objective factual circumstances pursuant to Article 253 of the CPC whereby a judge:

“shall adjudicate an action according to the belief that he has formed with full freedom. That notwithstanding, he may not base his judgment on any evidence not presented to him in the hearing.”

The Ministry of Justice confirmed to the assessment team that judges frequently use this provision in their deliberations in criminal cases. The Ministry of Justice also indicated that the “knowing, believing or being justified in believing” element of the money laundering offence would confer some discretion to the judiciary. The assessment team remains unconvinced of this argument. Bahrain takes an all crimes approach to predicate offenses for money laundering. Countries must criminalize, at a minimum, all designated offenses as set out in the FATF Glossary regardless of which approach they take to the number of crimes which may be predicates to money laundering. Bahrain has not criminalized terrorist financing although it has frozen funds under UNSCR 1267.

A draft law amending DL 4/2001 is in parliamentary committee and would criminalize the financing of terrorism. Other predicate crimes not yet criminalized include market manipulation, insider dealing, products piracy and piracy (on the seas). Predicate offenses for money laundering do extend to conduct that occurred in another country, which constitutes an offence in that country, as criminal activity includes any activity which is a crime in either Bahrain or any other state.

The offence of money laundering applies to persons who commit the predicate offence pursuant to Article 2.4 of DL 4/2001; accordingly, self laundering is an offence in Bahrain. Article 2.1 (a) of DL 4/2001 applies to all those who knowingly engage in ML activity. Money laundering may also be ascribed to corporate bodies pursuant to Article 2.5 of DL 4/2001, but the ancillary offenses in Articles 2.6 and 3.5 are not specifically extended to corporate bodies. Corporate bodies may be fined under Article 3.3 up to BD 1 million (USD 2.65 million). Natural persons may face a term of imprisonment up to 7 years as well as a BD 1 million fine pursuant to Article 3.1. Article 2 of DL 4/2001 specifies corporate criminal liability for offenses without limiting civil or administrative liability. Financial institutions may also be separately sanctioned by the BMA and the MOIC respectively.

Ancillary offenses are contained in Articles 2 and 3 of DL 4/2001 which cover all financial institutions and DNFBPs except those carrying out transactions relating to jewelry and other high value goods, such as automobiles, art galleries, and other purveyors of high value goods. A proposed amendment to Ministerial Order 23/2002 issued by the MOIC will cover these DNFBPs in the near future. Attempts to commit an offence and conspiring to commit an offence are criminalized by Chapters 6 & 7 of the Bahrain Penal Code 1976.

The AML regime is very new. Currently, there are only four cases before the courts and none have yet gone to trial. All the predicate offences are local predicate offences. There have yet to be any cases involving predicate offences committed abroad with the proceeds being laundered through Bahrain, as a regional financial center.

Recommendations and comments

- Criminalize the financing of terrorism so that it becomes a predicate offence for money laundering.
- Extend corporate criminal liability to infringements of the AML requirements penalized by Articles 2.6 and 3.5 of DL 4/2001.
- Criminalize other predicate crimes, such as market manipulation, inside dealing, product piracy, and piracy (on the seas).
- Specifically add legal documents or instruments, in electronic or digital form, evidencing title to the definition of property, particularly as Bahrain is a financial center.
- Specifically add use or conversion of property to the definition of activity of money laundering.

Compliance with FATF Recommendations

R.1	Partially compliant	ML scope is not fully consistent with Vienna and Palermo Conventions; financing of terrorism is not a predicate offence to ML
R.2	Largely Compliant	Extend corporate criminal liability to ancillary offenses in Articles 2.6 and 3.5

Criminalization of terrorist financing (SR.II)

Description and analysis
<p>While Article 2 of DL 4/2001 criminalizes money laundering, there is no provision criminalizing the financing of terrorism. In practice, terrorist funds have been frozen using the Royal prerogative. Currently, 5 accounts representing US\$10.3 million have been frozen pursuant to STRs filed by financial institutions in Bahrain but no further action has been taken.</p> <p>A draft law amending the provisions of DL 4/2001 is now in parliamentary committee. If passed, the amendments would create an offence of terrorist financing in Article 3.1 of the amended DL 4/2001. As the draft law currently reads, the terrorist financing offence would not be fully compliant with international standards as it does not criminalize providing funds to a terrorist or terrorist organization and only criminalizes terrorist financing when the terrorist act, for which funds were provided, actually takes place.</p> <p>The assessment team recommended substantive changes to the draft law in order that the law is fully compliant with international standards. More particularly, the assessment team recommended that the offence be enhanced to include the following concepts:</p> <p>“An act by any person who by any means, directly or indirectly, willfully, provides or collects funds, or attempts to do so, with the intention that they should be used or in the knowledge that they are to be used in full or in part:</p> <ol style="list-style-type: none"> a) to carry out a terrorist act, or b) by a terrorist, or c) by a terrorist organization. <p>The offence is committed irrespective of any occurrence of a terrorist act referred to in paragraph (1), or whether the funds have actually been used to commit such act.”</p> <p>While the Directorate of Legal Affairs for the Cabinet Office agreed to make some of the substantive drafting changes recommended, it was not prepared to introduce any new definitions of terrorist organization or terrorist even though the recommended drafting changes will use these terms. There is, therefore, only a definition for terrorism taken from the Islamic Conference Convention on Combating International Terrorism. This definition of terrorism is different than the one being used in the draft law on anti-terrorism. The mission was advised that altering amendments to existing articles was possible, but introducing new terms or articles was not.</p> <p>The assessment team also recommended that the offence be drafted in the common law style in order to mirror the drafting of the money laundering offence in the same law. This was rejected and so the DL 4/2001 (soon to be the AML/CFT Law 2001 (amended)) will have two styles of offenses and it may appear that the FT offence is not criminalized.</p> <p>The mission further discussed the situation regarding the current draft law with the Ministry of Justice who had a different draft of the law than the mission. The Ministry of Justice agreed with the mission that the draft law needed further work and also agreed to work on the draft in conjunction with the Legal Affairs Directorate of the Cabinet Office.</p> <p>When criminalizing the FT offence, legal drafters should ensure that the offence applies regardless of whether the person alleged to have committed the offenses is in the same country or a different country from the one in which the terrorist organizations are located or the terrorist acts occurred or will occur.</p> <p>Once terrorist financing is criminalized, it must become a predicate offence to money laundering. As Bahrain has taken an “all crimes” approach to predicate offenses, this will occur by operation of law.</p>
Recommendations and comments
<ul style="list-style-type: none"> • Enact proposed legislative amendments on criminalizing terrorist financing, particularly for the case of financing terrorist organizations or terrorists who have not committed a specific terrorist act. • Form a drafting sub committee of the AML Policy Committee who can coordinate drafting of all relevant AML/CFT laws with the Legal Affairs Directorate of the Cabinet Office before the bills are submitted to the

parliamentary process.		
Compliance with FATF Recommendations		
SR.II	Non-compliant	FT is not criminalized.
Confiscation, freezing and seizing of proceeds of crime (R.3)		
Description and analysis		
<p>Confiscation:</p> <p>With the ratification of both the UN 1988 Vienna and the 2000 Palermo Conventions, Bahrain has transposed the relevant measures pertaining to seizure and confiscation into domestic legislation, insofar as these measures were not already in force. In the absence of a specific terrorist financing offence, both as a stand alone offence or as a predicate to money laundering, confiscation on these grounds is not possible, except indirectly in some cases on the basis of aiding and abetting offenses that occur in a terrorist context.</p> <p>As a rule, confiscation is conviction-based. Article 64 of the 1976 Penal Code (PC) governs the general confiscation regime. It provides for the discretionary possibility for the judge to confiscate – without prejudicing the rights of <i>bona fide</i> third parties - the items seized “in connection with” an offence, and those “used or in the process of being used” in committing an offence (par. 1). Confiscation becomes compulsory when the items concern dangerous or prohibited materials (such as drugs, explosives, arms...) even “if not belonging to the accused” or if no conviction has been pronounced (par. 2). This seems to infer that for the confiscation of other goods there is a condition of the property belonging to the convicted person and this difference risks creating confusion. Items that are given as a reward, payment or compensation, intended to induce the commission of a crime are also subject to compulsory confiscation (par. 3).</p> <p>Decree Law 4/2001 on the Prevention and Prohibition of Money Laundering (DL 4/2001) installs a specific regime for ML cases. As <i>lex specialis</i>, it supersedes the <i>lex generalis</i> of the Penal Code where they differ. Article 3.2 of DL 4/2001 imposes the confiscation of all property constituting the object of the offence (the proceeds of crime laundered or to be laundered). As according to the definition in Article 1 of DL 4/2001 “proceeds of crime” covers all property directly or indirectly derived from any criminal activity, the confiscation measure also includes substitute assets and income yields. Alternatively all other property belonging to the convicted person, his spouse or minor children is subject to confiscation up to the value equivalent to the laundered assets. Although not expressly stated, it is understood that such equivalent value confiscation will only take place when the offence related assets have disappeared or when direct confiscation cannot be executed for any other reason.</p> <p>Deviating from the general conviction-based rule, confiscation is still possible when the suspect dies during the judicial enquiry (led by the Public Prosecutor) before the conviction, except if the heirs prove the legal origin of that property (proof onus reversal). Again, the rights of the <i>bona fide</i> third parties are protected. If the suspect absconds, criminal proceedings are still possible <i>in absentia</i>.</p> <p>Corporate criminal liability in ML cases is provided for in Articles 2.5 and 3.3 of DL 4/2001, imposing a fine on the “corporate body” beside the confiscation of corporation owned assets, which are the object of the ML offence. The liability of any natural person does not affect that of the corporate body, so both penalties may concur simultaneously. Corporate criminal liability is not a general rule in the Bahrain penal regime, as it was introduced especially for the money laundering offence and is at present only applicable in this specific context. Neither the Penal Code, nor DL 4/2001, however, define the concept and coverage of the terms “corporate” or “corporate body”, which may lead to interpretation problems and opens the way for court challenge. As there is no case law on this issue yet, the authorities are of the opinion that the term refers to any body that has legal personality as a “moral person” in the sense of Article 17 of the Civil Code, and that consequently can own assets liable for confiscation.</p> <p>While it seems clear that in the penal context the term “corporation” has a broader coverage than (commercial) companies and associations, it does not answer the question if other entities as, for instance, public bodies and authorities, municipalities and trade unions are included. It is not advisable to limit corporate criminal liability to one or more offenses anyway, as it may be considered needlessly and discretionarily discriminative, and lacking consistency. The concept of corporate criminal liability should be introduced in the PC as a general principle,</p>		

and clearly defined in terms of coverage *ratione personae*.

The *bona fide* third party can claim its rights before, during and after the court proceedings on the basis of the relevant Articles 104, 108 and 109 of Chapter IV of the 2002 Code of CPC. Goods are returned to the prejudiced party and any discussion in this context that is not solved by the trial judge is dealt with by the major criminal court in chambers. The Public Prosecutor plays a decisive role in this as seizure is within his prerogative.

Seizure:

Ex parte seizure is provided for in Article 73 (police seizure) and in part 2 of Chapter 2 (Articles 89 – 97) of the CPC during the judicial procedure under the Public Prosecutor. The terminology used is quite broad, including the seizure of evidentiary material, instrumentalities, objects of the crime and proceeds. Article 98 of CPC covers the equivalent value seizure of assets unrelated to the crime. Basically everything that may be the subject of a confiscation order can be seized as a conservatory measure.

Adequate and speedy detection of criminal proceeds is a prerequisite for any successful seizure/confiscation regime. In this respect, the efficiency of the AML system in terms of timely reporting is of primordial importance. There is room for improvement (*see below* on the STRs).

Other conservatory measures:

In the context of money laundering investigations, Article 6.1 of DL 4/2001 specifically provides for temporary conservation measures (“attachment and freezing” ... “prohibition of transfer”) for any property that is subject to confiscation according to Article 3.2. These measures must be issued by court order at the request of the AMLU. Even if still applicable, this regime is largely duplicated and superseded by the subsequent CPC provisions.

To avoid any risk of dissipation of suspect assets that may be subject to confiscation during the time it takes to obtain a court order (up to 2 days), the AMLU has the power to order the financial institution to freeze the assets for a maximum of 3 days, during which period a court order has to be obtained if extension of the measure is needed (Article 6.2 of DL 4/2001). The procedure allows for an appeal within 15 days, after which the decision becomes final until the end of the criminal proceedings. The court may also confer reasonable subsistence rights to the suspect and family members (Article 10.1).

Article 6 of DL 4/2001 provides the FIU with powers to identify and trace property that is or may become subject to confiscation or is suspected of being proceeds of crime. Preventing or voiding actions is also possible pursuant to this Article. Any contract aiming at subtracting any property from confiscation is considered null and void (Article 10.2 of DL 4/2001), subject to the *bona fide* third party rights’ protection.

No civil forfeiture procedures related to proceeds of crime exist in Bahrain, nor is there any reversal or sharing of the burden of proof provided in confiscation matters, except in the specific case of the heirs of the deceased suspect having to prove the legal origin (Article 3.2 of DL 4/2001). Confiscation of property belonging to criminal organizations cannot be pronounced *in se*, since there is no such autonomous offence.

Recommendations and comments

- Criminalize corporate liability in the Penal Code and clearly state to which bodies corporate criminal liability applies.
- Beside the lacuna created by the absence of an autonomous or predicate FT offence, the seizure and confiscation regime is quite comprehensive, but would benefit from clarifying the condition of the property belonging to the defendant or not, especially in the context of proceeds of crime; expressly stating when the equivalent value confiscation is applicable; introducing corporate criminal liability as a general rule to allow confiscation of corporate assets outside the specific ML context and consideration to extend the mandatory confiscation to all objects of an offence beyond the specific ML context.
- Amend Article 64, paragraph 2 of the PC in respect of the condition of the property (not) belonging to the accused.

Compliance with FATF Recommendations		
R.3	Partially compliant	No confiscation in terrorist financing cases. Efficiency may be affected by both misinterpretation of condition to confiscation and lack of clear delineation of the corporate criminal liability concept. No effective confiscations have been pronounced on money laundering cases yet.
Freezing of funds used for terrorist financing (SR.III)		
Description and analysis		
<p>Under SR III, countries should have laws and other procedures in place to freeze terrorist funds and other assets of persons designated pursuant to both UNSCR 1267 and UNSCR 1373. As terrorist financing is not criminalized in Bahrain, there are no laws to adequately comply with this. See discussion regarding this matter at SR II and discussion of procedures below. Laws and other measures should also provide for provisional measures, including the freezing and/or seizing of property, to prevent any dealing, transfer or disposal of property subject to confiscation and such freezing should take place without delay and without prior notice to the designated persons involved. This is not currently possible in law in Bahrain. There are currently, however, provisions in Articles 98 and 99 of the CPC dealing with restraint of property on application to the court by the Public Prosecutor where there is a criminal investigation underway. It is possible that this may be used as a measure of restraint in the future when financing of terrorism becomes a crime. This would likely necessitate, however, that a criminal case be opened in Bahrain in order to freeze or seize assets in Bahrain at the request of another country under a 1373 request.</p> <p>In practice, this requires a country to have a designated authority to receive in place that receives both the UNSCR 1267 and UNSCR 1373 requests. In Bahrain, this authority is the Directorate of International Organizations at the Ministry of Foreign Affairs. With regard to UNSCR 1267, the Ministry of Foreign Affairs distributes the lists that it receives from the UN to the BMA, the Ministry of Interior, the NSA and Ministry of Finance by both fax and by courier. The lists are sent to the relevant Minister or, in the case of the BMA, to the Governor. The four parties receiving the lists disseminate them as appropriate in their ministries. The BMA circulates the lists to their financial institutions by circular addressed to each licensee. The circular is issued by H.H. the Prime Minister and the Chairman of the Board of the BMA. The circular may not be binding, however, as Article 14 of the Agency Law allows for the issuance of “special regulations” and it is unclear that the circular is a special regulation. It is clear, however, that licensees consider themselves bound by the circulars. The Capital Markets Directorate of the BMA also sends a separate copy of the list to the BSE and asks that they distribute it to the stockbrokers. The MOIC does not receive a copy of the list. The NSA receives a copy of the list as it relates to matters of terrorism.</p> <p>Should any names match those on the UN list, the accounts are blocked by the financial institution in question and the matter is reported to the regulatory body in charge, then to the FIU. The Ministry of Foreign Affairs is then notified and they correspond with Bahrain’s UN mission in New York who notifies the UN 1267 Committee. This is the procedure that was utilized in 2002 when five accounts belonging to 2 persons/organizations were blocked by the BMA as the names matched those on the 1267 list.</p> <p>With regard to implementing a procedure for requests for freezing of funds received by another country under UNSCR 1373, the same procedure described above for UNSCR 1267 is employed. While the Ministry of Foreign Affairs is technically the designated authority, it sends requests to the same four entities as for the UNSCR 1267 lists. In practice, Bahrain takes the view that unless the person is listed on the UNSCR 1267 list, no action will be taken unless that person or entity is engaged in an activity which is contrary to the penal laws of Bahrain. Each individual Ministry who receives the list reviews it to see if the entities listed may be in breach of Bahraini law within the remits of the each of those respective ministries. No cases of breaches of Bahraini law have been reported in these circumstances. The process is then complete as far as the Foreign Ministry is concerned.</p> <p>The procedures for UNSCR 1373 are not compliant with international standards as the designated authority is required to designate an entity (or not) without delay by ensuring that a prompt determination is made. In the case in Bahrain, this determination is not being made by the Ministry of Foreign Affairs, but is instead being delegated to the various ministries who receive the request; no unified single decision is being made. While a</p>		

committee approach is acceptable, the committee would need to formally meet and make this unified single decision promptly. Alternatively, a single entity or person could make such a determination. If there was a positive determination by that person or entity regarding a terrorist target, that determination must then be promptly communicated to the appropriate ministries in order to initiate a freezing action and the subsequent freezing of funds or other assets without delay, through a court order or otherwise.

There must also be procedures in place so that, in a case where Bahrain did designate a terrorist target from a 1373 request, all entities that may be holding terrorist funds or assets would be notified of the designated persons. This would include being able to notify both financial institutions and other persons or entities that may be holding terrorist funds or assets. As “assets” are defined widely to include property of any kind, physical goods would be included in this definition and therefore traders who are trading in physical goods are also caught by this provision and need to be notified of terrorist targets. Note that this system could also be used if the NSA in Bahrain decided to issue its own list of terrorist targets. The names could then be circulated through the same committee and any terrorists’ funds or assets could be frozen using the above procedure. The list could also be distributed on a bilateral or regional basis to other countries with the request for assistance in freezing any funds or assets of the targeted persons or entities.

Procedures should also be in place to consider de-listing requests, unfreezing funds and other assets of delisted persons or entities, as well as procedures for unfreezing funds or assets of persons or entities inadvertently affected by a freezing order. Rights of bona fide third parties must also be protected. Article 6.2 of DL 4/2001 gives third parties the right to appeal to the Courts any freezing order, within 15 days of its issue and could also be utilized to facilitate these above requirements. There should also be procedures in place for allowing payment of basic living expenses and fees in line with UNSCR 1452, as well as procedures for court review of designation decisions made by the committee. Bahrain will also need to implement an effective system for monitoring compliance with such a system. This could be incorporated into the on-site inspections currently being undertaken in various sectors in Bahrain.

In practice, the AMLU has received 9 STRs from banks with possible terrorist financing links. Four of the STRs were received from banks regarding attempts to wire funds from Bahrain to persons overseas who were on the US OFAC list. The banks themselves were independently reviewing the OFAC list and the action taken was not as a result of a specific request from the United States. The Bahraini authorities also stopped a credit card account of a suspected terrorist arrested in the United States and have provided financial information on that person to FinCEN, the U.S. FIU.

It is also noted that Article 6.1 (c) of DL 4/2001 allows the AMLU to apply to the investigating magistrate to obtain an order attaching or freezing any property related to the offence of money laundering. Article 6.2 allows the AMLU to attach property without a court order for a period of up to 3 days. When the proposed CFT amendments to DL 4/2001 are passed, the AMLU would be able to use its 3 day freeze order to freeze funds of 1373 targets without delay after a prompt determination has been made. A court order could then be applied for during the three day freeze period.

Criminal sanctions will be applicable once the amendments on FT have been made to DL 4/2001. Other sanctions would be applicable as for money laundering. The authorities should consider how they would wish to monitor this designation system once it comes into effect.

Recommendations and comments

- Criminalize the financing of terrorism in order to then create a designated agency or committee in this area.
- Designate a committee or agency to be the 1373 designated agency who can make a prompt and binding determination regarding terrorist targets designated by other countries.
- Have systems in place whereby notification of such a designation can be disseminated to all parties who may be holding terrorist funds or assets so that such funds or assets can be frozen without delay.

Compliance with FATF Recommendations

SR.III	Partially compliant	FT is not criminalized. There is no 1373 designated agency who can make a prompt determination that binds the government of Bahrain to trace and freeze/seize terrorist assets.
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The Financial Intelligence Unit and its functions (R.26, 30 & 32)

Description and analysis

The Financial Intelligence Unit for Bahrain is the AMLU, a police unit created by Article 4.4 of the Law 4/2001 for the Prevention and Prohibition of Money Laundering and receiving operational status since 12 June 2001 pursuant to Ministerial Order (MO) 102/2001. It plays a pivotal role in the anti-money laundering regime, as it receives and investigates all STRs from the entities subjected to Law 4/2001 and all other money laundering related information from other sources. Structurally, it is an autonomous component of the Anti Economic Crime Directorate (AECD) located within the Directorate General of Criminal Investigation (CID) of the Ministry of Interior. Beside the Head of the unit with Colonel rank, it numbers 7 full-time staff (2 investigators, 1 IT/Analysis specialist, 4 support staff) and 2 part-time legal advisors.

The powers and functions of the AMLU are defined in MO 18/2002. The AMLU performs the typical FIU functions of receiving and processing the disclosures of suspected money laundering and related crimes forwarded by the entities subject to the reporting obligations of the DL 4/2001 (hereafter “the reporting entities”). It also *de facto* receives and processes suspected terrorist related disclosures. The use of a standard form is encouraged, but STRs submitted in other forms are also accepted. No guidance on filing STRs has been issued by the AMLU. A secure online STR submission system was recently started and is presently being used by 57 financial institutions. The FIU also receives money laundering related information from other sources (see below) which are considered an STR and recorded as such.

Being a police-type FIU, it not only has an intelligence function, but also carries out its own investigations, has access to the appropriate information to perform its functions, and executes money laundering related court orders. It can query additional information directly from the disclosing entity, but has to address the court to obtain information and documents from other persons or entities (Article 6(1)(a) of DL 4/2001). It can seize suspect assets upon court order, but in urgent cases it can do so on its own authority for a maximum period of 3 days (see above). As part of the AECD, it has access to all police resources and to the information held by other State authorities. The investigation routinely also focuses on the probable predicate criminality. If there is enough *prima facie* evidence to warrant a prosecution, the case is forwarded to the Public Prosecutor, who then either continues the (judicial) investigation or starts criminal proceedings. Currently criminal proceedings have been initiated in 2 money laundering cases, with 2 other cases pending. In these particular cases it took about 1 month between the filing of the STR and the conclusion of the investigation. The length of an STR investigation is varies significantly however, as there are still ongoing investigations dating from 2003.

STR related information held by the AMLU has “top secret” status and is protected as such. Physical access to the premises and the STR files is highly secured. The STR database is a stand alone and separated from the internet network and online submission system. Access to the database is protected and a history log of any user’s action is maintained. Finally, the AMLU staff is bound to the confidentiality provision of Article 371 of the PC. General statistics are, however, periodically released on the AMLU website; FATF typologies are also placed on the website as Bahrain does not yet have any of its own typologies.

Given the support of the Ministry of Interior, the number of staff and resources seem adequate for the moment. The FIU members have received appropriate training in law enforcement or IT/analysis. They also attend specific AML/CFT training sessions in national and international fora, besides drawing on their own “on the job” experiences. High integrity standards are observed for the FIU staff: the investigators are police officers who have undergone scrutiny when entering the force, whereas the IT analyst has been sourced from Ernst & Young. Corruption is not a serious problem in Bahrain, and social control in a small community such as Bahrain is high.

The international cooperation component and mission of the AMLU is important (see below). The unit was recognized as an Egmont Group member in July 2003. Its cooperative relations with other FIUs are guided by the Egmont Group’s Principles of Information Exchange.

<p>Regular contacts take place between the FIU officers and the MLROs to streamline and enhance the reporting. The FIU manages its own public website which is used as a way of providing feedback of relevant information to the reporting entities and the public.</p> <p>The AMLU keeps statistics on its activities. All STRs, including information from sources other than the reporting entities, are investigated by the AMLU as potential ML cases. For analysis of the statistical figures and conclusions, see below (suspicious transaction reports). No statistics are kept on the number of spontaneous referrals to foreign authorities. The FIU should periodically review the effectiveness of its systems to combat ML and FT.</p>		
<p>Recommendations and comments</p> <ul style="list-style-type: none"> • The FIU should periodically review the effectiveness of its systems to combat ML and FT. • The FIU should issue guidance on filing STRs to raise awareness and to ensure consistent understanding of its role in the AML/CFT framework. 		
<p>Compliance with FATF Recommendations</p>		
R.26	Largely compliant	No guidance on filing STRs has been issued by the FIU.
R.30	Compliant	
R.32	Largely compliant	The FIU is not periodically reviewing the effectiveness of its systems to combat ML and FT. No statistics kept on the number of spontaneous referrals to foreign authorities.
<p>Law enforcement, prosecution and other competent authorities—the framework for the investigation and prosecution of offenses, and for confiscation and freezing (R.27, 28, 30 & 32)</p>		
<p>Description and analysis</p>		
<p>Police:</p> <p>The AMLU is the designated law enforcement agency for AML/CFT investigations. In the absence of a formal and autonomous FT offence, the CFT component is restricted and viewed either under the money laundering or the aiding and abetting offence. As a police-type FIU, the AMLU has the normal law enforcement powers at its disposal to conduct police investigations and gather evidence, including taking witness statements. Coercive measures, such as searches and seizures, need the authorization of the judicial authorities (Article 6 of DL 4/2001), though in urgent cases or <i>in flagrante delicto</i> they can act on their own authority (Articles 67-73 of the CPC; Article 6.2 of DL 4/2001). Postponing arrests or seizure for investigative and suspect identification purposes is also considered to be within their normal police powers, although this assertion is not supported by any formal legal text. Where it is normal police practice to choose the appropriate moment to arrest a suspect, the postponement of seizure is less obvious, as this may infer allowing an offence to be (continued to be) committed without intervening (<i>e.g.</i> drug trafficking and transportation). Such tolerance needs, at a minimum, to be subject to judiciary control and formally regulated in terms of conditions and modalities to give the law enforcement officer firm guidance.</p> <p>Telephone tapping is provided for in Article 93 CPC and is conducted under the supervision of the Public Prosecutor after court authorization. There is a practice of other special investigative techniques such as controlled delivery, undercover operations and observation, again without being formally regulated. Jurisprudence on entrapment, provocation and other illegal evidence collection exists, that may set some guidance to the use of those techniques. These techniques have not yet been used in ML investigations however. Multi-disciplinary investigative teams and cross-border coordinated actions are possible and have indeed already been used. The establishment of a unit specialized in tracing, seizing and managing proceeds of crime is not under consideration, as the AMLU is thought to be adequate in that respect. Multi-disciplinary review of the money laundering situation is done within the Policy Committee.</p>		
<p>Customs:</p>		

The Bahrain Customs Authority numbers approximately 600 officers which is an adequate figure. They have the usual customs investigating powers, including the right to stop people and goods at the border, and checking for, searching and seizing restricted and prohibited goods (e.g. arms, drugs...). The law does not designate this authority with a specific AML role, but in practice money is considered to be a good that is subject to customs inspection. If there is a suspicion of criminal proceeds (mainly because of the large amounts of cash), Customs feel empowered to stop and seize (see below). There is a *de facto* consultation/cooperation process with the BMA and the AMLU, and whenever the suspicion is upheld, the police are called in.

The statistics kept by the Customs show a certain drug transportation activity at the borders, mainly of soft drugs although also some relatively important seizures of heroin have taken place in the recent past (10.3 kg in 2003; 9.5 kg in 2004) and there is definitely a traffic in drug tablets (more than 70,000 tablets in 2002 and 2004, 39,050 in 2003). Although not indicative of a serious psychotropic or drug scene, it does raise questions about the amount of drug proceeds that circulate in Bahrain and to what extent the reporting system is able to catch it.

International cooperation with other Customs authorities is extensive, and with any unusual cross-border transport enquiries are made with the Customs authorities of the country concerned. The Bahrain customs is a member of the World Customs Organization.

NSA:

The National Security Agency (“NSA”) has been a separate ministry with a direct reporting line to the Prime Minister since 2004. It has the jurisdiction over counter terrorist operations. Previously, NSA was part of the Ministry of the Interior. NSA has all of the investigation and arrest powers necessary to perform its functions. NSA frequently exchanges information and intelligence with other GCC member countries. Regarding training, NSA has frequent internal training programs and has also received training from the U.S. Department of State. NSA indicated that they had adequate staff but would not reveal the number for national security reasons.

Public Prosecution:

The Public Prosecutor’s Office obviously is the key component of the AML law enforcement effort. There is a constant interaction between the Public Prosecutor’s Office and the FIU. The Public Prosecutor’s Office is headed by a Prosecutor General, assisted by a Senior Advocate General, and further consists of a National Advocate-General and 5 District Prosecutors with their deputies. In total the Office consists of 37 members. The Public Prosecutor’s office has moved from the Ministry of Interior to the Ministry of Justice as part of the Judiciary Power since 2003 (Article 36 Constitution). The Public Prosecutor’s Office is in charge of the (judicial) investigation and prosecution of offenses.

The role of the Public Prosecutor’s Office, with regard to money laundering cases, consists of receiving, investigating and prosecuting the cases forwarded by the AMLU. Furthermore the Public Prosecutor’s Office supports the AMLU investigation whenever coercive measures are required (cfr. Article 6.1 of DL 4/2001 and the CPC), supplies legal advice to the police and supervises telephone tapping (Article 93 of the CPC). The Public Prosecutor’s Office also plays an important role in mutual legal assistance and extradition. In the absence of a specific TF offence, its authority is restricted because as it can only act on suspicion of an offence. The public prosecutors need to meet high integrity and professional standards, and are bound to confidentiality pursuant to Article 371 of the PC, as are all other law enforcement officers.

There is presently a reorganization in the access to the magistrature, whereby all candidates have to pass an examination committee of legal experts and practitioners (judges, prosecutors) before being appointed by the King. This procedure is expected to start by the end of the summer, but it now has a delaying effect on the recruitment of new magistrates. It is hoped that 10 to 15 new prosecutors will take up their function shortly. This reinforcement of the judiciary indeed seems necessary in the light of the increased input as a result of a more productive functioning of the reporting system, and the intention to create specialist prosecutors for taking on ML and FT cases efficiently. The performance rate of the Public Prosecutor’s Office is quite high, as 97% of the cases initiated in 2004 were finished by the beginning of 2005. The Courts however are confronted with a backlog.

The Public Prosecutor is highly conscious of the need for training of the magistrates focused on money laundering and terrorist financing, and the new approach that an efficient fight against those criminal phenomena requires. A training course for judges and public prosecutors on financial issues including money laundering was organized in February 2004 to June 2004 in coordination with the Bahrain Institute for Banking and Financial Studies. There are now on-going training programs and seminars covering AML topics. There is a strong appeal for outside investigative and jurisprudential experience and expertise to introduce the Bahrain judiciary authorities to new ways to cope with such serious forms of criminality.

LE Statistics:

For the AMLU: see below. (*Suspicious transaction reporting*)

The Public Prosecutor’s Office is presently considering 4 cases, 2 of which are pending before the court. No confiscations have been pronounced as yet in ML cases. Annual statistics are kept on the criminal situation and judicial actions. The statistics provided to the assessment team did not, however, contain information on the amount of seized and confiscated criminal proceeds. Such statistics should be kept on criminal proceeds in general, not only on money laundering or terrorist financing.

Effectiveness:

The AMLU centralizes all information related to ML and (*de facto*) FT and as such is the only provider of such cases to the Public Prosecutor. Out of the 330 STRs that the FIU received since the inception of the reporting system on 12 June 2001, 24 STRs (or 7%) constituting 18 cases were forwarded to the Public Prosecutor, of which only 4 cases related to money laundering (or 1.25% of the total STRs) reached the next to final stage of prosecution (status on 17/4/2005). This number may yet increase in the near future as 147 STRs are still under investigation. Of the other 14 cases relating to other forms of criminality 1 case ended in an acquittal, with 5 cases still pending before the court. These figures are modest, although it is a positive and hopeful sign that at least some cases have been brought to court.

The efficiency of the whole law enforcement effort is being put to the test, and a lot will depend on the outcome of the court’s decision in the AML cases currently before it. The key issue in any ML prosecution is the extent of the burden of proof on the predicate criminality. The 4 ML cases all have a predominant local character and in every case a predicate criminality was identified (prostitution, illegal gambling, fraud, bribery). Although no conviction is needed for the predicate offence (Article 2.3 of DL 4/2001), it remains to be seen if the courts require positive and formal proof of the specific predicate criminality, or will satisfy themselves with a lesser proof requirement, such as the condition of only having to prove any illegal origin of the assets as a consequence of the all-crime coverage of the money laundering offence.

Recommendations and comments

- Introduce an autonomous and predicate FT offence required to complete the AML/CFT regime.
- Formally regulate the conditions and modalities for postponing or waiving seizure.
- Create jurisprudence that will give direction to law enforcement regarding achieving efficiency in terms of convictions and asset recovery.
- Reinforce the human resources of the Public Prosecutor’s Office in the expectation of an increased demands related to AML/CFT and the specialization of the prosecution.
- Keep statistics on the amount of criminal proceeds seized and confiscated.
- Review the effectiveness of the evidence gathering process regarding anti-money laundering.
- More cases have to be submitted to the courts, not limited to local events but particularly those with an international connotation where the assets appear in Bahrain, but the predicate activity occurred outside the national territory. The ensuing jurisprudence will show if prosecution of ML as an autonomous offence, separated from its predicate criminality, stands a real chance for positive results.

Compliance with FATF Recommendations

R.27	Largely compliant	<i>De facto</i> investigation of FT offenses. No formal regulation for postponing or waiving seizure.
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R.28	Partially compliant	No autonomous or predicate FT offence as legal basis for investigative/compulsory measures.
R.30	Largely compliant	Greater output needed to prosecution and court to create guiding jurisprudence on autonomous character of the ML offence (efficiency rating). Reinforcement of Public Prosecutor's Office advisable.
R.32	Partially compliant	No statistics on the amount of criminal proceeds seized and confiscated. No effective review of system undertaken.
Cash couriers (SR.IX)		
Description and analysis		
<p>Bahrain Customs control three borders: at the seaport, the airport and the causeway to Saudi Arabia. Bahrain has not introduced a cash or bearer negotiable instruments declaration system at these borders, nor is there a disclosure obligation. The Government is contemplating the introduction of a declaration system on the basis of recommendations being formulated by an ad hoc subcommittee of the Policy Committee. Most checks and screenings are done on a selective/random basis (up to 14,000 cars per day may pass the causeway border). When people are found to be carrying large cash amounts and are unable to provide a valid explanation, the police is called in under the suspicion of criminal proceeds. Articles 24 (prohibited and restricted goods), 128 (smuggling and contraband) and 142 (definition of smuggling) of the GCC Common Customs Law empower the Customs authority to carry out searches, detain persons and seize goods (which then would also include cash and negotiable instruments). This practice is based on an interpretation by the Customs authorities and is not expressly provided for in the law.</p> <p>Between 2001 and 2004, 30 persons were intercepted in this context, with a total of US\$14,054,000 involved. None of these instances, however, led to a prosecution or a police investigation (see statistics AMLU).</p>		
Recommendations and comments		
<ul style="list-style-type: none"> • Develop a disclosure or declaration system for the Bahrain borders. This is being envisaged in Article 5bis of the draft amended AML law. • Address the legal basis of the Customs interception of large cash amounts, which is open to challenge • Consider adding a legal provision to the amendments planned for DL 4/2001 regarding false declarations/disclosures and lack of declarations/disclosures under the proposed disclosure system. 		
Compliance with FATF Recommendations		
SR.IX	Non-compliant	A declaration or disclosure system and full regulation of the Customs' powers of interception has not been put in effect.

Preventive Measures—Financial Institutions

Risk of money laundering or terrorist financing
Description and analysis
<p>A key risk for the BMA is the lack of integration of the capital markets and insurance licensees into the BMA framework for AML/CFT compliance. Neither of these licensees has been subject to an onsite inspection for AML/CFT and none have ever filed an STR. In addition, the insurance licensees have never been subject to a comprehensive regulatory framework for AML/CFT. This has now been addressed with the issue of insurance rulebook in May 2005, which has the effect of a regulation. However, the real work will begin with implementation efforts. Capital markets licensees have been subject to regulations on AML, but not CFT, since the passage of Resolution 1/2004. However, the Resolution is significantly lacking when assessed against international standards and it is difficult to identify the level of implementation given the lack of supervisory inspections to date, although discussions with industry participants identified some concerns.</p> <p>The situation for the banking licensees is better, both with respect to the regulatory environment, as well as implementation efforts. Banks have been subject to detailed regulatory requirements since 2001, which has given them a lead in implementation within the financial services industry in Bahrain. The regulations were further strengthened when the Financial Crimes Module in the rulebooks became effective in early April 2005; the</p>

Module covers conventional banks and Islamic banks. For example, customer due diligence requirements have been significantly enhanced in the new rulebooks. It is important to recognize, however, that implementation efforts remain a key priority given the extent of the new requirements issued under the rulebooks.

Overall, understanding and integration of CFT in both the regulations and the practices of the financial institutions is in a transitional phase. The legislative framework is not yet in place for terrorist financing, which is a contributing factor to the slow integration of CFT into the BMA regulations and policies. The BMA has made strides through the new rulebooks for both banks (conventional and Islamic), as well as an initial circular in 2002, and insurance companies will similarly benefit from the insurance rulebook which was issued in May 2005. However, the rulebooks do not provide for full coverage of FT and there is limited guidance on this issue to assist institutions. Resolution 1/2004 covering capital markets licensees does not address the financing of terrorism at all.

The BMA has introduced the concept of risk-based customer due diligence in the new rulebooks (regulations), but it is not obligatory. No risk-based framework is permitted for money changers, operating under the 2001 Regulation, nor for the capital markets licensees under Resolution 1/2004.

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

Description and analysis

R. 5

Customer due diligence is covered briefly in Decree Law 4/2001, which is applicable to all financial institutions. Different implementing regulations have been drafted for each of the financial sectors, which has created significantly different levels of compliance with Recommendation 5, as detailed below. The regulatory framework for the banks is covered in the new rulebooks (Financial Crimes Module, Section 1, known as “FC 1”), insurance companies are covered by the rulebook issued in May 2005 (FC 1), capital markets are covered by Resolution 1/2004, and money changers and brokers covered by the 2001 Regulation on AML. All entities are also covered by Ministerial Order 7/2001, which, because of its limited detail, is only useful when considering the situation with the capital markets licensees, as the Resolution also contains little detail.

Anonymous accounts are not permitted in Bahrain based on DL 4/2001, which states that financial institutions may not “open or keep any secret, fictitious, or anonymous accounts.” This is also prohibited in MO 7/2001 which applies to all financial institutions. However, there is confusion for institutions still subject to the 2001 Regulation (money changers and money brokers) and the rulebooks (banks), as these documents appear to provide more leniency and seem to allow these accounts provided the institutions know the original identity of the account holder. The BMA provided draft language during the assessment that would be used in amending the rulebooks to fully prohibit these accounts; the amendments would be part of a quarterly amendment package to go to institutions in July. Despite the regulatory confusion, there appear to be no anonymous, numbered or fictitious accounts in Bahrain, based on discussions with both financial institutions and examiners from the BMA.

The 2001 Regulation for customer due diligence covers all financial institutions that were licensees of the BMA in 2001; insurance and capital markets are covered by a different regulatory framework, discussed below. The 2001 Regulation has the following requirements:

- CDD must be performed before an account is opened;
- CDD must be carried out on occasional transactions above BD 6,000 (approximately USD 15,915);
- The FI must verify the authority of persons acting on behalf of a legal entity;
- Customer identity must be verified using two original identification documents;
- In the context of a legal entity, licensees must verify the beneficial ownership through knowledge of the principal shareholder and those who have control over the funds. This must be done before any transaction can occur;
- The FI must ensure that it has completed CDD requirements on all existing customers within a “reasonable period of time”;

The new rulebooks for banks, and, as of May 2005, insurance companies, are more expansive than the 2001 Regulation, but these requirements have not yet been implemented by the licensees because they are so new. An important addition to the rulebooks is the addition of terrorist financing alongside money laundering as a key driver in the CDD process. Other critical elements where the rulebooks provide a more expanded CDD framework include (FC 1):

- Source of funds and the nature of the account and intended relationship must be obtained;
- Introduction of a “certification” program that must be utilized when original documents (i.e., copies) are presented to the bank or insurance licensee. The example provided within the regulation is that of a customer sending in a copy of the required documentation following an initial meeting with the licensee. In this case, the documents must be certified as “originals sighted” by a lawyer, notary, accountant, government official, official of an embassy, or an official of another licensee.
- CDD documentation must be reviewed on all customers every three years and for documentation that is out-of-date (i.e., passport has expired), new documentation must be obtained;
- Expanded discussion on verification of identity of beneficial owners/ultimate beneficiary of an account or facility, whereby when a customer is acting on behalf of a third party, the bank or insurance licensee must obtain a signed statement from the beneficial owner(s) that they are the ultimate beneficiary or beneficial owner of the account;
- Ensure adequate customer details are documented for all wire transfers (irrespective of amount) made by the bank on behalf of a customer; and
- Simplified CDD is allowed in certain circumstances as follows when the customer is: a licensee of the BMA; a customer of the BSE; one-off transaction with a value less than BD 6,000 (USD 15,915); a Ministry of a GCC or FATF government; an “equivalently supervised” financial institution; a listed GCC or FATF company with equivalent disclosure standards of the BSE.

There is a call for CDD in the case where there is suspicion of ML or FT in both the insurance and bank rulebooks. However, there are discrepancies between the new rulebooks which create confusion. One example is that the rulebooks for banks require that the nature and intended relationship be established for individual and legal entity accounts. The insurance rulebook, however, only requires this information for individual accounts and not for those opened by legal entities. Another key issue is enhanced due diligence for customers identified as having a higher risk profile. Within the FC Module of the banks rulebooks, one section requires this enhanced due diligence (FC1.11.2), while another section only mentions it as advice (FC 1.10). According to the authorities, this is not yet a requirement and a change will be made to the rulebook to downgrade the requirement to complete enhanced due diligence. The BMA expects banks to be working on a risk-sensitive approach, but does not believe that it should be a regulatory requirement because few banks have the capacity to implement such systems currently. The rulebook does require that an MLRO increase their scrutiny of accounts that, in the MLRO’s opinion, constitute a higher-risk.

The rulebooks address the need to review CDD in the event that there are doubts about the veracity of previously obtained customer identification information. There is, however, no requirement to obtain source of wealth information, although source of funds is required for all accounts. Source of wealth information must only be requested when the source of funds is inconsistent with a PEP’s known circumstances. The BMA has developed a proposal to require capture of source of wealth information as part of an amendment to the rulebook, which will, as standard practice, be consulted with the industry before being adopted.

Money changers and brokers are currently covered by the 2001 Regulation. The BMA is in the process of developing a rulebook for those licensees, which will contain more detailed CDD procedures, similar to those found in the banking rulebooks.

The capital markets CDD requirements are predominantly found in Resolution 1/2004, as well as MO 7/2001. The Resolution has significant gaps on CDD requirements and cannot be considered as a comprehensive reference guide on money laundering requirements for the capital markets licensees. For example, the Resolution does not require the following information: beneficial ownership; source of funds; and purpose and intended nature of business relationship (for individuals). There are no provisions for simplified or enhanced due diligence, nor is there any requirement to verify the authority of persons acting on behalf of a legal entity. CDD is not required to be applied to the existing customer base or on an ongoing basis, and all verification procedures

can be done using copies of documentation. However, the Resolution does prohibit opening the account if the full information requested is not received.

Ministerial Order 7/2001, applicable to all financial institutions, including capital markets licensees, addresses several of the deficiencies of the Resolution. In particular, it highlights the need to identify the source of funds for clients, allows for a simplified CDD process (but does not require any enhanced CDD), and addresses occasional customers, although the threshold is high at BD 10,000 (USD 27,000). A key concern about the Order, however, is that it specifically exempts brokers from completing CDD or identifying the source of a customer's funds if that customer is purchasing a share in a collective investment venture. Overall, the two regulations, even taken together, do not meet many of the essential criteria established under FATF Recommendation 5 for capital markets licensees.

With respect to implementation, banks are at a more advanced stage when compared against the insurance and capital markets licensees. The banks are aware of the rules and regulations and have undergone inspections which have identified key weaknesses in their CDD processes. The capital markets and insurance licensees have not undergone any AML/CFT checks and the level of overall implementation by those entities must be questioned particularly given the poor state of the capital markets regulations on CDD and the newness of the insurance regulations.

R. 6

PEP requirements have been introduced through the rulebooks for both banks (FC 1.4) and insurance companies (FC 2.3). The rulebooks specify that banks must have risk management systems in place to identify PEPs, both when opening an account and on a periodic basis. Senior management approval must be granted to establish the business relationship, with ongoing monitoring of these accounts also the responsibility of senior management (i.e., the MLRO). Enhanced monitoring and CDD requirements are specified. Bahrain's definition of PEPs includes both foreign and domestic (from Undersecretary level and up) PEPs.

Information on source of funds is clearly required, but not on source of wealth. Instead, the rulebooks indicate that a bank or insurance firm, respectively, need to capture source of wealth information only "if the amount of the funds seems inconsistent with the PEP's known financial circumstances" (FC 1.4.2(b) for banks and FC 2.3.3 (b) for insurance licensees). There are two concerns with this phrase. First, on a practical level it is difficult to determine someone's known financial circumstances without knowing their source of wealth. With respect to Recommendation 6, however, the additional concern is that this clearly gives financial institutions an opportunity to avoid requesting the source of wealth information. The BMA has developed a proposal to require capture of source of wealth information as part of an amendment to the rulebook, which will, as standard practice, be consulted with the industry before being adopted.

Because the PEP requirements are being introduced through the new rulebooks, it is important to note that money changers, money brokers, and other non-bank licensees are not subject to any PEP requirements at this time. Capital markets licensees are subject to no provisions regarding PEPs under Resolution 1/2004 and, as there are currently no plans to issue a rulebook on AML/CFT for capital markets licensees, this is a significant deficiency. As noted above, insurance companies (including Takaful/Retakaful) became subject to appropriate requirements when the insurance rulebook was put into effect in May 2005.

Implementation is underway within the banking sector, but discussions with a few banks indicated differing states of implementation and understanding. Some internationally-active banks noted that they have had to apply enhanced procedures to identifying, verifying, and monitoring PEPs prior to the enactment of the rulebooks because of requirements in other jurisdictions. However, in other cases, the assessment team was informed that implementation will begin now that the regulations are in force.

There is no mention of PEPs in the existing legislation. However, given that that legislation is in the process of being amended, consideration might be given to adding a section on PEPs in the new law.

The UN Convention against Corruption was signed by the Kingdom of Bahrain on February 8, 2005. Ratification is in process.

R. 7

Prior to the issuance of the rulebooks, BMA licensees were subject to the 2001 Regulation, which required them to gather sufficient information about their respondent institutions, to document the respective AML/CFT responsibilities of each institution, and to undertake due diligence where a payable through situation exists (Section 5.1). The Regulation, however, does not require approval by senior management to establish a new account, nor does the Regulation require an assessment of the respondent's AML/CFT controls.

The new rulebooks for banks expand the requirements on correspondent banking accounts in two principal ways. The rulebook creates the requirement that prior to opening a correspondent banking relationship, the bank must "ensure that the correspondent banking relationship has the approval of senior management" (FC 2.2.2(b)), which addresses one of the weaknesses noted above regarding the 2001 Regulation. The second concern, requiring an assessment of the AML controls, is also addressed through FC 2.2.2(d). However, TF is not addressed in the controls language and this is an important absence. The BMA has, however, significantly expanded the list of factors that banks must consider to open a correspondent banking relationship to include (FC 2.2.1 and FC 2.2.2):

- Information about the respondent's bank ownership structure;
- Where the customers of the respondent bank are located;
- The purpose for which the account will be opened;
- Confirmation that the respondent bank is able to provide relevant customer identification data on request to the correspondent bank;
- Verification that the bank has not been subject to a AML/CFT investigation; and
- Requirement of a signed statement outlining the respective responsibilities of each institution in relation to money laundering detection and monitoring responsibilities. However, as with the controls issues identified above, there is no requirement to document CFT responsibilities.

With respect to the capital markets licensees, all settlement activity takes place directly through one bank in Bahrain, which is Bank of Bahrain and Kuwait.

Payable through accounts are addressed in both the 2001 Regulation, as well as the new rulebooks for banks. In the new rulebook, the bank must get "confirmation that the respondent bank has verified the identity of any third party entities that will have direct access to the correspondent banking services without reference to the respondent bank" (FC 2.2.1(f)). In practice, the BMA noted that payable through accounts are extremely rare.

R. 8

There is no specific regulatory requirement to set in place appropriate measures to deter ML/FT threats from new technologies. However, there are non-face-to-face CDD requirements for financial institutions as follows:

- For banks, the new rulebooks require that banks "establish specific procedures for verifying customer identity where no face-to-face contact takes place" (FC 1.3.1). Ongoing due diligence is required for all accounts, including non-face-to-face.
- For insurance companies, there are no specific requirements addressing non-face-to-face account opening in the new rulebook. This is because non-face-to-face account opening does not currently occur. However, the authorities noted that it is not prohibited to open accounts in this manner, so they plan to issue requirements as part of the insurance rulebook, with the requirements based on those found in the bank rulebooks.
- There are currently no requirements on non-face-to-face account opening for capital markets licensees.
- For money changers and money brokers, which follow the requirements of the 2001 Regulation, there is the following statement regarding specific CDD procedures: "Identification procedures where there is no face-to-face contact must serve two purposes: they must ensure that the applicant is indeed that person, and a person bearing the name of the applicant exists and lives at the address provided" (Section 4.6). While the intent of this statement appears to be that the licensees have a policy for identification of non-face-to-face, it does not appear to be a firm requirement.

Recommendations and comments		
<ul style="list-style-type: none"> • Banks and insurance companies must implement the regulatory requirements introduced in the new rulebooks. • The BMA must verify implementation efforts related to the new rulebooks through continued (in the case of banks) and new (insurance) on-site inspection programs. • PEP requirements should be included in regulations for capital markets licensees, as well as money changers and money brokers. • Regulations for capital markets must be enhanced to meet the CDD requirements of the FATF Recommendations , as well as meeting the same comprehensiveness standards as applied to other financial sector licensees by the BMA. • Language should be added in the regulations to ensure that financial institutions pay attention to ML/FT risks arising from new technologies. • CDD requirements for non-face-to-face account opening should be established for capital markets licensees, unless this type of account opening is specifically prohibited. • FC 2 should be reviewed and updated to address TF concerns, particularly paragraphs 2.2.1(d), 2.2.1(g), 2.2.2(a), and 2.2.3. 		
Compliance with FATF Recommendations		
R.5	Partially compliant	CDD regulations must be enhanced for capital markets licensees and implementation efforts must be in place, particularly for insurance and capital markets licensees.
R.6	Partially compliant	Requirements for PEPs must be in place for all financial institutions; currently only banks, and as of end-April, insurance companies, are covered. There are no requirements for capital markets licensees to check for PEPs.
R.7	Largely compliant	Requirements to assess CFT controls should be put in place.
R.8	Partially compliant	Measures to deter ML/FT threats arising from new technologies must be put in place and regulations for insurance and capital markets licensees on non-face-to-face account opening must be developed.
Third parties and introduced business (R.9)		
Description and analysis		
<p>The BMA addresses third parties and introduced business in two ways, depending on whether the funds are in an account that co-mingles clients versus individual accounts in the name of the third party or introducer. For those that are not co-mingled (sub-accounts), both the 2001 Regulation and the rulebooks indicate that the beneficial owners must be identified under the CDD requirements. In these cases, the CDD requirements may not be fulfilled other than by the licensee itself.</p> <p>For accounts that are co-mingled, the regulations allow third parties and introducers to perform certain elements of the CDD process as follows:</p> <ul style="list-style-type: none"> • 2001 Regulation: The Regulation indicates that when “the intermediary is subject to the same regulatory and money laundering regulation and procedures (and, in particular, is subject to the same due diligence standards in respect of its client base) the [BMA] will not insist upon all beneficial owners being identified <u>Provided</u> the relevant licensee is able to establish that the intermediary has engaged in a sound due diligence process” (Section 4.10 (b)). The Regulation also indicates that if an intermediary is not “empowered” to share information on beneficial owners or is not subject to the same standards, no reliance is allowed unless approved by the BMA. The Regulation does not address the need to obtain information from the intermediary, nor to ensure that the third party is adequately regulated and supervised. There is also no discussion on FATF compliance in the Regulation as a factor to consider. The 2001 Regulation covers money changers and money brokers. • Rulebooks for banking: Much more detail is provided on the reliance on third parties or introducers than in the 2001 Regulation. There are two key sections that cover the requirements for introduced business or third parties; these are FC 2.1 and FC 2.3. These sections require that information be made available from the third party upon request. Introducers are required to provide “all relevant data pertaining to the customer’s 		

<p>identity, the identity of the beneficial owner and the purpose of the relationship” (FC 2.3.1(c)). In FC 2.3.1, the BMA indicates that “Banks may accept clients introduced to them by other financial institutions or intermediaries that the banks have satisfied themselves are subject to the equivalent CDD measures as themselves. Where a bank delegates part of the customer due diligence measures to another financial institution or intermediary, the responsibility remains with the bank relying on the third party.” The requirement to consider FATF compliance is covered in FC 2.1.4.</p> <ul style="list-style-type: none"> • Rulebook for insurance: Same requirements as the rulebook for banks, but in the insurance rulebook, the key section is FC 2.5. • Resolution 1/2004 and MO 7/2001, both of which cover capital markets licensees: The Resolution does not address reliance on introducers or third parties. The MO does allow for introducers, as follows: “If the customer is an agent of a business or firm subject to the supervision of a controlling authority and resides in a country that has similar laws for prohibition and combating of money laundering, it may be sufficient evidence to receive written confirmation from the customer of the availability of proof of the principal’s identity, its registration and maintenance thereof” (Section 6). In Section 7(c), there is a more confusing explanation of when introducers may be relied upon as follows: “Procedures for proving a customer’s identity and sources of funds indicated in this Order shall not be applicable in the following cases... if a separate significant transaction takes place with or for the account of a third party with the intervention of a person who is subject to a supervisory authority who has provided confirmation that the identity of the third party has been established and registered according to the custody procedures for such person.” The meaning of the two passages in the MO requires clarification in order to understand the exact circumstances under which an introducer may be relied upon for capital markets licensees. <p>Practically, there appears to be little reliance on third parties or introducers. The BMA expressed little comfort with the concept and this was echoed by the financial institutions. It was interesting to note, for example, that BMA staff stated that the capital markets licensees would not currently be considered “equivalently supervised” for the purposes of this section. As a result, banks and other financial institutions would not be permitted to rely on the CDD completed by a capital markets licensee.</p>		
Recommendations and comments		
<ul style="list-style-type: none"> • Clarification is required as to the exact circumstances under which a capital markets licensee, such as a broker, could rely on an introducer. • The regulations should specify that consideration will be given to the country where the introducer is based and whether that country abides by the FATF recommendations. 		
Compliance with FATF Recommendations		
R.9	Partially compliant	Capital markets licensees, money changers, and money brokers must be brought under the requirements now in place in the rulebooks for banks and insurance companies.
Financial institution secrecy or confidentiality (R.4)		
Description and analysis		
Article 7 of DL 4/2001 covers secrecy of records and over-rides all other confidentiality requirements. Many financial institutions including insurance companies and capital markets licensees have not been subject to onsite supervision yet and so this practice has yet to be confirmed.		
Recommendations and comments		
<ul style="list-style-type: none"> • Conduct on-site inspections of insurance and capital markets licensees to confirm that there is no bank secrecy in place in practice with regard to accessing information from financial institutions pursuant to their responsibility under the requirements of DL 4/2001. 		
Compliance with FATF Recommendations		
R.4	Largely compliant	No on-site inspections have been completed for insurance or capital markets licensees.
Record keeping and wire transfer rules (R.10 & SR.VII)		
Description and analysis		

R. 10

Decree Law 4/2001 requires that institutions keep copies of records regarding the identity of clients for five years after the relationship has ended. Similarly, transaction records must be kept for five years after the transaction has been completed.

The 2001 Regulation, which remains pertinent to money changers and money brokers covers record keeping in Section 11. Evidence of identity and business relationship records (including account opening forms, investment agreements, account files, etc) must be kept for five years from the end of the relationship with the licensee. Transaction records on account holders and non-account holders must also be kept for five years from the date the transaction was completed. All records must be available for prompt access by the BMA (Section 11.3).

The same requirements of the 2001 Regulation are found in the rulebooks for banks and insurance, with one exception. The rulebook contains two standards—required elements of the regulation are in bold text, while suggested elements are in normal text. In the banking rulebooks, the discussion on ensuring that records are available for prompt and swift access are in normal text, indicating that this is not a requirement, just good practice. According to BMA officials this is an error and they provided a copy of an earlier consultative version of the text that was in bold. The BMA committed to correcting this error in the July update to the rulebooks.

Capital markets recordkeeping requirements are found in Article 16 of Resolution 1/2004. The Article indicates that records should be kept for five years and that they must be stored in an “easily retrievable manner.”

None of the regulations specifically require that the records be sufficient to permit reconstruction of individual transactions, although the breadth and depth of records that must be kept under the BMA regulations would indicate that such transactions could be recreated if necessary.

SR VII

On January 27, 2002, the BMA issued a circular (BC/1/2002) to all licensees entitled “FATF Special Recommendations on Terrorism Financing.” This circular, which the authorities consider to have the effect of a regulation, covers all the elements of SR VII. In particular, the circular requires that all licensees must include the details of originator information with all electronic transfers that they make for their clients. No distinction is made between domestic and cross-border wire transfers. Originator information means the name of the payer, the address of the payer, and the account number of the payer. This information must be provided on all transfers, irrespective of amount.

For transfers coming into a financial institution in Bahrain, the requirements are as follows (Section 1(b)):

- All licensees must maintain records of all originator information received with an inward transfer; and
- Any transfer that comes in without originator information must be carefully scrutinized; these transfers should be presumed to be suspicious unless the sending institution can immediately inform the licensee in writing of the originator information.

While the requirements are the same under the new rulebooks, there are two differences. Corresponding to guidance from FATF, the BMA no longer requires that address information be captured, as each person has a unique identifying number (based on a residency-type card, known as the CPR). The second difference is that the rulebooks prohibit batching of non-routine transfers “if batching increases the risks of money laundering or terrorist financing” (FC 3.1.1). As the rulebooks have just gone into effect, the batching requirement is still in process of implementation.

Sanctions are provided for in the event of a breach of the regulations. For the FATF circular of 2002 (to the extent that it can be considered to have the status of a regulation), the BMA has sanction authority under Article 84 of the BMA Law of 1973. In addition to the provisions of the 1973 Law, financial institutions operating under the rulebooks are covered by additional penalties under Section FC 9.1.1.

Recommendations and comments

- Implementation of the recordkeeping requirement should be verified for capital markets and insurance licensees through on-site inspection.

Compliance with FATF Recommendations

R.10	Largely compliant	Although the regulation is in place, capital markets licensees and insurance licensees have not been subject to inspection to determine implementation.
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SR.VII	Compliant	
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Monitoring of transactions and relationships (R.11 & 21)

Description and analysis

R. 11

Money changers and money broker licensees are currently subject to the 2001 Regulation which contains very little detail on paying special attention to large, complex or unusual transactions. The Regulation does not currently cover any of the essential criteria for Recommendation 11, with the exception of transactions coming from countries that do not adequately apply the FATF recommendations, as described under Recommendation 21. The BMA believes that the new rulebook for money changers and money brokers, expected to be released later in 2005, will address these issues. Capital markets licensees are subject to both Resolution 1/ 2004 and MO 7/2001. Article 12(2)(e) of Resolution 1/2004 requires that capital markets licensees report any “suspicious and extraordinary” transactions. Extraordinary is defined by size, recurrence, nature, the surrounding circumstances, or when a transaction does not have clear economic or legal objectives. There is no requirement, however, that the background and purpose of these transactions be reviewed with the findings set in writing.

For banks, the new rulebooks covers some of the criteria under FC 1.13, which includes:

- Banks must develop risk-based transaction monitoring systems, but should a bank not have this system, all transactions above BD 6,000 (USD 15,915) will be captured in a daily report for monitoring by the money laundering reporting officer;
- The risk-based monitoring systems should recognize significant or abnormal transactions or patterns of activity, as well as those transactions that do not have a clear purpose or make no economic sense, and those that are unusual or significant;
- When one of these transactions is identified, the rulebook indicates that the bank should “verify the source of wealth or income for these transactions, particularly where the transactions are above the occasional transactions threshold of BD 6,000.”

While banks are required to keep all the transaction records related to these transactions for five years (FC 1.13.1), there is no specific requirement for the financial institution to examine the background of the transaction, its purpose, and to set all of this in writing. This does appear to be the current practice, however, based on discussions with banks.

The requirements in the insurance rulebook are very similar to those found in the bank rulebooks. In particular, there is the expectation that insurance firms and brokers be alert to financial flows and transaction patterns among policyholders. There is specific emphasis in those instances where there is a “significant, unexpected and unexplained change in the behavior of policyholders’ account (e.g., early surrenders),” Section FC 2.2.25. As with banks, however, there is no requirement to examine those transactions and set the findings of any review in writing.

R. 21

The 2001 Regulation (Section 12.1) and the insurance rulebook (FC 2.2.26) have the same paragraph that covers, in part, the requirements of Recommendation 21. The paragraph indicates that special attention must be given to relationships and transactions with persons (including companies and financial institutions) from countries that have been identified by the FATF as non-cooperative in the fight against ML/FT. The Regulation also requires that transactions from non-cooperative countries, when they appear to have no economic or lawful purpose, must be reviewed, with findings established in writing. These transactions must also be reported. The Regulation does not address countries other than those that are identified by FATF and there are no measures in place to advise

licensees on weaknesses in AML/CFT systems of other countries. Regulation does not address the possibility of counter-measures.

The bank rulebooks provide more detailed requirements for banks. First, instead of just relying on the FATF list of non-cooperative countries, the rulebooks indicate that the BMA will identify the list of non-cooperative countries. In practice, however, the BMA was clear that they currently rely on the FATF listing. The BMA has also provided for a system to advise banks when there are serious deficiencies in a country’s AML/CFT regime; this is covered in FC 8.1.3. As with the 2001 Regulation and the insurance rulebook, transactions which have no apparent economic or visible lawful purpose must be reviewed closely, with the findings established in writing; this would include examining unusual transactions coming from other countries. While there is no specific mention of counter-measures in the rulebook, as with the abovementioned documents, there is an expectation that banks will pay special attention to any transactions with these countries and will report any concerns to the BMA and the AMLU.

Capital markets licensees are required by Article 8 of Resolution 1/2004 to “take the necessary precautions and exercise due care when dealing with investors from countries not maintaining a co-operation arrangement with the Kingdom, or which do not have integrated laws or procedures in place for the prevention or prohibition of money laundering.” There are no specified measures in place to advise licensees on weaknesses in other countries AML/CFT systems, no counter-measures, and no requirement to examine unusual transactions coming from other countries with findings set in writing.

Recommendations and comments

- Requirements should be established for money changers, and money brokers to ensure that due attention is given to unusual, large or complex transactions.
- Capital markets, money changers, and money broker licensees should also be required to ensure that the background of large, complex or unusual transactions, including those coming from other countries are reviewed and that the findings of those reviews are put in writing and, for money changers and money brokers, maintained in the financial institution’s records for five years.
- Counter-measures should be established for those situations involving transactions with jurisdictions that do not adequately apply the FATF Recommendations.
- Capital markets licensees should be subject to stronger requirements when dealing with clients or transactions from jurisdictions that do not sufficiently apply the FATF recommendations. The BMA must also develop a mechanism to inform the capital markets licensees of the jurisdictions where greater caution should be considered.

Compliance with FATF Recommendations

R.11	Partially compliant	Requirements must be established for money changers and money brokers. All financial institutions should be expected to examine the specified transactions and put their findings in writing.
R.21	Partially compliant	More detail must be specified for capital markets licensees. On-site inspections must be performed for capital markets and insurance licensees. Counter-measures must be established in the regulation.

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

Description and analysis

R. 13

The reporting system is suspicious transaction based (Article 5 (c) of DL 4/2001), regardless of the amount involved. DL 4/2001 requires entities to report “any transactions suspected by the relevant officer by reason of the identity of the persons involved, the nature of the transaction or any other circumstances”. Several definitions are given of suspicious and suspicious transaction in Ministerial Orders, such as in Article 1 of MO 7/2001(Ministry of Finance), in Article 3 of MO 23/2002 (Ministry of Industry and Commerce), and in Article 1 of MO 1/2004 (BMA). There is also the definition given in item 7.4 and 7.5 in the BMA’s 2001 Regulation and in the banks and insurance rulebooks. Capital markets licensees must report any transaction that appears “suspicious or extraordinary.”

The reporting obligation relates to any suspicious transaction irrespective of the possible predicate criminality or of the possibility that it might involve tax related matters, or foreign offenses given the all crimes approach in Bahrain. It is not incumbent on the reporting entities to (try to) identify the nature of the suspected illegal activity when submitting a disclosure.

As the majority of the countries that have introduced a reporting regime, Bahrain has deliberately not opted for a threshold based currency transaction disclosure system. The DL 4/2001 is in the process of being amended however to establish a declaration/disclosure system at the border in compliance with SR IX.

The reporting system based on DL 4/2001 does not (yet) include CFT, although the BMA circular on the FATF Special Recommendations, issued in 2002 does address the need for reporting on CFT. The authorities believe the circular has the status of a regulation and can be enforced. The subsequent bank and insurance rulebooks instruct all licensees to report all funds suspected to be terrorist related to the AMLU and BMA. *De facto* the FIU has already received 9 such disclosures from the banks in the form of STRs.

Neither DL 4/2001, nor the MO's refer to any obligation to disclose attempted transactions, although it was argued that Article 5 (c) of DL 4/2001 refers to "operations" rather than "transactions", thus encompassing attempted transactions. Whatever the correct translation, no doubt should be left as to the fact that there is an unequivocal obligation to report attempted transactions, which are normally highly relevant in terms of suspicious activity. Financial institutions do have an obligation to report attempted transactions, as described below.

As for the timing of the reports, Article 5(e)(i) of MO 18/2002 and Article 7 of MO 23/2002, obliges the reporting entities to forward their disclosures to the FIU "immediately" and "within 24 hours" after drafting the STR and consulting with the supervisor. The 2001 Regulation (Section 7.2), which covers money changes and money brokers, indicates that if the MLRO "suspects that a person has been engaged in money laundering, he must report the fact promptly" to the BMA and AMLU. Other regulations and the rulebooks do not specify, but always refer to past transactions. The term "immediately" is open to interpretation and gives a certain unwanted margin to the reporting entities that is enhanced by the condition of at least "within 24 hours". Any reporting system should be geared to efficiently intercept and recover criminal proceeds. The power given to the AMLU by Article 6.2 of DL 4/2001 to seize the suspected assets immediately only makes sense when the reporting is done in a timely fashion, *i.e.* before executing the transaction. This is of course not always possible because of the instantaneous character of certain transactions (such as money exchange) or because the suspicion is raised *a posteriori*, but it should be made a clear and unequivocal rule that any STR must, whenever possible, be reported to the FIU before the execution of the transaction.

Some confusion about reporting standards has been introduced into the BMA regulations. For example, in Sections 7.4 and 7.5 of the 2001 Regulation, there seems to be an effort to link the reporting requirement to a list of "suspicious transactions" identified by the BMA in the appendix of the regulation. This is carried over from the 2001 Regulation into the rulebooks in paragraphs FC 5.2.4 and FC 5.2.5. Paragraph FC 5.2.4 indicates that a report must be filed by the MLRO "where he knows or has suspicions that a transaction or a customer's conduct might involve money laundering or the financing of terrorism, *either due to the customer's economic standing or because it meets one of the examples of suspicious transactions described in Appendix FC 3*" (emphasis added). However, FC 5.2.5 states that "The examples of suspicious transactions listed in Appendix FC 3 are given for guidance purposes only. For the avoidance of doubt, banks must report all suspicious transactions or attempted transactions, irrespective of amount, even if they do not conform with any of the examples listed in the Appendix." The BMA committed to removing the phrase in italics above to ensure that there is no confusion about the point that all suspicious transactions must be reported.

There are several key additional points raised by the 2001 Regulation. The Regulation makes no mention of any thresholds for reporting and all transactions, regardless of size, that meet the regulatory requirements must be reported. Attempted transactions are not addressed in the 2001 Regulation.

The rulebooks for banks and insurance licensees address reporting for both ML and FT. MLROs must send STR reports to the BMA and AMLU where the MLRO "knows or has suspicions that a transaction or a customer's conduct might involve money laundering or the financing of terrorism" (FC 5.2.4). There are two important

differences between the bank and insurance rulebooks. Reporting is done regardless of whether the matter involves tax, however this is addressed only in the bank rulebooks and not in the insurance rulebook. Attempted transactions are also only addressed in bank rulebooks and not the insurance rulebook.

There are significant concerns with the regulatory status of reporting STRs for capital markets licensees. First, these licensees are not required to report any STRs related to the financing of terrorism. A more critical concern, however, is the lack of clarity about where the licensees are supposed to report. The BMA published Resolution 1/2004 in both English and Arabic. In the Arabic version, STRs are reported to both the BMA and the AMLU. In the English version, however, STRs are only reported to the BMA in one section (Article 13), while another section says that they should be reported to both the BMA and the AMLU (Article 12(2)). This is further reinforced by the Memorandum of Understanding between the BMA and the BSE, signed in March 2005, which indicates that “the BSE shall report any suspicious transactions to the BMA’s Compliance Unit, giving all available details” (Article 6.16). In practice, the assessment team determined that some of the licensees are not aware of the AMLU or that there is a need to report to them and no STRs have been filed to date.

Overall in the Bahrain financial services sector, there is limited experience in filing STRs, with banks filing only 120 STRs in 2004 and 87 thus far in 2005. Along with capital markets licensees, insurance licensees have also not filed any STRs. More detailed statistical data highlights the performance of the reporting system and the FIU since its inception on June 12, 2001 (status on April 17, 2005):

STR Reporting Overview

Total Received	Under Investigation	Filed	To Public Prosecutor
330	147	136	24 (4 on ML)

STR Reporting Sources

Banks	Money Exchangers	Credit Card Co’s.	Others*
258	60	5	9

*Other reporters were those who are not subject to DL 4/2001 and included: CID, foreign police agency, foreign Central Bank, individuals, supervisory, and a foreign embassy.

STR Reporting: Details on the nature of the transaction

Cash	Wire Transfers (Domestic and Cross-border)	Terrorist-Related
157	164	9

Other Statistics:

Accounts frozen:

Suspected ML resulting from STRs: 16 (currently US\$3,121,180)
UN Resolution terrorist list : 5 (currently US\$10,334,614)

International cooperation:

Requests from FIUs: 38 (all complied with)
Requests to FIUs : 17 (3 still outstanding)

Analysis:

After a slow start, the number of STRs rose steadily, to increase sharply in 2004 for the banks (from 72 to 113)

and in 2005 for the money exchange offices (from 2 to 58 on 17/4/2005). This was explained by the awareness raising exercise by the BMA. Even if, in the absence of objective criteria, it is very difficult to rate the performance of the reporting system in terms of the quantity of reports, it is fair to say that the figures are on the low side. The underreporting is made abundantly clear by the sudden jump in number of STRs after an inspection round by the BMA. This confirms the *adagium* that low supervision may equal low compliance. A very noticeable fact is that no STRs have been received yet from the non-financial sector (DNFBPs), nor from the capital market or insurance licensees, none of whom have been inspected.

Some 45% of the STRs received are still under investigation. This is a relatively high percentage, but altogether understandable under the circumstances. It is not indicative of a lack of commitment or resources of the FIU, but seems mainly caused by the degree of difficulty of financial crime investigations and the dependence on outside sources and assistance that the FIU does not control (such as international cooperation). Furthermore the search for the predicate criminality is also a very exacting and time-consuming one.

The output to the Public Prosecutor, 24 STRS or 7%, is also on the low side. Those 24 STRs represent 4 ML cases and 14 cases related to other crimes. This figure can still increase with the results of the ongoing investigations. It is, however, encouraging that the system does start to produce results in terms of prosecutions, and it remains now to be seen if the courts will be satisfied with the evidence presented to them.

R. 14

There is an immunity clause for complying with DL 4/2001 obligations and specifically for reporting to the AMLU or the Public Prosecutor (Article 10.3 of DL 4/2001 & Article 7 of MO 7/2001). The provisions cover institutions and employees of institutions who are complying with the law in providing the report. This does not, however, cover reporting done in bad faith and carries the condition of acting in good faith. The tipping-off prohibition is sufficiently covered by Article 3.4 of DL 4/2001 and Article 8.2 of MO 7/2001 (see below Sanctions).

R. 19

There are no systems in place to report domestic or international currency transactions. This issue is under study, but no decisions have been reached. With respect to STRs, however, Customs cooperates routinely with its counterparts and other law enforcement agencies in exchanging information on suspect transports.

R. 25

The FIU gives feedback to the reporting institutions in different ways. It manages its own website where, beside general information on its activities, it publishes its annual statistics and provides information on typologies and actual (sanitized) cases. The AMLU does give feedback to the MLROs of the reporting entities regarding results of any investigations, without, however, offering specific details. However, on a practical level, none of the reporting entities that the assessment team spoke with that had filed an STR had received any feedback from the AMLU.

SR IV

Under the 2001 Regulation, which is currently applicable to money changers and money brokers, reporting for funds linked to terrorism is not addressed. It is also not addressed by Resolution 1/ 2004 for capital markets licensees. The rulebooks for banks and insurance licensees do address reporting when the MLRO “knows or has suspicions that a transaction or a customer’s conduct might involve money laundering or the financing of terrorism” (FC 5.2.4). However, there are other differences between the insurance and banks rulebooks that will impact the reporting, including that related to terrorist financing. Reporting is done regardless of whether the matter involves tax, however this is addressed only in the bank rulebooks and not in the insurance rulebook. Attempted transactions are also only addressed in bank rulebooks and not the insurance rulebook.

Recommendations and comments

- STR reporting should be clarified for capital markets licensees in two important ways: it should be made clear that all reports go to both the AMLU and the BMA; and reporting should be for both ML and FT suspicions.
- The requirements for money changers and money brokers should be brought up-to-date to make clear when a report must be filed (i.e., not based on a list of examples provided by the BMA).
- The BMA should assess the level of awareness and understanding of STR requirements within the capital markets and insurance licensees, given that these two groups have never filed an STR.
- The AMLU should also work to raise awareness within the capital markets and insurance licensees regarding STR reporting, and consider applying sanctions for willful non-compliance.
- The rate of forwarded cases to the Public Prosecutor should increase, irrespective of the predicate criminality being identified or not, if only to create the jurisprudence necessary to give direction to the investigations and clarify the evidentiary requirements.
- The introduction of a formal predicate or autonomous FT offence is required to create the necessary legal context for related STRs.
- The definition of suspicious transaction must be made a uniform one.
- The immunity clause for reporting to the appropriate authorities should carry the condition of good faith.
- There must be a formal and express obligation to report attempted transactions for financial institutions (excluding banks, which are already covered).
- STRs should, whenever reasonably possible, be submitted to the FIU before the transaction is executed, to enable immediate law enforcement intervention.

Compliance with FATF Recommendations		
R.13	Partially compliant	Implementation efforts must be strengthened, greater awareness of the need to report is necessary for the capital markets and insurance licensees.
R.14	Largely compliant	The immunity provision does not require good faith.
R.19	Compliant	
R.25	Largely compliant	The AMLU should contribute actively to the awareness raising of the entities that are deficient in complying with their reporting duties.
SR.IV	Partially compliant	No obligation to report FT related STRs for capital markets, money changers, and money broker licensees.

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

Description and analysis

R. 15

For each of the key elements of the ML/FT program, it is important to note the status of the 2001 Regulation, which applies to money changers and money brokers, Resolution 1/2004 and MO 7/2001, which apply to capital markets licensees and the new rulebooks for banks and insurance licensees, recognizing that the insurance rulebook is still new, having been issued in May 2005. The 2001 Regulation and the regulations for the capital markets licensees *contain no provisions related to terrorism*, so all discussion below on those documents is in regards to money laundering.

Policies, procedures and controls:

The 2001 Regulation (Section 12.2) requires that licensees develop policies, procedures and controls to ensure proper implementation of the requirements of the Regulation. Resolution 1/2004 also requires that controls, procedures and guidelines be established. This same requirement is echoed within the rulebooks, but with the added obligations to ensure that they are approved by the directors of the bank, then forwarded to the BMA for its records. The policies, procedures, and controls are communicated to staff through on-going training programs.

Money Laundering Reporting Officer—Appointment and Responsibilities:

The 2001 Regulation and the rulebooks require that financial institutions appoint an MLRO who must be approved by the BMA prior to appointment. Both the Regulation and the rulebooks require that the individual have sufficient seniority to act independently of management. The MLRO must be based in Bahrain and have unfettered access to all transactional and other information within the bank to meet its job requirements. A key

part of the job is ongoing monitoring of accounts that “in his opinion” constitute high-risk customer accounts. The MLRO also files the STRs with the BMA and the AMLU and responds to any requests from either of these agencies.

Resolution 1/2004 for capital markets licensees does establish a position that is similar to that of the MLRO, as described in the previous paragraph, but it is not referred to as a MLRO. According to the Resolution, the individual selected to take on this function must be approved by the BMA and must have “sound acquaintance” with AML laws and regulations. The individual is required to report suspicious transactions, ensure the adequacy of controls and procedures in place, and verify that staff have received appropriate training. There is no requirement to monitor any transactions.

Audit, training, and hiring:

External audits are required to check for compliance with money laundering regulations, and in the case of the rulebooks, terrorist financing requirements as well. The 2001 Regulation establishes an annual audit requirement for all issues related to combating money laundering. In the Regulation, the MLRO is expected to commission outside auditors. Similarly, the rulebooks indicate that “a bank (with its external auditors) must review the effectiveness of its AML/CFT controls and procedures at least once every calendar year” (FC 4.3.2). Under the rulebooks, that annual audit may rely upon work completed by the internal auditor during the year. The overall evaluation, which includes foreign branches and subsidiaries, must be provided to the BMA. The first of these external audits is due to the BMA on April 30, 2006. While banks and insurance licensees have been given a year to transition to the new and expanded reporting format, they must still provide the annual reports as specified under the 2001 Regulation during 2005.

Internal audits are not currently a requirement for conventional banks, but are a requirement for Islamic banks. The lack of requirement for conventional banks is due to the ongoing consultative process for one element of new the rulebook, covering corporate governance issues. This does include a requirement for an internal audit program, so once the Corporate Governance Module is completed, the requirement will be in place. The practice appears clearly to be that there are internal audit programs in the banks.

There are no provisions for audit under Ministerial Order 7/2001, but there are provisions for capital markets licensees under Resolution 1/2004. The BSE is required to complete “direct and regular” audits on the trading, settlement, clearing and central depository system, and the shareholders register regarding AML/CFT. In addition, audits must be completed by the licensees. However, no timeframe for completion or frequency of these audits is specified.

Training requirements for AML issues are comprehensive and addressed in the 2001 Regulation, the rulebooks, and Resolution 1/2004. However, there is no requirement in any of the regulations to ensure training on FT. Based on conversations with industry participants, the requirement of FT training should be requisite in the regulations. For ML, staff who “have contact with customers or handle, or who are managerially responsible for the handling of, client transactions or client relationships” must receive ongoing training that covers a range of topics including the financial institution’s AML controls and procedures, typologies, and procedures for STR reporting.

Since the 2001 Regulation, banks, money changers and money brokers have been required to ensure that controls are in place so that criminals or their associates are not employed by the licensees. Insurance companies will introduce the requirement when the rulebook becomes effective. Screening procedures to ensure high standards when hiring employees are required in the 2001 Regulation (Section 12.2) and the rulebooks (FC 6.1.4 for banks and FC 4.1.7 for insurance licensees). The requirement for capital markets licensees is not a definitive as that for the other financial licensees in that the Internal Regulation for capital markets licensees requires that the brokers “be of good reputation” (Article 16 Second (4)(a)), but criminals may not be employed by the brokers.

R. 22

The 2001 Regulation, the rulebooks for bank and insurance licensees, and MO 7/2001 for capital markets licensees require the application of the requirements to branches and subsidiaries of locally incorporated banks

<p>operating in foreign jurisdictions. In these documents, there is a specific notation that the higher standard, whether it be Bahrain’s or the foreign jurisdiction will prevail. The rulebooks additionally note that if “a bank cannot implement these rules and regulations in a foreign branch or foreign subsidiary, it must contact the [BMA] immediately in order that a joint review of acceptable measures may be carried out.” There are currently no provisions to give extra attention to branches and subsidiaries in countries that insufficiently apply the FATF Recommendations for capital markets licensees; it is a requirement under the banks and insurance rulebooks.</p> <p>Discussions with industry participants revealed a lack of understanding of these provisions. There was some confusion, with some financial institutions believing that local standards overseas would, in fact, prevail over those established by the BMA. While this may be the case in some circumstances, these instances must be well understood by the institution to ensure that the risks are being appropriately managed in those branches or subsidiaries.</p> <p>The regulations do not address application of these standards to the wider group (e.g. to the parent entities of the Bahrain licensee and its subsidiaries and branches).</p>		
<p>Recommendations and comments</p>		
<ul style="list-style-type: none"> • The MLRO for capital markets licensees should be required to monitor transactions, unless that responsibility is specifically assigned to another individual. • The BMA should ensure that audit, training, and internal controls for capital markets licensees, money changers and money brokers encompass FT, as well as ML. • Capital markets licensees should be required to give extra attention to branches and subsidiaries in countries that do not sufficiently apply the FATF Recommendations. • Capital markets licensees with foreign branches or subsidiaries should be required to inform the BMA when local requirements abroad prohibit them from implementing the BMA regulatory requirements. • Implementation of this requirement for insurance companies should be verified through on-site inspection.. 		
<p>Compliance with FATF Recommendations</p>		
R.15	Partially compliant	Requirements for FT training and subsequent implementation for all financial institutions are necessary. High hiring standards must be a requirement of the capital markets licensees.
R.22	Largely compliant	Weaknesses of capital markets framework. No implementation verification completed for insurance licensees.
<p>Shell banks (R.18)</p>		
<p>Description and analysis</p>		
<p>Shell banks are not licensed in Bahrain. While there is an offshore banking license (OBUs), the licensing criteria still require that mind and management of these entities reside in Bahrain, along with all records, which must be available for inspection by the BMA. In addition, senior management of the OBU’s must be approved by the BMA as part of its authorization. These elements are covered in the Licensing and Authorization Requirements module and the High Level Controls Module.</p> <p>Licensees of the BMA are not permitted to deal with shell banks from other jurisdictions. In fact, FC 1.8.2 requires that licensees file an STR with the BMA and the AMLU if they are “approached by a shell bank or an institution they suspect of being a shell bank.”</p> <p>With respect to correspondent banking, the 2001 Regulation states that “banks should refuse to enter into or continue a correspondent banking relationship with a bank incorporated in a jurisdiction in which it has no physical presence and which is unaffiliated with a regulated financial group” (Section 5.1(b)). This same prohibition is found in the bank rulebooks (FC 1.8.1). Banks are also not permitted to establish relations with banks that have relations with shell banks (FC 1.8).</p>		
<p>Recommendations and comments</p>		
<p>Compliance with FATF Recommendations</p>		

R.18	Compliant	
The supervisory and oversight system—competent authorities and SROs: Role, functions, duties and powers (including sanctions) (R.17, 23, 29 & 30)		
Description and analysis		
<p>R. 17</p> <p>Criminal sanctions (maximum of 2 years and/or BD 50,000 fine (USD 133,000) are imposed on anybody (including corporate bodies) who is found guilty of following acts, that are considered “offences related to money laundering” (Article 2.6 and 3.4 of DL 4/2001):</p> <ul style="list-style-type: none"> • non disclosure of suspicious transactions; • obstructing the execution of AMLU or judicial orders; • tipping-off on investigating or freezing orders. <p>Even if obviously the entities subjected to DL 4/2001 are targeted by these provisions, they are not limited to them as they refer to “any person (or entity)”.</p> <p>The tipping-off prohibition is twofold:</p> <ul style="list-style-type: none"> • There is the sanction of Article 3.4 of DL 4/2001, applicable to everybody (“any person”) who leaks information related to an “investigation order or attachment order” when this may prejudice the investigation; and • There is the prohibition of Article 8.2 of MO 7/2001, with punishment covered by Article 3.5 of DL 4/2001, for the entities subject to the DL 4/2001 to divulge information “with respect to money laundering” (<i>sic</i>) to the suspect or anybody else, except if the AMLU consents. <p>It might be a matter of translation, but the term “with respect to money laundering” is extremely vague and can be understood in so many ways as to affect legal security.</p> <p>Infringements of Regulations or MOs issued under the regime of the DL 4/2001 are punished by a maximum of 3 months imprisonment and/or BD 20,000 (USD 53,000) fine (Article 3.5 of DL 4/2001). Again the term “any person” is used, but this cannot be seen outside the context of the AML obligations and so this provision can logically only apply to the entities subject to such obligations.</p> <p>No statute of limitation applies in such cases (Article 3.6 of DL 4/2001). No corporate criminal liability is provided for violating the AML requirements, as Articles 2.5 and 3.3 of DL 4/2001 only apply for the offence of money laundering itself.</p> <p>Administrative sanctions can be imposed by the supervisory authorities for non-compliance with the anti-money laundering obligations. There are no formal and clear criteria to differentiate between the sanctions, and on who should decide and how it is decided what kind of sanction is to be applied, nor is there any regulated coordination between the competent authorities on this. In one instance, the AMLU has informed the BMA of a minor shortcoming by a reporting entity they had discovered during their investigations. In practice, it appears that minor violations stay within the supervisory agency to be dealt with, whereas major infringements would give rise to criminal proceedings and sanctions. The Public Prosecutor holds the opinion that every case of non-compliance should be reported to him as an offence pursuant Article 3.5 of DL 4/2001, and that the decision of taking action or not is his decision and his alone. No such case has reached the Public Prosecutor however.</p> <p>Sanctions available to the BMA to apply against licensees can be found in several documents including DL 4/2001, the 2001 Regulation, and the banks and insurance rulebooks (Financial Crimes and Enforcement Modules). DL 4/2001, applicable to all licensees, allows for imprisonment and fines. The regulations and the Financial Crimes Module of the banks and insurance rulebooks permit financial fines of up to BD 20,000 (USD 53,000) without a court order. The Enforcement Module also lists the BMA’s general powers of sanction, which may be applied where any of its regulations, including those contained in the FC Module, are breached. These sanctions range from informal warnings to, in extreme cases, cancellation of the license.</p>		

In addition to the penalties discussed under DL 4/2001 above, capital markets licensees are also subject to Article 23 of Resolution 1/2004. However, it is a concern that the primary AML regulation for capital markets licensees does not have specified penalties for non-compliance with the AML requirements. Instead, the only penalty identified in Resolution 1/2004 is if there is a breach of only one type of transaction (ownership thresholds) and the penalty is specified as follows: “a breach of the provisions of Articles (10) and (11) of this Law shall result in the cancellation of the transaction, the subject matter of the breach, and the person in breach shall bear all costs arising in this connection.” There are other sanctions available to the BMA for capital markets licensees; these currently fall under the Internal Regulation for those licensees in Article 73, where a range of penalties and sanctions are provided for breach of any law.

R. 23

The BMA became a consolidated regulator for all financial institutions in 2002. Prior to that, it had no responsibility for insurance or capital markets licensees. The insurance function is integrating gradually into the BMA, but the integration of capital markets has been more complicated because there is the added layer of supervision conducted through the SRO function that the BSE plays. The BMA is a well-regarded supervisory authority with experience in supervision and regulation, primarily, however, of banking institutions. The current situation with on-site inspection work within the BMA is as follows:

- **Banks:** On-site inspections for AML/CFT have been limited to banks (conventional and Islamic), covering only the 2001 Regulation. Because the FC module of the rulebook only became effective in April 2005, the BMA’s Compliance Unit has not yet completed any inspections using these new procedures, but will begin to do so during 2005.
- **Insurance:** The insurance rulebook was issued in May 2005. No inspections for AML/CFT have been completed on insurance licensees since the BMA became responsible for these entities in August 2002.
- **Capital Markets:** No inspections have been undertaken by the BMA on capital markets licensees for AML/CFT compliance.
- **Money changers, money brokers and other licensees not listed above:** All persons and legal entities provide money or value transfer service must be both registered (by the Ministry of Commerce) and licensed (by the BMA). The BMA is the supervisor for these entities and they are inspected as part of the BMA’s compliance program. Currently, these licensees are inspected using the 2001 Regulation.

The regulatory environment is in a state of transformation. The BMA is moving away from the original 2001 Regulation and its circular system, which provided the basic framework for compliance with the earlier FATF standards. The BMA is now drafting, for all but the capital markets licensees, a series of regulations, called rulebooks, to bring licensees into compliance with the revised FATF recommendations, while also providing more detailed requirements. To date, two bank rulebooks have been issued covering conventional banks and Islamic banks. An insurance rulebook was issued in May 2005 and that will be followed within the next few months by two additional rulebooks. These last two rulebooks will cover investment advisors and all other licensees, excluding the capital markets licensees. For capital markets licensees, the authorities inform us that those licensees will be covered by a new Securities and Exchange Regulation (SER), currently in draft form and expected to be passed once the new Central Bank law has been passed, which may be in a year or more from now. Per discussions with the Capital Markets Directorate, the SER will not cover AML/CFT issues. The rulebooks are a positive development, as they clarify the requirements of the BMA and introduce the concept of FT, which has been covered in only a very limited way by a previous circular.

The essential criteria require that for financial institutions that are subject to the Core Principles, the regulatory and supervisory measures that apply for prudential purposes and are relevant to money laundering should apply “in a similar manner for anti-money laundering and terrorist financing purposes.” The financial institutions that this criteria refers to are banking and deposit-taking businesses, insurers and insurance intermediaries, and collective investment schemes and market intermediaries. With the passage of the new insurance rulebook, insurers and insurance intermediaries will become subject to those types of prudential standards, but they are not subject to them currently. It is not clear if these prudential standards will be brought in for collective investment schemes and market intermediaries through the SER, when it is passed.

As noted under Recommendation 15, the AML/CFT rulebooks require that banks put into place controls to

ensure that criminals or their associates are not employed by the licensees. In addition, the BMA designates several key positions within the licensee senior management structure where a licensee must get approval from the BMA before hiring individuals for those positions. This ensures that full Fit and Proper criteria are assessed against individuals applying for these positions. The positions that are subject to this requirement are: Directors; Chief executives/general managers; Managers; and Controllers or holders of significant ownership or controlling interest in the license.

The Fit & Proper criteria for capital markets licensees are specified within Article 16 of the Internal Regulations. Individuals who apply for a brokerage license may not have declared bankruptcy, nor been convicted for a crime, resulting in punishment involving prison time. When a legal entity is involved, two sections of the regulation apply. First, the regulation indicates that brokers can be hired by these legal entities at a slightly lower standard, with the broker simply needing to have a “good reputation.” However, Article 16(B)(5) indicates that companies and those undertaking brokerage or market making functions in the company “should not have been...convicted of an offence.” It should be noted that there is no requirement for the BMA to approve any of the management or staff of the capital markets licensees.

R. 29

Chapter 13 (Investigation of Banking Firms) of the Bahrain Monetary Agency Law of 1973 grants the power of inspection to the BMA. The Chapter allows inspections to be carried out by BMA inspectors or qualified auditors. Banks are required to submit all documentation requested by the inspector within the timeframe established by the inspector. Power to enforce the AML/CFT law and regulations is available through both the existing Regulation of 2001 and the new rulebooks in both the Financial Crimes and the Enforcement Modules. This enforcement authority is for all financial institutions.

The 1973 BMA Law grants the power of inspection over “banking firms.” This power was carried over to insurance and capital markets licensees when they were merged into the BMA in 2002. However, this was done in very different ways. The insurance firms are now subject to inspection by the BMA via the 2002 Decree which changed all regulatory citations of “Ministry for Commerce and Agriculture” to the BMA. As a result, Article 18 of Legislative Decree No. 17 of 1987 With Respect to Insurance Companies and Organizations indicates now that the BMA “shall have the authority to exercise supervision and control over insurance companies and organizations.” Article 18 also gives the BMA full access to the books and records of the insurance licensees. Section FC 6.3.1 of the insurance rule provides for fines for any breach of the AML/CFT regulations, while the Enforcement Module of the insurance rulebook provides the detail on the sanctions and penalties available to the BMA in the event of a breach of law or regulation.

The right to inspect capital markets licensees has been drawn through Article 7 of the Bahrain Stock Exchange Law, amended by Decree 21/2002, which effectively made the capital markets licensees the responsibility of the BMA. The BMA, through the capital markets Internal Regulation, has the authority to request any document, as well as to sanction or penalize any licensee for a breach of any law or regulation. However, as mentioned in the response to Recommendation 17, it is of concern that there is not specific mention of penalties or sanctions for non-compliance of Resolution 1/2004 for non-compliance with AML standards. Instead, the only penalties mentioned are for breaching ownership thresholds.

There are adequate sanctions available to the BMA regarding AML/CFT compliance by its licensees. See response to Recommendation 17 above.

R. 30

All financial institutions are supervised and regulated by the BMA. Article 2 of the 1973 BMA Law establishes its operational independence within the government. Until 2002, the BMA was responsible for the supervision of banks, money changers, and money brokers. Insurance licensees were supervised by the Ministry of Industry and Commerce and capital markets licensees were supervised and regulated by the Bahrain Stock Exchange and the Ministry of Industry and Commerce.

With the assumption of the new responsibilities, substantial additional demands have been placed on the BMA.

<p>The BMA does not currently have sufficient resources, particularly human resources, to meet all of the supervisory and regulatory functions that are identified in the laws and regulations. The Compliance Unit, which currently comprises six individuals, includes no individuals with an insurance or capital markets background. However, these individuals do have strong supervisory backgrounds, having previously worked within the Inspection Directorate of the BMA. This expertise, along with specialty expertise for those two markets, will be critical when the BMA begins on-site inspection work of the capital markets and insurance licensees for compliance with AML/CFT laws and regulations later this year. It will be important that existing resources are not diverted entirely to inspecting these new entities as the existing entities (namely banks) are now subject to far more extensive regulation as of April 2005 and initial compliance needs to be reviewed. The compliance checks serve two important goals: to ensure that banks are actively integrating the new requirements into their AML/CFT programs; and to ensure that there is no confusion over any of the new elements within the rulebooks that will need to be addressed by the BMA.</p>		
<p>Recommendations and comments</p> <ul style="list-style-type: none"> • Extend corporate criminal liability to infringements of the AML requirements penalized by Articles 2.6 and 3.5 of DL 4/2001 • Inspections must be undertaken on the capital markets and insurance licensees. • Existing BMA resources, particularly human resources, need to be enhanced to meet its responsibilities as a consolidated supervisor. In particular, expertise in insurance and capital markets should be added to the Compliance Unit for the on-site inspection program. • Clarify or redraft Article 8.2 of MO 7/2001 to specify that the prohibition relates to information concerning the disclosure and the intervention of the FIU. • Establish clear rules and appropriate coordination regarding the criteria to either apply administrative sanctions or criminal penalties. 		
<p>Compliance with FATF Recommendations</p>		
R.17	Largely compliant	There is no coordination between criminal and administrative sanctioning and no corporate criminal liability provided for DL 4/2001 infringements.
R.23	Partially compliant	No inspections have been undertaken on the insurance or capital markets licensees.
R.29	Compliant	
R.30	Largely compliant	Additional resources are needed within the BMA to address the full work program on AML/CFT.
<p>Financial institutions–market entry and ownership/control (R.23)</p>		
<p>Description and analysis</p> <p>The BMA became a consolidated regulator for all financial institutions in 2002. Prior to that, it had no responsibility for insurance or capital markets licensees. The insurance function is integrating gradually into the BMA, but the integration of capital markets has been more complicated because there is the added layer of supervision conducted through the SRO function that the BSE plays. The BMA is a well-regarded supervisory authority with experience in supervision and regulation, primarily, however, of banking institutions.</p> <p>Financial institutions in Bahrain must be registered with the MOIC and licensed by the BMA. This includes banks, brokers, insurance firms and insurance brokers, investment advisors, money changers, and money brokers. Information on ownership and control of all of these entities is available on a public government website, allowing for full transparency of the BMA licensees.</p> <p>As noted under Recommendation 15, the AML/CFT rulebooks require that banks put into place controls to ensure that criminals or their associates are not employed by the licensees. In addition, the BMA designates several key positions within the licensee senior management structure where a licensee must get approval from the BMA before hiring individuals for those positions. This ensures that full Fit and Proper criteria are assessed against individuals applying for these positions. The positions that are subject to this requirement are: Directors; Chief executives/general managers; Managers; and Controllers or holders of significant ownership or controlling interest in the license.</p>		

The Fit & Proper criteria for capital markets licensees are specified within Article 16 of the Internal Regulations. Individuals who apply for a brokerage license may not have declared bankruptcy, nor been convicted for a crime, resulting in punishment involving prison time. When a legal entity is involved, two sections of the regulation apply. First, the regulation indicates that brokers can be hired by these legal entities at a slightly lower standard, with the broker simply needing to have a “good reputation.” However, Article 16(B)(5) indicates that companies and those undertaking brokerage or market making functions in the company “should not have been...convicted of an offence.” It should be noted that there is no requirement for the BMA to approve any of the management or staff of the capital markets licensees.

Recommendations and comments

Compliance with FATF Recommendations

R.23	Compliant
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AML/CFT Guidelines (R.25)

Description and analysis

The BMA issues its guidelines via regulations and circulars. This system is gradually being replaced, however, by a series of rulebooks that provide expanded detail on all the requirements. The BMA issued the FC Module of the bank rulebooks (conventional banks and Islamic banks) in early April 2005 and the insurance rulebook was issued in May 2005. These will be followed by a rulebook for investment advisors and other BMA licensees later this year. The capital markets licensees will not be under the rulebook system, which is of concern given the desire of standardization of practices and terminology across the BMA. Instead, the authorities informed us that they will be issuing a Securities and Exchange Regulation, which will have the same authority as the rulebook (i.e. a regulation), but will not be as expansive as the rulebooks. For example, there are no plans to create a Financial Crimes section in the SER to cover AML/CFT issues, despite the significant weaknesses with the current regulations on AML issued to capital markets licensees, including the lack of coverage of FT issues. On a general note, the BMA should consider establishing further guidance on FT for all financial institutions, as this is a relatively new area for financial institutions in Bahrain and institutions indicated little familiarity with this topic in discussions.

Feedback for financial institutions is limited to normal supervisory mechanisms including reports of examination, routine correspondence, and rulebooks and other documents issued for consultation. The assessment team spoke to several financial institutions that had provided STRs in the course of the previous year; none of these institutions indicated that they had received any feedback from the BMA or the AMLU on these filings.

Recommendations and comments

- The BMA should address the regulatory weaknesses identified in the assessment, particularly those related to capital markets licensees, since there are no current plans to enhance the existing regulatory framework for AML/CFT for those licensees.

Compliance with FATF Recommendations

R.25	Largely compliant	Capital markets regulations on AML/CFT must be enhanced to meet international standards.
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Ongoing supervision and monitoring (R.23, 29 & 32)

Description and analysis

R. 23

The BMA became a consolidated regulator for all financial institutions in 2002. Prior to that, it had no responsibility for insurance or capital markets licensees. The insurance function is integrating gradually into the BMA, but the integration of capital markets has been more complicated because there is the added layer of supervision conducted through the SRO function that the BSE plays. The BMA is a well-regarded supervisory authority with experience in supervision and regulation, primarily, however, of banking institutions. The current situation with on-site inspection work within the BMA is as follows:

- Banks: On-site inspections for AML/CFT have been limited to banks (conventional and Islamic), covering only the 2001 Regulation. Because the rulebooks only became effective in April 2005, the BMA's Compliance Unit has not yet completed any inspections using these new procedures, but will begin to do so during 2005.
- Insurance: The insurance rulebook had not been issued at the time of the assessment, but was subsequently issued in May 2005. Nevertheless, no inspections have been completed on insurance licensees since the BMA became responsible for these entities in August 2002.
- Capital Markets: No inspections have been undertaken by the BMA on capital markets licensees for AML/CFT compliance.
- Money changers, money brokers and other licensees not listed above: All persons and legal entities provide money or value transfer service must be both registered (by the Ministry of Commerce) and licensed (by the BMA). The BMA is the supervisor for these entities and they are inspected as part of the BMA's compliance program. Currently, these licensees are inspected using the 2001 Regulation.

The regulatory environment is in a state of transformation. The BMA is moving away from the original 2001 Regulation and its circular system, which provided the basic framework for compliance with the earlier FATF standards. The BMA is now drafting, for all but the capital markets licensees, a series of regulations, called rulebooks, which, with respect to AML/CFT will work toward bringing licensees into compliance with the revised FATF recommendations. To date, two bank rulebooks have been issued covering conventional banks and Islamic banks. An insurance rulebook was issued in May 2005 and that will be followed within the next few months by two additional rulebooks. These last two rulebooks will cover investment advisors and all other licensees, excluding the capital markets licensees. For capital markets licensees, the authorities inform us that those licensees will be covered by a new Securities and Exchange Regulation (SER) that is to be passed once the new Central Bank law has been passed, which may be in a year or more from now. The SER will not cover AML/CFT issues. The rulebooks are a positive development, as they clarify the requirements of the BMA and introduce the concept of FT, which has been covered in only a very limited way by a previous circular.

The essential criteria require that for financial institutions that are subject to the Core Principles, the regulatory and supervisory measures that apply for prudential purposes and are relevant to money laundering should apply "in a similar manner for anti-money laundering and terrorist financing purposes." The financial institutions that this criteria refers to are banking and deposit-taking businesses, insurers and insurance intermediaries, and collective investment schemes and market intermediaries. With the passage of the new insurance rulebook, insurers and insurance intermediaries will become subject to those types of prudential standards, but they are not subject to them currently. It is not clear if these prudential standards will be brought in for collective investment schemes and market intermediaries through the SER, when it is passed.

R. 29

Chapter 13 (Investigation of Banking Firms) of the BMA Law of 1973 grants the power of inspection to the BMA. The Chapter allows inspections to be carried out by BMA inspectors or qualified auditors. Banks are required to submit all documentation requested by the inspector within the timeframe established by the inspector. Power to enforce the AML/CFT law and regulations is available through both the existing Regulation of 2001 and the new rulebooks in both the Financial Crimes and the Enforcement Modules. This enforcement authority is for all financial institutions.

The 1973 BMA law grants the power of inspection over "banking firms." This power was carried over to insurance and capital markets licensees when they were merged into the BMA in 2002. However, this was done in very different ways. The insurance firms are now subject to inspection by the BMA via the 2002 Decree which changed all regulatory citations of "Ministry for Commerce and Agriculture" to the BMA. As a result, Article 18 of Legislative Decree No. 17 of 1987 With Respect to Insurance Companies and Organizations indicates now that the BMA "shall have the authority to exercise supervision and control over insurance companies and organizations." Article 18 also gives the BMA full access to the books and records of the insurance licensees. Section FC 6.3.1 of the insurance rule provides for fines for any breach of the AML/CFT regulations, while the Enforcement Module of the insurance rulebook provides the detail on the sanctions and penalties available to the BMA in the event of a breach of law or regulation.

<p>The right to inspect capital markets licensees has been drawn through Article 7 of the Bahrain Stock Exchange Law, amended by Decree 21/2002, which effectively made the capital markets licensees the responsibility of the BMA. The BMA, through the capital markets Internal Regulation, has the authority to request any document, as well as to sanction or penalize any licensee for a breach of any law or regulation. However, as mentioned in the response to Recommendation 17, it is of concern that there is not specific mention of penalties or sanctions for non-compliance of Resolution 1/2004 for non-compliance with AML standards. Instead, the only penalties mentioned are for breaching ownership thresholds.</p> <p>There are adequate sanctions available to the BMA regarding AML/CFT compliance by its licensees. See response to Recommendation 17 above.</p> <p>R. 32</p> <p>The BMA, specifically the Compliance Unit, does keep records and statistics on the number of inspections that it completes for AML/CFT and the number of sanctions imposed. There are few to date. In addition, the Compliance Unit also keeps statistics on the number of STRs have been filed by its licensees based on both type of license and chronologically. The BMA can be seen as effectively reviewing its systems on the basis that it must begin to incorporate the insurance and capital markets licensees into the inspection program. This has been the source of much discussion and planning, particularly within the Compliance Unit.</p>		
<p>Recommendations and comments</p> <ul style="list-style-type: none"> The BMA should move forward rapidly with its plans to inspect insurance and capital markets licensees for AML/CFT. 		
<p>Compliance with FATF Recommendations</p>		
R.23	Partially compliant	No inspections undertaken for capital markets or insurance licensees.
R.29	Compliant	
R.32	Compliant	
<p>Money or value transfer services (SR.VI)</p>		
<p>Description and analysis</p> <p>Money changers are licensed by the BMA and registered with the MOIC. They are subject to the rules and regulations of the BMA, including those related to AML. Money changers will be subject to a new rulebook later in 2005, which will incorporate elements of CFT into their regulatory program. Money changers are subject to routine on-site inspection by the BMA. As a result of recent inspections, many more STRs are now flowing from the money changers.</p> <p>There are seventeen licensed and registered money changers in Bahrain. Individuals wishing to transfer money out of Bahrain have two legal routes—the first is through the banks and the second is through these licensed and registered money changers (referred to as Authorized Money Transferors). The rulebook for banks prohibits transfers by any other means as follows: “Banks must <u>not</u> transfer funds for customers to a person or organization in another country by <i>any means</i> other than through an Authorized Money Transferor. Where a licensee is found to be in contravention of this rule, the Agency will not hesitate to impose sanctions upon that licensee (and in serious cases may revoke that licensee’s license.)” (FC 3.2.2).</p> <p>In reality, alternative or “underground” transfer systems do not appear to be a significant element of the financial landscape. The Authorized Money Transferors provide extremely cheap and efficient service, including “door to door” service. However, it is worth noting that the BMA is currently following up on two reported Hawala situations, both very small operations.</p>		
<p>Recommendations and comments</p>		
<p>Compliance with FATF Recommendations</p>		
SR.VI	Compliant	

Preventive Measures–Designated Non-Financial Businesses and Professions

Customer due diligence and record-keeping (R.12)
<p>Description and analysis</p> <p>The schedule to DL 4/2001 lists real property transactions, bullion dealing, legal practice and advocacy, audit and accountancy as activities covered by the legislation. The law does not cover casinos, company and trust service providers and dealers in precious metals and stones. The authorities indicate that there are no casinos or company and trust service providers in Bahrain. The MOIC considers precious metals and stones to fall under the definition of real property and therefore believes that dealers are covered by the schedule to MO 23/2002. The mission was not provided with a definition of real property that includes precious metals and stones and therefore does not consider that dealers in precious metals and stones are covered by the legal framework. This deficiency will be addressed by a proposed amendment to MO 23/2002 which has been prepared by the Ministry (see discussion under “Regulation, supervision and monitoring (R.17, 24-25)</p> <p>MO 23/2002, issued by the MOIC, applies various AML requirements on all persons listed in the Commercial Registry (whether a natural or corporate person), carrying out those activities specified in the Schedule to DL 4/2001, unless those persons are otherwise subject to the supervision of another specified body. The DNFBP listed in the schedule to DL 4/2001 are therefore subject to the provisions of that law as well as MO 23/2002.</p> <p>MO 7/2001 also creates certain obligations for DNFBPs. For the purpose of DNFBPs, MO 7/2001 is considered <i>lex generalis</i> and MO 23/2002 is considered <i>lex specialis</i>. Where both laws address the same issue, the provisions of MO 23/2002 are considered to prevail.</p> <p>DL 4/2001 and MO 23/2002 are supplemented by AML guidelines issued by the MOIC in 2003. It does not appear that the guidelines are enforceable through the Ministry’s general enforcement powers as these are limited to breaches of the Commercial Companies Law and its implementing regulations. They therefore do not meet the test of “law, regulation or other enforceable means” as set out in the interpretative note to the FATF recommendations.</p> <p>Customer due diligence:</p> <p>Article 4 of MO 23/2002 requires that, before establishing any business relationship, “registered persons” establish the identity of their customers, representatives and beneficiaries from the transaction by using all reasonable methods and adopting all possible precautions to ascertain the validity of documents or details concerning their identities. The article requires that registered persons should obtain the customer’s full name, date of birth, nationality, full details of identity card and passport, the CPR number, occupation, employer’s name and address, and usual place of residence.</p> <p>In the case of corporate persons, registered persons are required to obtain the customer’s full name, legal status, registration number and place, its objectives, name and address of head office and branches, names of the members of the board of directors and the legal representative of the corporate person and his identity. There is also a requirement that the constitutional documents of a corporate person including the memorandum and articles of association and the corporate persons deed of representation should be verified.</p> <p>Article 4 (12) of MO 7/2001 provides that where the customer is a lawyer, accountant, holder of a general power of attorney or authorized agent acting as a financial broker, he shall not be able to plead professional confidentiality as a reason for not disclosing the true identity of the beneficial owner.</p> <p>Article 4 (2) of MO 7/2001 requires that where a customer wants to establish a business relationship or undertake a separate transaction (defined as any transaction made outside the scope of the business relationship) for an amount in excess of BD 10,000 (USD 27,000), he must be identified and must provide sufficient evidence of the source of funds.</p> <p>Article 4 of MO 23/2002 provides that a transaction or transactions which total less than BD 10,000 (USD 27,000) are exempt from customer identification requirements. The exemption is too wide and should be restricted to an occasional transaction or separate transactions as defined by MO 7/2001.</p>

The threshold of BD 10,000 (USD 27,000) used in MOs 7/2001 and 23/2002 is high in comparison to the suggested threshold for occasional transactions in Recommendation 5 of US\$/EUR 15,000. The threshold is also inconsistent across various laws. Under the Financial Crimes module of the BMA rulebook for banks (April 2005), the threshold for occasional transactions was lowered to BD 6,000 (USD16,000). The draft amendment to MO 23/2002 by MOIC will change the threshold for customer identification to BD 6,000 from the current BD 10,000.

Article 5 (4) of MO 23/2002 requires registered persons to apply their required CDD measures to all customers within one year of the effective date of the order.

Article 4 (5) of DL 4/2001 provides that in exceptional cases a business relationship can be initiated without completing the customer identification details where two authorized officers of the registered person provide reasons for the non-completion of the documents and provided that the required information will be provided within a reasonable time to be established by the registered person. The article provides that under such circumstances, no transaction related to the transfer of funds or rights shall be completed before the required documents have been submitted and ascertained to be correct.

Article 4.6 of MO 7/2001 provides that if the customer is an agent or a business or firm that is subject to the supervision of a controlling authority and resides in a country that has similar laws for the prohibition and combating of money laundering, it may be sufficient evidence to receive written confirmation from the customer of the availability of proof of the principal's identity, its registration and maintenance thereof.

Article 4.7 of MO 7/2001 provides that the procedures for proving a customer's identity and source of funds as indicated in the Order are not applicable under the following circumstances:

- If the customer is an organization affiliated to or under the supervision of the MOIC, the Bahrain Stock Exchange, the Ministry of Justice and Islamic Affairs, or if it is a company in which the government has a major stake, or if it is a company incorporated by virtue of a law or decree;
- If the subject matter of the transaction is payment of sums by the customer or on his behalf through another organization; and
- If a separate transaction takes place with or for the account of a third party with the intervention of a person who is subject to a supervisory authority who has provided confirmation that the identity of the third party has been established and registered according to the custody procedures for such persons.

These exemptions are too wide and have not been modified by any subsequent law or regulation, as is the case with the BMA Financial Crimes module in the rulebook for banks. The first exemption is apparently based on the assumption that there is an equivalent level of supervision by the named government departments. Neither MOIC or MOJ, for example, have started to assess compliance with AML laws by the entities they supervise and do not have supervisory experience comparable to the BMA. It is therefore not appropriate to create this exemption.

The second exemption is unclear and appears to be unnecessarily wide.

The third exemption which provides a basis for reliance on confirmations provided by a supervisory authority also presumes that all supervisory authorities undertake their work in a manner that is effectively equivalent to the AML regime in Bahrain. It does not provide the safeguards established in Recommendation 9 and therefore creates vulnerability in the AML framework for DNFBPs.

There is no requirement for institutions to undertake CDD measures when there is a suspicion of ML or where there are doubts about the veracity of CDD information previously obtained. There is also no requirement for on-going scrutiny of transactions during the course of a relationship to ensure that transactions are consistent with the institutions knowledge of the customer and for registered persons to consider making an STR where they are unable to complete CDD.

The provisions of the law in respect of auditors and accountants go beyond the requirements of the Recommendations that they be covered where they are engaged in the following activities:

- buying and selling of real estate;
- managing of client money, securities or other assets ;
- managing bank, savings or securities accounts;
- organizing contributions for the creation, operation or management of companies;
- creating, operating or managing legal persons or arrangements, and buying and selling of business entities.

The open-ended nature of the legal provision suggest that all activities of auditors and accountants are covered by the legislation.

Guidelines:

The MOIC guidelines recommend that businesses develop a risk-based approach to the process of CDD. They recommend that the approach developed by the Basel Committee could also be adopted by non-financial businesses. In this regard, the guidelines indicate that in determining the level of risk that might be associated with customers, businesses should have regard to the customer’s background, country of origin, persons in public or high profile positions, linked accounts and the type of business activity being conducted. Businesses are advised to apply more rigorous levels of due diligence to higher risk categories of customers.

The guidelines stress the importance of “registered persons” understanding the nature, size and type of financial activity that may be associated with a customer’s business in order to establish patterns of activity that may be expected over time. Registered persons are advised to continuously monitor the customer’s transactions to ensure that they remain consistent with the established profile.

The guidelines stress the importance of businesses knowing the ultimate beneficiary of a transaction and properly identifying such persons. They indicate that some jurisdictions allow anonymity of corporate ownership through various means including nominee or bearer shares and recommend that business should be aware of the beneficial owners of entities from such jurisdictions. In this regard, the guidelines caution that care should be exercised in accepting references from jurisdictions that are known to have inadequate AML systems.

The guidelines highlight that non-resident customers represent a specific type of risk that must be properly addressed. They include in the category, customers that have been referred by an affiliated company or firm. They indicate that particular care should be taken to ensure that customer identification documents can be linked to the customer in question and that it may be necessary to obtain certification of documents, third party references, independent contact, bank references or other means of substantiating the identity of the customer.

There is also no requirement that institutions have measures in place to prevent the misuse of technological developments in ML or FT schemes.

The guidelines specifically allude to the threat posed by high profile individuals, who are described as persons holding important positions in government or public companies or individuals or companies associated with such persons. They suggest that business should be on the alert when dealing with persons who come from countries known for corruption. The guidelines recommend that decisions to enter into business relationships with such high profile individuals should be taken by senior management.

While the guidelines address some issues related to PEPs, as outlined above, they do not advise registered persons to establish systems to identify customers as PEPs, subject the activity of such persons to enhanced monitoring, take reasonable measures to verify the source of wealth or source of funds and require senior management approval to maintain a relationship with an existing customer who is subsequently identified as a PEP.

Implementation:

Real estate firms visited have systems in place to identify their customers for their commercial purposes. In

general it appears that they require customers to produce the same types of documents required by MO 23/2002 (i.e., the CPR and a passport). The firms indicated that where identification procedures are not completed to their satisfaction they will not conduct business with the customer. One firm uses an electronic registration form which cannot be completed unless the identification details are entered. The firms indicated that they do not accept cash from customers and for transactions involving the purchase or sale of real estate, they require that the funds come to them through the customer's bank account. However, for transactions related to the leasing of real property they will accept direct credits by the customer into their bank account.

The firms did not, in general, have a framework for designating customers into various risk categories and were generally unfamiliar with the concept of a PEP.

Audit firms generally have rigorous customer take-on policies and practices that meet the requirements of Recommendation 5.

Jewelry firms do not appear to generally have appropriate systems in place to identify their customers although one firm visited did encourage customers to participate in a loyalty program under which their identity details would be recorded.

Record keeping:

Article 5 of MO 23/2002 requires that registered persons maintain information and documents related to the identity of customers and their representatives and beneficiaries of transactions as well as accounting and other records related to the details of transactions. In respect of transaction records, the law requires that the information should include the type of transaction, the date on which it was concluded, the amount and details related to the method of payment, and identification details. Registered persons are required to have a system for updating such records. Where transactions relate to accounting transfers, from customers or on their behalf, registered persons are required to ascertain that the transfers include the person who issued the order, originator of the transfer, his account number and address.

Article 5 of MO 7/2001 provides that institutions should maintain a register containing all details of transactions to enable the AMLU to follow-up every transaction as well as the institution's duties provided in the order. It is also required that records should allow the institution to respond in a reasonable time to enquiries from the AMLU in respect of implementing any orders issued with respect to disclosure of transactions including the identity of the owner of the funds or beneficiary thereof and monetary transactions conducted by the institutions, requiring proof of identity.

MO 23/2002 requires that documents and records, as well as related correspondence for the transactions shall be maintained for a period of five years from the date of completing the transaction. The law does not require that identification records be maintained for five years following the end of the customer relationship. However, this is covered by Article 5 of DL 4/2001 which is applicable to activities involving real property transactions, legal practice and advocacy, audit and accountancy, and bullion dealing. Since DL 4/2001 is considered *lex generalis* in respect of DNFBPs it is not clear that registered persons are adequately covered in respect of the maintenance of identity records.

Article 5 of MO 7/2001 provides that where a matter relates to investigations conducted by the AMLU, the register of transactions or any other documents shall be maintained after the expiry of the prescribed safekeeping period (generally speaking, five years) until the AMLU issues an order for the destruction of such records.

Implementation:

The real estate and jewelry firms visited were not familiar with the requirements of Bahrain's AML regime with respect to the maintenance of records. The record retention policies and practices of all firms visited were based on company policy and the requirements of the Commercial Companies Law. While such practices may be adequate to meet the FATF retention standard for transaction records, they may not always be adequate for the standard required for identification records.

Lawyers:

Lawyers are subject to the provisions of DL 4/2001 as “legal practice and advocacy” is listed in the activities of institutions to be covered by the law. The provisions of the law go beyond the international requirements in that all aspects of legal practice are subject to the provision of DL 4/2001 and not simply the required ones of:

- buying and selling of real estate;
- managing of client money, securities or other assets ;
- managing bank, savings or securities accounts;
- organizing contributions for the creation, operation or management of companies;
- creating, operating or managing legal persons or arrangements, and buying and selling of business entities.

This means, for example, that all clients of a lawyer should be identified and not merely the clients for whom the lawyer is performing the above activities. In practice, lawyers do not engage in buying and selling of real estate as all land transactions must be conducted through notaries who are part of the land registry department of the Ministry of Justice. Lawyers also do not take part in management of client money or bank, savings or securities accounts save for cases of non-Bahrainis who come to lawyers to create companies for them. In this case, a Bahraini bank account is required and the lawyer may open an account in the name of the corporation and arrange for money to be placed in the account on behalf of the client as an opening balance.

MO7/2001 issued by the Ministry of Finance apply to lawyers as it applies to all persons who are listed in the schedule to DL 4/2001. No other ministry has issued any secondary legislation pertaining to lawyers. It is clear that lawyers are not uniformly aware that either DL 4/2001 or MO 7/2001 applies to them. Some lawyers were not undertaking verification of customer identity or record keeping. Training is urgently required in this regard so that they fully understand their role in the AML framework.

The assessment team met with Bahraini legal practitioners. In one case, verification of client identification was kept for all clients, but in another case no client identification was required or being kept for any clients save for those who were asking the lawyer to create a company for them. Then, only the information required to open the company was being asked for and retained. This includes the details of the shareholders of the company, but a passport of the individual shareholder is taken only where they are the shareholder. If the shareholder is another company or legal person, only the copy of the certificate of incorporation of that legal entity is required for verification of identity.

Recommendations and comments		
<ul style="list-style-type: none"> • The exemptions from customer identification requirements in Article 4 of MO 23/2002 and Article 7 of MO 7/2001 should be reviewed to make them consistent with the FATF recommendations, particularly Recommendation 9. • The requirements in respect of beneficial ownership, PEPs, understanding the nature of a customer's business, introduced business and companies that have nominee shareholders or shares in bearer form should be addressed in law, regulation, or through other enforceable means. • The guidelines on measures to be employed for PEPs should be strengthened to require that registered persons establish systems to identify customers as PEPs and that the activity of such persons be subject to enhanced monitoring. • Provisions should be made for persons to undertake CDD measures when there is a suspicion of ML or FT or where there are doubts about the veracity of CDD information previously obtained. • Persons should be required to adopt measures to prevent the misuse of technological developments in ML or FT schemes. • Persons should be required to consider filing an STR in circumstances where they are unable to complete CDD measures in respect of a customer. • Provisions should be made for persons to undertake on-going scrutiny of transactions during the course of a relationship to ensure that transactions are consistent with the institutions knowledge of the customer. • MOIC should reinforce with all DNFPs that the requirements for the retention of customer identification records are those found in MO 4/2001 and not MO 23/2002. • MOIC should intensify its program of inspections to verify compliance with AML requirements. • Training for lawyers on the application of the DL 4/2001 to their practice of law. • Lawyers should keep client identification records on all their clients pursuant to the DL 4/2001 requirements. • MOIC or Ministry of Justice should issue MO for lawyers regarding CDD and record keeping. 		
Compliance with FATF Recommendations		
R.12	Partially compliant	<p>There are a number of deficiencies related to CDD and record keeping measures.</p> <p>There is no uniform understanding by lawyers that they need to identify and verify the identity of their clients and keep client identification for all clients for a minimum of five years after the termination of the client relationship.</p>
Monitoring of transactions and relationships (R.12 & 16)		
Description and analysis		
<p>Article 3 of MO 23/2002 requires that a registered person shall establish rules, procedures and internal regulations to allow it to uncover, combat and report suspicious transactions. The article indicates that the term suspicious transactions means any transaction or group of transactions about which doubts arise with the registered person concerning their link to money laundering. It indicates that doubts about whether a transaction is linked to money laundering may be related to the unusual size of transactions, repetition, nature, conditions and circumstances surrounding them, their unusual pattern that does not involve a clear economic objective and or obvious legal purpose, if the activity of the person involved in the transactions do not conform to their normal activities or if the domicile of such persons in situated in countries that do not adequately apply AML measures.</p> <p>Article 7 of MO 23/2002 requires the compliance officer to draw-up a report with a full description of the type of transaction, the date, the names of the parties involved, the reasons that it was considered to be suspicious and all information required by the AMLU. Where the compliance officer is satisfied that a transaction is not suspicious, he is not required to prepare the above-mentioned report, but must note the reasons for his conclusion.</p> <p>There is no specific requirement that the above records be maintained for a period of five years.</p> <p>There is no requirement for registered persons to give special attention to business relationships and transactions with persons from or in countries that do not or insufficiently apply the FATF Recommendations.</p> <p>Where transactions from countries that do not or insufficiently apply the FATF Recommendations have no apparent economic or visible lawful purpose, there is no requirement that the background and purpose of such</p>		

transactions be examined and written findings made available to assist competent authorities.

MOIC and MOJ have not developed systems to advise registered persons of countries with weak AML/CFT systems. And, there are no provisions to apply counter-measures in respect of countries that do not adequately apply the Recommendations

Guidelines:

The guidelines indicate that there are many reasons that a transaction or a group of transactions might be considered suspicious. They emphasize that the size of the transaction is not necessarily, by itself, a good indicator of suspicion and that regardless of their value, all suspicious transactions should be reported. The guidelines recommend that transactions should be monitored in the context of what is considered normal in the particular business or industry. They also indicate that transactions should be reviewed against all aspects of the customer’s business, financial history and background. This description does not include suspicion that funds have been used for terrorism, terrorists acts, terrorist organizations or those who finance terrorism.

The guidelines provide examples of suspicious transactions for lawyers, auditors, accountants, real estate brokers-consultants-managers, and jewelers-goldsmiths-other purveyors of high value moveable items. The guidelines caution that the examples provided are common indicators that would be useful to consider when determining if there are reasonable grounds to assess that a transaction is suspicious or unusual.

MOs 4/2001, 23/2002, and 7/2001 do not require the reporting of attempted transactions that are considered to be suspicious.

Discussions with firms visited suggested that their concept of suspicion was limited to a customer trying to undertake a transaction with a large amount a cash. Only one firm was aware of the industry specific examples provided in the MOIC guidelines.

Lawyers:

It is unclear that any ongoing monitoring is being undertaken by lawyers regarding their clients’ business.

Recommendations and comments

- MOIC needs to intensify its efforts to familiarize DNFBPs with the notion of suspicious transactions and the requirements for monitoring customer activity.
- Registered persons should be required to report attempted transactions that are considered to be suspicious.
- Registered persons should be required to give special attention to business relationships and transactions with persons from or in countries that do not or insufficiently apply the FATF Recommendations.
- Where transactions from countries that do not or insufficiently apply the FATF Recommendations have no apparent economic or visible lawful purpose, the background and purpose of such transactions should be examined and written findings should be available to assist competent authorities.
- There should be a requirement that records of suspicious transaction activity be maintained for a period of five years.
- MOIC and MOJ should develop systems to advise registered persons of countries with weak AML/CFT systems.
- MOIC or Ministry of Justice should issue MO to lawyers on above recommendations.

Compliance with FATF Recommendations

R.12	Partially compliant	MOIC has not yet started the process of assessing compliance and DNFBPs’ understanding of the concept of suspicious transactions is very narrow. There are no adequate provisions in respect of a number of issues related to the monitoring of suspicious activity.
R.16	Partially compliant	See comments in following section re compliance with recommendation 13.

Suspicious transaction reporting (R.16)

Description and analysis

Article 6 (e) of MO 23/2002 makes a registered person's compliance officer responsible for reporting suspicious reports to the AMLU.

Article 7 contains detailed provisions for the reporting of suspicious transactions. It requires that STRs be reported to the AMLU and the MOIC within 24 hours of the time they were identified. There is no exception relating to circumstances in which the activity giving rise to the suspicion is believed to be a tax related matter.

Protection afforded to registered persons and their employees in respect of the reporting of STRs is provided by Article 8 of MO 23/2003, which states that no registered persons or their employees shall be under any civil or criminal liability by reason of performing their obligations under the Order.

The compliance officer is required to draw-up a report with a full description of the type of transaction, the date the names of the parties involved, the reasons that it was considered to be suspicious, and all information required by the AMLU. The report must be sent to the AMLU and the MOIC. Where the compliance officer is satisfied that a transaction is not suspicious, he is not required to prepare the above-mentioned report, but must note the reasons for his conclusion.

The compliance officer is required to maintain a register of suspicious transactions to enable him to prepare periodic reports. The register must contain details including the type of transaction, date of reporting and customer details to provide clear information about the transaction and the action that was taken by the registered person.

MOIC indicates that there are no Self-Regulatory Organizations in Bahrain for DNFBPs. It is therefore expected that STRs will be filed in accordance with the provisions of Article 7 of MO 23/2002 (i.e. directly to the AMLU).

Implementation:

The real estate and jewelry firms visited were uncertain about the institutions to which STRs should be sent, as was one audit firm. In general, they seemed not to know of the AMLU and indicated that they would send STRs to MOIC. MOIC is entitled to receive STRs under Article 7 of MO 23/2002, but was unaware that some registered persons might not be simultaneously submitting the STR to the AMLU. The firms were generally not aware of the tipping-off offence. No STRs have been filed by DNFBPs.

Lawyers:

Lawyers are required to file suspicious transaction reports under Article 5(c) of DL 4/2001 and Article 8 of MO 7/2001 issued by the Ministry of Finance. Lawyers registered with the MOIC must comply with Article 7 of MO 23/2002 issued by the Ministry of Commerce. In practice, no lawyer has filed an STR since the inception of DL 4/2001. Some lawyers were not aware of the requirement to file or where they would be required to file.

Legal Privilege:

Some discussion of legal privilege is also warranted. Article 29 of the Advocacy Law states that "a lawyer who knew through his profession any events or information shall not disclose them even after the end of his power of attorney unless it is to prevent a felony or a misdemeanor or to report the occurrence of the same. A lawyer shall not be asked to give a testimony in a dispute in which he was a representative or a consultant without a written permission from his client to do so."

If, however, a lawyer is charged with an offence under Article 3.5 of DL 4/2001, failure to file an STR, for example, under the requirements of either MO 7/2001 issued by the Ministry of Finance or MO 23/2002 issued by the MOIC, Article 10.5 of DL 4/2001 states that "it shall not be a defense to the offences created under this Law that the accused was prohibited from disclosing any information available to him in respect of the offence or suspicion thereof where the prohibition is imposed by law or otherwise."

<p>Both the Ministry of Justice and private lawyers confirmed that this could mean that a client in the case may lose legal privilege where a lawyer was charged in a case of failure to file an STR, perhaps where he had learned of facts during a privileged conversation with his client. Article 20 of the Constitution of the Kingdom of Bahrain guarantees legal representation. Article 20e states, “every person accused of an offence must have a lawyer to defend him with his consent.” It was conceded that Article 10.5 of DL 4/2001 could deprive a person of the right to counsel and therefore could be challenged as being unconstitutional. Bahrain has recently set up a Constitutional Court where such matters can be referred.</p> <p>It was clear from discussions with private practitioners that they are unclear on their obligations under the DL 4/2001 regarding filing of STRs. They are also unclear on when they would breach legal privilege. All agreed that legal privilege attached both at an advice stage (for example, regarding company formation) and also at a litigation stage, either criminal or civil. All also agreed that if, in an extreme case, they themselves were charged with an offence and asked by the court, they would breach legal privilege in order to comply with Article 10.5 of DL 4/2001. Some felt that they would also breach that privilege if they were questioned by the AMLU without being a defendant, reflecting perhaps, the newness of democracy in Bahrain. The constitution, which guarantees the right to a fair trial and the right to counsel, was brought into force in 2002. A guaranteed right to legal privilege is therefore new. There have been few legal challenges to legislation in Bahrain as it is still not considered within the purview of the population to challenge laws set out by the government or the King. Nobody has yet challenged Article 10.5 of DL 4/2001. Such a challenge would provide useful judicial opinion and precedent on this matter. All agreed that, in the absence of such legal precedent, further clarification of the law and the issuance of guidance on this matter by the Ministry of Justice is urgently needed.</p>		
<p>Recommendations and comments</p> <ul style="list-style-type: none"> • MOIC needs to intensify its efforts to familiarize DNFBPs with the requirements for the reporting of suspicious transactions and in particular reinforcing that STRs should be sent to the AMLU. • Ministry of Justice should issue regulations and guidance regarding the clarification of requirements to file STRs and how this requirement can be complied with in the face of legal privilege. • Urgent training for lawyers is required regarding the filing of STRs for suspicious transactions or attempted transactions by their clients. • MO to be issued to lawyers by either the Ministry of Justice or the MOIC regarding STRs; clarification needed on legal privilege and filing STRs. • Ministry of Justice and MOIC to coordinate and decide which Ministry to conduct onsite inspections of lawyers. 		
<p>Compliance with FATF Recommendations</p>		
<p>R.16</p>	<p>Partially compliant</p>	<p>MOIC has not yet started the process of assessing compliance and DNFBPs appear to have little knowledge of their obligation to send STRs to the AMLU. Law and some regulation in place but no clear understanding by lawyers of their obligation to file.</p>
<p>Internal controls, compliance & audit (R.16)</p>		
<p>Description and analysis</p> <p>Article 6 of MO 23/2002 requires a registered person to appoint a senior officer, on obtaining approval of the MOIC, to monitor its compliance with the requirements of the law. It is a requirement that such officer have full knowledge of national legislation and other international rules and guidelines related to combating money laundering, including those issued by the FATF.</p> <p>The compliance officer is required to ascertain the appropriateness of the registered person’s internal control systems and procedures for achieving compliance with the provisions of the Order. The compliance officer must ensure that employees are properly trained to meet their duties under the order and must monitor the extent to which they comply with the internal rules, systems and procedures related to money laundering. There is no requirement that internal programs be developed to address the risk posed by the financing of terrorism or that there should be an audit to assess the effectiveness of AML systems. The draft amendment to MO 23/2002 addresses the deficiency related to the financing of terrorism.</p>		

Article 3 of MO 23/2002 provides that registered persons shall lay down rules, procedures and internal regulations that enable them to uncover and report suspicious transactions.

Article 3 of MO 7/2001 required institutions to prepare regular and continuous training programs for concerned employees in laws relating to the prohibition and combating of money laundering, the institutions AML policies and regulations and new developments in the areas of ML and other suspicious activities and ways of identifying such activities.

There is no specific requirement for the compliance officer to have timely access to customer identification information data and other CDD information, transaction records and other relevant information. There is also no requirement for institutions to put in place screening procedures to ensure high standards when hiring employees.

Guidelines:

The guidelines recommend that AML should be adopted as an important part of the general corporate culture of registered persons. They recommend that staff who will be responsible for interacting directly with customers should be properly trained from the point of induction into the business and through on-going refresher training.

The guidelines also stress that registered persons who operate in a number of countries should ensure that their measures are applied across their entire network.

Implementation:

The real estate and jewelry firms visited did not have any internal systems and controls that were specifically geared to address their AML vulnerability. There were generally no programs for staff training that focused on AML issues. One small jewelry firm did however have an internal AML system in place. It has provided AML training for its staff and has designated an MLRO. Its has not only adopted procedures for its retail operation, but also for its wholesale activities where its purchases gold for the manufacturing aspect of its operations. Some audit firms do not have adequate internal AML systems.

Lawyers:

It is unclear that there are internal controls or systems in place in law firms regarding AML/CFT.

Recommendations and comments

- DNFBPs should be required to undertake audits to assess the effectiveness of their AML systems.
- There should be a requirement for compliance officers to have timely access to customer identification information data and other CDD information, transaction records and other relevant information.
- There should be a requirement for registered persons to have screening procedures to ensure high standards when hiring employees.
- Either the Ministry of Justice or the MOIC should issue a MO mandating onsite inspections of lawyers.
- Coordination between the Ministry of Justice and MOIC to determine who is best suited to conduct the onsite inspections is critical.
- Onsite inspections should be carried out on lawyers to ensure compliance with the requirements of the DL 4/2001.
- MO should be issued to lawyers regarding the application of DL 4/2001 to their practices.

Compliance with FATF Recommendations

R.16	Partially compliant	MOIC has not yet started the process of assessing compliance. There are inadequate provisions in respect of a number of issues relating to the maintenance of effective internal systems.
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Regulation, supervision and monitoring (R.17, 24-25)

Description and analysis

The MOIC is responsible for the registration of all business in Bahrain. Businesses are required to be registered in the commercial register within one month of commencing operations. MOIC reports that in practice businesses are required to be registered prior to commencing operations and taking up occupation of premises. This role makes the Ministry an important first line of defense in the fight against money laundering and terrorist financing.

In undertaking its due diligence, the Ministry requires applicants to produce personal identification documents and evidence of beneficial ownership. It also reviews financial statements, and a “receipt of a capital certificate” from the applicant’s bank indicating that funds deposited in the applicant’s account have been subject to bank’s AML procedures. Due diligence is undertaken on directors, shareholders, and partners of applicants. The MOIC uses a real time on-line system in which information goes live as soon as it is entered and accepted in the system.

In April 2005, the Ministry signed a contract with World Check to enhance its due diligence capabilities. Prior to signing the contract the Ministry used World Check on an experimental basis for a period of one month. Over the next six months the Ministry plans to use World Check in the process of conducting retroactive due diligence on its existing database of registrants.

Over the next three months, the Ministry plans to roll out a new system to be known as e-investor. The system will electronically link all government agencies that play a role in the registration of business in an effort to make the process faster and more efficient. An application being processed by MOIC will be automatically available to other departments, such as the BMA, that may have an interest in the particular applicant. Where the applicant requires a banking license, for example, the BMA will be able to undertake its review of the application at the same time it is being processed by MOIC. The BMA does not appear to be aware of this initiative. In light of the integral role MOIC envisages for the BMA and other agencies in this regard, it should widen its consultation before proceeding further with the proposal.

Under Article 2 of MO 23/2002, which was issued by MOIC, persons under the supervision of the Ministry of Justice and Islamic Affairs, the Ministry of Labour and Social Affairs, the BMA and the BSE are excluded from the scope of the application of the law. DNFBPs activities that fall under the scope of the law are therefore real property transactions, legal practice and advocacy and audit and accountancy. The Ministry plans to expand the scope of DNFBPs to include automobile buying/selling leasing, auctions, galleries, other purveyors of high value moveable property, and any other activities which the Minister shall decide from time to time.

MOIC indicated that its powers of supervision and inspection of DNFBPs arise from the Commercial Companies Law 21/2001 (CCL 21/2001) and its implementing regulations. Article 351 of the law indicates that MOIC “shall supervise companies governed by the provisions of this Law with respect to the implementation of this Law and the proper enforcement of its provisions and the provisions of the Memoranda of Association of these companies.” Article 243 of the implementing regulations is similarly worded.

The wording of these provisions appears to be specific to the supervisory powers relative to CCL 21/2001. To date, MOIC has undertaken its supervisory responsibility for DNFBPs without challenge and in all likelihood, may continue to do so. However, for the avoidance of doubt, it is recommended that MOIC seek to have its supervisory powers in relation to MO 23/2002 provided more explicitly.

MOIC has developed AML training programs for its staff. Staff are required to undergo a training program upon joining the Ministry and external consultants have provided training to other selected members of staff. It has appointed an MLRO to whom its own staff must report suspicious transactions. MOIC also expects to receive copies of STRs submitted to the AMLU by DNFBPs. MOIC does not plan to undertake its own investigation into the reports, but where necessary, would be willing to provide assistance to the AMLU in its investigations.

Article 6 of MO 23/2002 requires the appointment of an AML compliance officer. MOIC requires such persons to sign a certificate indicating that he understands the AML laws and will uphold the integrity of DL 4/2001 and MO 23/2002. The compliance officer also undertakes to cooperate in investigations and prosecutions of any persons involved in money laundering activities. The certificate signed by the compliance officer does not make

reference to MO 7/2001.

At the time of the mission, there were 46,000 persons listed in the commercial registry. MOIC targets to perform 10,000 visits per year. These visits are primarily geared towards verifying compliance with commercial registration requirements. The Ministry has 13 inspectors who visit approximately 8 registered persons per day.

The Ministry has determined that approximately 1,700 registrants meet the definition of DNFBBs. At the time of the mission, MOIC had undertaken 178 AML visits to DNFBBs for 2005. 20 visits undertaken during March focused on entities deemed to be higher risk. The judgment on their risk profile was based on their size and the nature of their activities. Institutions visited included law firms, audit firms, jewelers, real estate agents, dealers in high value automobiles, and import/export businesses. In some of their visits to registrants in 2005, MOIC was accompanied by the AMLU and the Ministry's Financial Analysis Department.

In light of its current strategy of visiting 10,000 registrants per year, the Ministry will be unable to effectively supervise the activities of DNFBBs. Supervision of these entities will require periodic visits to assess compliance with their obligations under MOs 4/2001, 7/2001, and 23/2002. The current rate of 8 visits per day will mean that no visit will be long enough to allow the Ministry's staff to undertake this assessment in an effective manner.

The Ministry sent a checklist to registrants asking them to assess their compliance with the AML law. There was no requirement that the questionnaire be returned. MOIC should consider asking registrants to return the completed questionnaire, as this would be a useful input in the development of a risk-based approach to undertaking their supervisory responsibility.

MOIC plans to take supervisory responsibility for lawyers through the proposed amendment to the existing legislation. This initiative on the part of MOIC is not being undertaken in coordination with the Ministry of Justice, which is not only unaware of MOIC's plans but indicates that it has its own plans for the supervision of lawyers as DNFBBs. This situation creates confusion about the proposed arrangements for the supervision of lawyers as DNFBBs and should be discussed by the two Ministries. It is of particular significance in an environment in which a number of DNFBBs are already uncertain about the AML Decrees and Orders that are applicable to them.

MOIC has prepared a draft amendment to MO 23/2002. A schedule to the order will list persons with the following occupations as being subject to the Order:

- Audit and accountancy;
- Legal practice and advocacy;
- Real estate buying/selling and leasing;
- Precious metals and precious stones dealers;
- Automobile buying/selling leasing;
- Auctions;
- Galleries and other purveyors of high value moveable property; and
- Any other activities which the Minister shall decide from time to time.

The amendment will reduce the threshold for the exemption from customer identification from BD 10,000 (USD 27,000) to BD 6,000 (USD 15,915) and will indicate that all references to money laundering shall include the financing of terrorism.

MO 23/2003 also provides that any breach of its provisions can be punishable by imprisonment not exceeding 3 months and/or a fine of BD 20,000 (USD 53,000). In addition, the MOIC has the power to apply the sanction of striking a person off the list of registered persons.

It does not appear that the guidelines are enforceable through Ministry's general enforcement powers as these are limited to breaches of the Commercial Companies Law and its implementing regulations. They, therefore, do not meet the test of "law, regulation or other enforceable means" as required in the interpretative note to the FATAF Recommendations. In addition, the sanction regime for DNFBBs would be enhanced with the provision of a

wider range of sanctions that could be progressively applied by MOIC.

Lawyers:

Bahraini lawyers are required to be licensed by the Ministry of Justice if they are sole practitioners or heading a practice or firm. Other Bahraini lawyers who work for them may or may not have a license from the Ministry of Justice. If they do not have a license from the Ministry of Justice, they must have a business license from the MOIC. Foreign lawyers who work for Bahraini lawyers must have a license from the MOIC and are ineligible to be granted a license from the Ministry of Justice. The few foreign legal firms that operate in Bahrain are licensed by the MOIC only, unless they operate in partnership or other arrangement with a Bahraini lawyer in which case, the Bahraini lawyer will have a license from the Ministry of Justice and the non-Bahraini members of the firm will be licensed by the MOIC. There is a plan in the MOIC to require all lawyers, Bahraini and non-Bahraini, to obtain a license from the MOIC in order to operate a legal business.

There is no onsite monitoring program currently in place for lawyers by either the Ministry of Justice or the MOIC. There is no AML/CFT compliance checking program. The MOIC is planning on beginning an AML/CFT onsite inspection program for all lawyers, whether licensed by them or not.

While the Ministry of Justice accepts that the MOIC may require all lawyers to obtain a commercial license to operate legal business, it disputes the authority of the MOIC to conduct AML/CFT compliance checks on all lawyers. Further, the Ministry of Justice indicated that it is the natural supervisor of lawyers in this area as it issues the practicing certificates and needs to ensure that its licensees are competent in all respects to practice law. Neither ministry has yet issued a MO mandating onsite inspections.

Lawyers with MOIC business licenses are subject to the same sanctions as other DNFBPs (see above). Lawyers with Ministry of Justice licenses are subject to Article 43 of the Regulatory Decree No. 26/1980 concerning the Advocacy Law (the “Advocacy Law”) and, when they have breached any of the requirements in the advocacy law, sanctions include:

1. Notice.
2. Reproach.
3. Prevention from practicing the profession for 3 years.
4. Writing off the lawyer’s name from the Table.

It is unclear that a breach of DL 4/2001 would give rise to a disciplinary matter under the Advocacy Law, as it only deals with issues of client money and the behavior of lawyers during trial. Contraventions of DL 4/2001 by a lawyer would result in the possibility of criminal sanctions as laid out under Article 3.5 of DL 4/2001.

Recommendations and comments

- For the avoidance of doubt, MOIC should have its supervisory powers in relation to MO 23/2002 provided more explicitly in law. It should also ensure that all AML requirements in respect of DNFBPs are addressed through law, regulation or other enforceable means.
- MOIC should develop a wider range of sanctions to make the sanction regime more effective.
- MOIC and MOJ should agree on a single supervisory arrangement for lawyers as DNFBPs.
- MOIC needs to generally intensify its efforts to promote awareness of AML/CFT legislative and regulatory requirements among DNFBPs.
- MOIC should consider requesting DNFBPs to return their self-assessment circulars as it could be a useful input as the Ministry tries to establish a risk-based framework for its supervisory responsibility for DNFBPs.
- MOIC should increase its staff compliment to allow it to effectively supervise the DNFBP sector.
- MOIC should amend the certificate signed by compliance officers to include reference to MO 7/2001.
- Appropriate civil and administrative sanctions should be created for failure to comply with DL 4/2001 and any consequent Ministerial Order.

Compliance with FATF Recommendations

R.17	Partially compliant	A wider range of sanctions would enhance the effectiveness of the current regime. There are no clear civil or administrative sanctions for failure to comply with the customer due diligence requirements in DL 4/2001; no onsite inspections for AML compliance by either the Ministry of Justice or the MOIC.
R.24	Non-compliant	No legal arrangements in place for DNFBPs and regulatory arrangements for existing DNFBPs are unsatisfactory.
R.25	Partially compliant	The Ministry of Finance has issued a MO to advise financial institutions (including lawyers) on their obligations under DL 4/2001. For lawyers registered with the MOIC, MO 23/2002 also applies. Neither deal specifically with issues arising for lawyers, particularly with reference to legal privilege.
Other non-financial businesses and professions—Modern secure transaction techniques (R.20)		
Description and analysis		
<p>The MOIC has prepared a draft amendment to MO 23/2002. Under the proposed amendment, the schedule to the Order will be expanded to include automobile buying/selling leasing, auctions, galleries, other purveyors of high value moveable property, and any other activities which the Minister shall decide from time to time. MOIC will have supervisory responsibility for these new categories of DNFBP. Because the draft Order also addresses the financing of terrorism, it will not be finalized until the planned amendments to MO 4/2001 are effective.</p> <p>Even though they are not covered under the current AML regime, the Ministry included dealers in high value automobiles in its AML awareness raising visits in March 2005.</p> <p>There are no specific provisions related to the threat posed by new technologies and the provisions of MO 7/2001 create vulnerabilities in relation to non face to face customers (see previous discussion under CDD Recommendation 12).</p>		
Recommendations and comments		
<ul style="list-style-type: none"> Registered person should be required to pay attention to the threats posed by new technologies. 		
Compliance with FATF Recommendations		
R.20	Partially compliant	Weaknesses relate to the absence of provisions in respect of the threat posed by new technologies and the provisions of MO 7 7/2001.

Legal Persons and Arrangements & Nonprofit Organizations

Legal Persons—Access to beneficial ownership and control information (R.33)		
Description and analysis		
<p>There are measures in place to prevent the unlawful use of legal persons by money launderers, but these measures cover banking, insurance, money changers, and money brokers. Capital markets licensees are not currently covered. The financial institutions that are covered are subject to requirements in the 2001 Regulation and the rulebooks for banks and insurance licensees. The 2001 Regulation, which is currently applicable to money changers and money brokers, highlights legal persons in Section 4.3. The CDD requirements in Section 4.3 require that the financial institution gather information on the: entity name, registration number, legal form, registered address, and type of business activity. This information is verified through receipt of specified documentation. In addition, licensees are required to (Section 4.3(i) and (ii)):</p> <ul style="list-style-type: none"> Make enquiries as to the structure of the company so as to sufficiently determine the provider of funds, the principal owner(s) of the shares and those who have control over the funds; and Require corporate customers to update them on significant changes to ownership and/or legal structure. <p>The rulebooks for banks and insurance licensees have differing requirements, with more stringent requirements</p>		

applied to banks. The bank rulebooks (FC 1.6.1 and FC 1.6.2) indicate that a “bank must obtain a signed statement from all new customers confirming whether or not the customer is acting on their own behalf or not....A bank must establish and verify the identity of the customer and, where applicable, the party/parties on whose behalf the customer is acting (including that of the beneficial owner of the funds) prior to conducting transactions.” The rulebook requirements are further enhanced in FC 1.6.3 with the requirement that “where a customer is acting on behalf of third parties, the bank must obtain a signed statement from the beneficial owner(s) that he/they is/are the ultimate beneficiary or beneficial owner of the account/facility, and giving authority to the customer to act on his/their behalf.”

The insurance rulebook more closely mirrors the requirements of the 2001 Regulation, with one exception. There is no requirement to conduct the due diligence identified in the two bullets above. However, the rulebook does require insurance companies to obtain a list of and verify the identity of the main shareholders of a legal entity holding 20% or more of the issued capital (FC 2.2.20(e)). In addition, Section FC 2.2.29 applies the CDD requirements to beneficiaries of life insurance policies, with the added requirement that the insurance licensee must establish the relationship between the insured party and the beneficiary or beneficiaries. A final key point is identified in FC 2.2.1, where it is required that “where a customer is acting on behalf of another, the insurance licensee must be reasonably satisfied with both their identities.”

Capital markets licensees are currently subject to MO 7/2001 and Resolution 1/2004. The MO only covers the general topic of client verification and does not address specific issues such as CDD for legal persons or determination of beneficial owners. Resolution 1/2004 provides slightly more detail and requires that information on the “particulars of the company’s owners and its main shareholders” (Article 6(f)) be obtained prior to account opening. This same language is repeated in Article 8(2). It is not clear what action would be taken if the companies owners and main shareholders are themselves companies, trusts or other legal arrangements. For this reason, the requirements of the Resolution do not appear to provide sufficient guidance to capital markets licensees regarding the information that should be obtained from legal persons to protect against the licensees being used for money laundering purposes.

Financial institutions have ready access to company information on Bahrain-registered companies via a public government website. All beneficial ownership and control information is placed on the Commercial Register at the time of registration and updated when new information arrives. For companies incorporated outside of Bahrain, financial institutions indicated that they use a series of mechanisms to determine beneficial ownership—from directly asking the client to doing research using public and private sources.

Bearer shares are permitted in Bahrain through the Commercial Companies Law. Article 115 states that “A company may issue bearer shares according to the rules and restrictions to be determined by an Order of the Minister of Commerce and Industry.” However, in discussions with the BMA and financial institutions, there was the general view that these were not permitted and none of the financial institutions had seen these instruments. In addition, no implementing regulations allowing bearer shares have been promulgated.

Recommendations and comments

- The capital markets regulations should be enhanced with respect to their approach to beneficial ownership. The regulations should mirror the approach taken in the bank rulebooks, which establishes a more robust requirement for licensees to know the beneficial owners of legal persons.

Compliance with FATF Recommendations

R.33 | Largely compliant | The capital markets regulations are too weak to be effective.

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

Description and analysis

There is no trust law in Bahrain at the current time and as a result, no trust arrangements have been put in place. The BMA indicated that there is not yet comfort with the trust structure and this business will not develop until there is legal standing that will allow the trust arrangements to be protected by law. Currently, because of the lack of legal certainty as to how trusts would be treated in a court of law, none have been created.

<p>It is important to note, however, that the BMA has included language about CDD for trusts in both its 2001 regulation and in the new rulebooks. This is in anticipation of the development of trust law and subsequent trust business. A draft trust law has been developed and it is currently before Parliament, although quick action on the bill is not expected. Once the trust law is passed, the BMA will need to review its CDD requirements for trusts to ensure that they are in conformity with the new law.</p>		
<p>Recommendations and comments</p>		
<p>Compliance with FATF Recommendations</p>		
<p>R.34</p>	<p>Not applicable</p>	<p>No trust law or instruments in Bahrain.</p>
<p>Nonprofit organizations (SR.VIII)</p>		
<p>Description and analysis</p>		
<p>Non-profit organizations are regulated by the Ministry of Social Affairs (MSA), a new ministry created by the recent reorganization of the work of the former Ministry of Labour and Social Affairs.</p> <p>The legal framework for the supervision of NPOs is established by a number of laws which have the objective of establishing an environment of sound corporate governance for these organizations. One of the principal laws under this framework is Regulatory Decree No 21/1989 Concerning the Issuance of a Law on Social and Cultural Societies and Clubs and Private Organizations Working in the Field of Sports and the Youth and Private Establishments (RD 21/1989). All entities that engage in fund raising activities are covered by this law.</p> <p>Article 4 of the law provides that applications for the establishment of a society must be made by at least ten persons, none of whom may have a criminal conviction related to dishonor or dishonesty.</p> <p>Under Article 16, societies are required to have an annual budget and where their expenditures or revenues exceed BD 10,000 (USD 27,000) the board of directors is required to have its accounts subjected to an external audit. Copies of the final accounts, the budget and the reports of the auditor and of the board of directors must be attached with the invitation letter to be sent to members entitled to attend its annual general assembly. MSA meets the cost of external audits for charities.</p> <p>Under Article 17, societies are required to deposit all cash money with an approved bank, and inform MSA of the establishment of the relationship. Societies are also required to inform MSA when they change banks, within one week from the date of the change. MSA has developed a form which certifies that a society has been registered. Banks expect to see this form before they open an account for a society. While the law does not appear to specifically require the MSA’s prior approval for a society to open a bank account, this has developed into a best practice and is referenced in the Financial Crimes module of the BMA’s rulebook for banks.</p> <p>Under Article 20, societies are not allowed to affiliate, participate or join a society, organization or club whose premises is outside Bahrain without prior permission from MSA.</p> <p>Article 22 provides that societies shall be subject to monitoring from MSA and that monitoring includes examination of the societies’ works and verification of their compliance with the law and the regulations and decisions of the general assembly.</p> <p>Ministerial Order 3/2004 (MO 3/2004) seeks to strengthen the legal framework for the regulation of societies and address some vulnerabilities related to the financing of terrorism.</p> <p>Article 2 requires that private organizations (defined to include organizations promulgated under RD 21/89) must maintain records of revenue and expenditure that include the name of each donor and beneficiary of a cash payment or donation. It must also provide the authorities with details of its accounts every three months via an information network established by MSA.</p> <p>Article 5 provides that the competent directorate, (defined as the Directorate of Development and Local Societies</p>		

(DDLDS)) within MSA, may conduct inspections on the activities of private organizations to ensure that they are complying with the provisions of the law. The manager, board of trustees and officers of organizations being inspected are required to provide DDLDS with any information, documents and particulars they require. DDLDS is required to submit its report to the Minister within 15 days of the date of inspection.

Article 7 provides that any payments in excess of BD 1,000 (USD 2,600) must be made through a financial institution.

Article 8 provides that with the exception of payments for books, publications and scientific and technical records, organizations shall not transfer any amounts abroad without the approval of MSA. Organizations wishing to make such transfers are required to submit evidence of the approval to financial institutions making the transfer.

Article 85 provides that MSA's approval is required where a society wishes to make a foreign transfer in excess of BD 3,000 (USD 8,000). A request must be submitted to MSA at least one week in advance of the intended date of transfer.

Article 89 of RD 21/89 establishes penalties for various breaches of its provisions. The punishment for such breaches is a term of imprisonment not exceeding six months and a fine not exceeding BD 500 (USD 1,300). MSA indicated that these punishments will soon be increased to a term of imprisonment not exceeding one year and a fine not exceeding BD 1,000 (USD 2,700).

Implementation:

At the time of the mission, there were 386 registered societies including 80 charities. The largest categories of societies are social societies (65), professional societies (51), foreign societies (43), foreign clubs (32), churches (20), corporations (20) Islamic charities (19) and women's societies (15). MSA is of the view that most of these societies do not fit the profile of organizations that are likely to send funds abroad. According to the authorities, the category that is most likely to send funds or resources abroad is the Islamic charities. These organizations often sponsor orphans in foreign countries and send funds to support them. The department reports that two societies are known to send resources abroad. The department is informed of the nature of the resources and the intended recipients, but does not have the capacity to verify information received in this regard. In instances of national or international disasters, societies can send funds abroad, but must do so through the Red Crescent.

The department reports that it has a good relationship with the Ministry of Interior and sends them the names of persons who apply for societies. In at least one instance, MOI objected to the name of one person out of a group of ten who applied to establish an organization.

DDLDS has a staff of 4 persons to undertake its work. These resources are inadequate to allow the department to undertake reviews of the financial information submitted by societies or to undertake inspections of these organizations. Staff members spend a substantial amount of their time attending general assembly meetings of the societies. In light of the large number of societies, this is a daily function for the staff.

DDLDS has not developed a risk-based approach to its supervisory function. Although it can isolate societies that have higher revenues/expenditures and those that are more likely to send funds out of the country, no attempt has been made to focus supervisory initiatives in this direction.

While banks appear to be aware of the requirement for charities to be licensed by MSA before establishing a banking relationship, it does not appear that they generally establish mechanisms that effectively monitor the transfer of funds abroad.

FC 1.5 of the Financial Crimes module of the BMA's banking rulebook cautions banks not to provide financial services to charitable funds and religious, sporting, social cooperatives, and professional societies until an original certificate authenticated by the relevant Ministry confirming the identities of persons purporting to act on their behalf (and authorizing them to use the service) has been obtained. Banks are advised that charities should be subject to enhanced monitoring and that they should develop a profile of anticipated account activity

<p>with particular reference to payee countries and recipient organizations. Banks are required to report all transfers in excess of BD 20,000 (USD 53,000) to the BMA. The rulebook does not, however, mention the requirement for charities to obtain the approval of MSA before making a foreign transfer in excess of BD 3,000 (USD 8,000).</p> <p>The department expects to see a significant increase in its staff resources over the next two months. Resources are expected to increase to 36 persons. This will significantly enhance the directorate’s ability to undertake its supervisory responsibilities. The directorate has made plans to provide a range of training for the new staff and to have them join its experienced inspectors when they visit societies. While MSA badly needs increased staff resources, the quantum of the increase will initially place a heavy burden on the Ministry as it tries to integrate the new staff into the operations of DDLS.</p> <p>The department also has an ambitious plan to create a database to facilitate the processing of financial transactions by societies. The system will allow participating organizations to process payments using a central facility. Data in this system will be available to DDLS, the society’s auditors and the society itself. It is hoped that the system will improve the efficiency and transparency of the operations of participating societies. MSA has already budgeted BD 55,000 (USD 146,000) for the necessary software and training and BD 250,000 (663,000) for the purchase of hardware and recruitment of staff.</p>		
<p>Recommendations and comments</p> <ul style="list-style-type: none"> • In terms of its program to address the potential for the abuse of charities for the financing of terrorism, DDLS should develop a more risk-based approach that focuses on potential vulnerability to this risk. • The BMA should consider revising FC 1.5 of the Financial Crimes module of the rulebook for banks to reflect the provision of Article 85 of RD 21/89 (i.e. that charities are required to obtain the approval of MSA before making a foreign transfer of funds in excess of BD 3,000 (USD 8,000)). 		
<p>Compliance with FATF Recommendations</p>		
<p>SR.VIII</p>	<p>Partially compliant</p>	<p>MSA has undertaken a review of the legal and regulatory framework for NPOs and has implemented a number of changes to address vulnerabilities in respect of the financing of terrorism. However, at the time of the mission, MSA did not have an effective framework for assessing compliance with these legal and regulatory requirements and the potential vulnerabilities were therefore not adequately addressed .</p>

National and International Cooperation

<p>National cooperation and coordination (R.31)</p>	
<p>Description and analysis</p> <p>The Policy Committee for the Prevention and Prohibition of Money Laundering (“Policy Committee”), coordinates all AML/CFT issues within Bahrain. The inter-ministerial committee was established pursuant to Article 4.1 of DL 4/2001 and MO 5/2001 within the Ministry of Finance. It is comprised of delegates from the Ministry of Finance, the Ministry of Industry and Commerce, the Ministry of Justice (Public prosecutor), Ministry of Interior (AMLU), customs, BMA and the stock exchange. With the conclusion of its first 3 year term, a new MO will extend the Policy Committee with representatives of the Ministry of Foreign Affairs, the Ministry of Labor, the Ministry of Social Affairs and the National Security Agency. The new Committee now covers both AML and CFT issues.</p> <p>Recently the Committee has been involved in a limited way in the preparation of the amended DL 4/2001 and the draft law on terrorism, which is now pending before the Parliament. However, the Policy Committee does not have a clear sense of the contents of the amendments or the timing of the passage of the amendments. Ideally, the Policy Committee should be given the authority to take charge of all revisions to DL 4/2001 and any related laws. The Legal Directorate of the Cabinet Office should take directions from the Policy Committee in this regard.</p> <p>Coordination and cooperation between supervisory agencies could be improved. Regarding coordination, there are numerous ministerial orders, regulations, circulars and rulebooks underpinning the AML/CFT program in</p>	

<p>Bahrain. The Policy Committee should take a central role in reviewing these instruments in order to ensure that there is a consistency of approach and a coordinated message. Another example where coordination and cooperation could be improved is that of inspecting the compliance of lawyers with the AML requirements under DL 4/2001. Both the Ministry of Justice and MOIC believe that they should supervise lawyers in this regard, although neither ministry has either issued a MO on this matter or undertaken onsite inspections. A coordinated approach to this issue is required. A final example of coordination involves the filing of STRs by supervisory authorities when they have inspected a licensee and found that an STR should have been filed. Some of the Bahrain supervisory authorities file STRs themselves, while others do not believe they have the power to do so. The Ministry of Justice has confirmed that it is their firm view that all supervisors can file STRs in this circumstance as DL 4/2001 states that “one” shall file (in the Arabic version) and this includes moral persons (ministries and supervisors). This is a matter that should be discussed within the Policy Committee so that all supervisory authorities are clear on this matter and adopt a coordinated approach to filing STRs.</p> <p>The interaction between the FIU and the supervisory agencies is based on custom and practical considerations, not on specific legal provisions. The AMLU and the BMA, for example, are legally bound to a high degree of confidentiality (Article 371 PC), and there is no legal framework regulating or coordinating any cooperative relationship between these natural allies. Recognizing that confidentiality remains an important consideration, they should be able to exchange information on non-compliance with the DL 4/2001 requirements by the reporting entities. Operational cooperation between law enforcement agencies, such as customs and police, is systematic and frequent.</p> <p>Generally, instructions and guidelines are issued by the supervisory authorities with limited consultation and coordination with the AMLU. There is some form of cooperation between the BMA and the AMLU, whereby the latter provides information supporting the supervisory and licensing function of the former. The BMA itself is bound to a strict confidentiality obligation which limits its operational cooperative possibilities, but is regularly involved in consultation processes with law enforcement. As both the BMA and the FIU receive the same STRs, they cross-check the information received. Minor irregularities in terms of compliance with the DL 4/2001 and related regulations, discovered during the FIU investigation, would be communicated to the supervisory to take administrative action (there has been one such case in the past). Major shortcomings established by the FIU would, however, be reported to the Public Prosecutor as an offence pursuant Article 3.5 of DL 4/2001, but there has been no such occasion as yet. No information concerning non-compliance has as yet been forwarded to the FIU by the supervisory authorities, although such infringement of DL 4/2001 is considered an offence that should be reported to the law enforcement authorities.</p>		
<p>Recommendations and comments</p> <ul style="list-style-type: none"> • Clear gateways should be created regulating communication between FIU and supervisory, especially in cases of non-compliance. • The Policy Committee should take a policy lead on revisions of DL 4/2001 and the Terrorism Law. • The Policy Committee should continue to take the lead in coordination and cooperation matters between ministries. • Appropriate Ministries should coordinate on the issue of inspecting lawyers for AML compliance. 		
<p>Compliance with FATF Recommendations</p>		
<p>R.31</p>	<p>Partially compliant</p>	<p>No gateways between law enforcement and supervisory for mutual assistance. Greater need for coordination and cooperation between ministries.</p>
<p>The Conventions and UN Special Resolutions (R.35 & SR.I)</p>		
<p>Description and analysis</p> <p>DL 17/1989 and Law 4/2004 have ratified the Vienna and Palermo Conventions respectively. The AML aspects of the two conventions have been implemented through DL 4/2001. Mutual legal assistance and extradition provisions are provided for by Articles 412 to 428 of the CPC. The Palermo Convention may not be fully implemented regarding criminalizing organizations carrying out primarily criminal activities.</p> <p>The 1999 convention has been ratified by Royal Decree 8 of 2004, but is still in the process of being implemented. The law on terrorist financing has been drafted and should be passed during the current session of the National Assembly. BMA regulations aimed at banking and insurance licensees address FT as well as ML,</p>		

requiring the reporting of suspicious transactions possibly linked to FT, and the screening of customers to ensure no dealings take place with names designated by the UN. Capital markets licensees, money changers and money brokers have no FT obligations currently. MO 23/2002, as amended, refers to terrorist financing and Ministry's AML Guidelines also refers to CFT.

In practice, Bahrain has complied with requests from the UN Security Council under UNSCR 1267 and has responded, in some cases, to other countries' requests for assistance.

Bahrain has signed the GCC Anti-Terrorism Agreement of 4 May 2004; and acceded to the Arab League Anti-Terrorism Convention (instrument of accession dated 22 April 1998, approved by Amiri Decree 15 of 1998).

Bahrain is also a party to the following international anti-terrorism conventions: (i) the Convention on Offences and Certain Other Acts Committed on Board Aircraft, 1963; (ii) the Convention for the Suppression of the Unlawful Seizure of Aircraft, 1970; (iii) the Convention for the Suppression of Unlawful Acts Against the Safety of Civil Aviation, 1971 (and the Protocol for the Suppression of Unlawful Acts of Violence at Airports, 1971); (iv) the Convention on the Marking of Plastic Explosives for the Purpose of Identification, 1991; and (v) the International Convention for the Suppression of Terrorist Bombings, 1998.

Parliamentary procedures are currently being followed towards Bahrain's accession to the following conventions: (i) the Convention on the Prevention and Punishment of Crimes Against Internationally Protected Persons, 1973; (ii) the Convention for the Suppression of Unlawful Acts Against the Safety of Maritime Navigation, 1988; (iii) the Convention Against the Taking of Hostages, 1979; and (iv) the Protocol for the Suppression of Unlawful Acts Against the Safety of Fixed Platforms, 1988. Finally, the Government of Bahrain is currently studying the possibility of accession to the Convention on the Physical Protection of Nuclear Material, 1980.

Regarding compliance with the UN Resolutions relating to the financing of terrorism, particularly UN Security Council Resolutions 1267 and 1373, the BMA circulates all UN designated names to its licensees, and requires these to confirm to the Agency the results of their searches. Three names designated by the UN were identified as having accounts in Bahrain, and their accounts were blocked. MO 23/2002, as amended, refers to terrorist financing and Ministry's AML Guidelines also refers to CFT. The MOIC website provides links to the UN, Bank of England, FATF and AMLU websites.

Recommendations and comments

- Fully implement the 1999 International Convention on the Suppression of Financing of Terrorism.
- Provide legal mechanisms to allow law enforcement to share information regarding AML/CFT and terrorism issues.

Compliance with FATF Recommendations

R.35	Partially compliant	Implement the International Convention for the Suppression of the Financing of Terrorism and confirm full implementation of the Palermo Convention with regard to criminalizing organizations of a criminal nature.
SR.I	Partially compliant	Implement the International Convention for the Suppression of the Financing of Terrorism.

Mutual Legal Assistance (R.32, 36-38, SR.V)

Description and analysis

Mutual legal assistance between judicial authorities is generally governed by Article 426 – 428 of the 2002 Code of Criminal Procedure (“Letters rogatory”). In money laundering related matters, Article 8 of the Anti-Money Laundering Law 4/2001 gives the AMLU a specific responsibility in the execution of foreign assistance requests, that goes beyond the cooperation at FIU level. Both regimes overlap to some degree, but here according to the judicial authorities, the CPC as the later law, takes precedence in case of conflict, not the *lex specialis*. Under both regimes the assistance is broad and virtually unrestricted, especially in money laundering cases but even in FT cases. It does not require dual criminality (also for coercive measures), only that the execution does not violate the public order of Bahrain (Article 427 CPC). The absence of a formal FT offence does not affect the mutual legal assistance capacity as it is not subject to the dual criminality principle.

No requests are refused using the fiscal exception pretext. Coercive measures, such as searches and seizures, do

however require the intervention of either the Public Prosecutor or the Court (Article 8.2 of DL 4/2001 – Article 427 CPC). Rogatory commissions should in principle pass the diplomatic procedure, but in urgent cases the request is handled in direct communication between the judicial authorities awaiting the arrival through diplomatic channels. Any refusal or delay should be explained (Article 8.1. of DL 4/2001). Article 7 of DL 4/2001 states that secrecy may not be used to defeat a request for information.

Execution of foreign confiscation orders is possible pursuant Article 12 Penal Code and Article 8.2&3 of DL 4/2001, including equivalent value confiscation (Article 3.2 of DL 4/2001). In the context of extraditions Article 423 CPC provides for the transfer of not only evidentiary material, but also instrumentalities and proceeds of crime. Foreign civil *in rem* confiscations can be dealt with according to Articles 252-255 of the Code of Civil Procedure through the intervention and *fiat* of the Senior Civil Court. No such requests have been made as yet.

No mechanisms or arrangements for determining the best venue for the prosecution, or for coordinating seizure and confiscation, in cross-border cases have been devised. This is dealt with on an *ad hoc* basis.

Disposal of the confiscated assets follows the general rule: they are devolved to the Treasury. The Bahrain authorities have not considered the establishment of an asset forfeiture fund.

Asset sharing with other countries is however made possible by Article 8.6 of DL 4/2001, even if this has not happened as yet.

The statistical data submitted by the authorities did unfortunately not contain any information on the MLA rendered in ML and predicate offence cases. No evidence provided on the length of time required to complete requests or the number of requests received.

Recommendations and comments

- Devise arrangements for coordinating seizure and confiscation.
- Consideration should be given to the utility to create an asset forfeiture fund.
- Statistics should be kept on the MLA requests (investigation, seizure and confiscation) pertaining to ML and predicate offenses in order to periodically review the efficiency of the system.

Compliance with FATF Recommendations

R.32	Non-compliant	No statistics were received on MLA concerning ML and predicate offenses.
R.36	Largely Compliant	No statistics received on MLA so efficiency could not be properly assessed.
R.37	Compliant	
R.38	Largely Compliant	No asset forfeiture fund considered.
SR.V	Largely Compliant	No statistics received on MLA so efficiency could not be properly assessed.

Extradition (R.32, 37 & 39, & SR.V)

Description and analysis

Extradition is governed by both the CPC (Article 412 to 425) and the DL 4/2001 (Article 8.3, 8.5 and 11). Again the CPC takes precedence in case of conflict. As a general rule, extradition is based on the extradition treaties Bahrain is party to and according to the relevant CPC provisions, but in the absence thereof the general rules of international law apply (Article 412 CPC). Extradition is subject to the dual criminality principle (Article 413.b CPC) and reciprocity (Article 11 of DL 4/2001). The dual criminality rule can be deviated from by treaty, whereas in the absence of any treaty the principle of reciprocity is upheld. To evaluate the dual criminality criterion it is not necessary that the formal qualification of the offence should be identical, but the conduct underlying the offence is taken into account. The requesting state needs to have jurisdiction over the crime. To be extraditable the offense must be penalized by at least 1 year imprisonment both under Bahrain law and the criminal legislation of the requesting country. In case of conviction, the sentence for the extraditable offence must be at least 6 months imprisonment. Both conditions must be fulfilled in case of conviction. Consequently according to the general rules of the CPC money laundering is an extraditable offence. This is confirmed in Article 11 of DL 4/2001. Extradition can be granted on the submission of an arrest warrant (Article 418.a CPC).

As terrorist financing has not yet been criminalized, no extradition is possible on this ground. Extradition can be granted, however, when the facts can be qualified as aiding and abetting, or other complicity to, extraditable crimes that have happened in a terrorist contest.

<p>Article 415 CPC lists the grounds for refusal, such as the rule that Bahrain does not extradite its own nationals and that it refuses extradition for politically motivated offenses, except in cases in the sphere of regicide and murder with certain aggravated circumstances. Based on Article 2b of the GCC terrorism convention and although not expressly stated in the CPC yet, the political exception does not apply for terrorist (related) offenses.</p> <p>In case of non-extradition, the judicial authorities of Bahrain can take over the prosecution of the suspect according to Article 8 and 9 of the PC. In that case, cooperation on procedure and evidence is a rule, or at least no special problems have been encountered. No such cases have been prosecuted in Bahrain regarding money laundering.</p> <p>Generally an extradition procedure takes priority and within tight time frames, especially in case of detention of the suspect in view of the extradition. In urgent cases direct communication between judicial authorities takes place, even if the extradition request passes through diplomatic channels (Article 417 CPC). An extradition procedure takes on the average some one to two months when the suspect is detained at the request of the foreign authorities. Otherwise the <i>exequatur</i> procedure takes 7 to 10 days. Simplified procedures are also possible with the consent of the suspect waiving formal extradition proceedings, but then under the regime of deportation (<i>persona non grata</i>).</p> <p>Statistical data on extraditions were submitted, without specification however of the offenses grounding the extradition requests. No data were submitted regarding the length of time required to complete the MLA process.</p>		
<p>Recommendations and comments</p> <ul style="list-style-type: none"> • Introduce the offence of financing terrorist activities, terrorist organizations and/or terrorists in criminal law to enable extradition on these specific grounds. • Statistics should detail the extradition grounds and the length of time to complete the MLA process. 		
<p>Compliance with FATF Recommendations</p>		
R.32	Largely compliant	The statistics provided did not specify the extradition grounds.
R.37	Compliant	
R.39	Largely Compliant	The statistics provided did not specify the length of time required to complete the process.
SR.V	Non-Compliant	No extradition possible on FT grounds.
<p>Other Forms of International Cooperation (R.32 & 40, & SR.V)</p>		
<p>Description and analysis</p> <p>Outside the context of MLA, the AMLU can give broad assistance both at FIU and at police cooperation level (Article 8 of DL 4/2001). Police investigative cooperation uses the Interpol channels or is conducted on a direct and bilateral basis. As an FIU, the AMLU does not require a formal agreement or MOU before entering a cooperative relation with a foreign counterpart, and in fact actively exchanges information with its Egmont Group colleagues, both spontaneously or upon request. As a rule the FIU will also spontaneously inform their counterparts whenever the case presents a certain interest for them. The available statistics, however, do not specify the number of such spontaneous referrals. The FIU can use all its investigative powers conveyed by DL 4/2001 in response to a foreign request, including accessing information subject to bank confidentiality. DL 4/2001 allows for enough flexibility to respond speedily and substantially, as no specific restrictions or conditions apply, except that the request should be “reasonable” (Article 9.2 of DL 4/2001) and that for coercive measures the intervention of the judiciary is required (Article 8.2 of DL 4/2001). In practice this has not given rise to any controversy. No requests have been refused yet and for the AMLU it does not matter if, for instance, the case presents fiscal aspects, as long as it can be viewed under the money laundering angle. The AMLU applies the Egmont principles of information exchange, and as such preserves the confidentiality of the information exchanged. No such information is disseminated without the prior consent of the supplying unit, whereas access to this information is strictly protected.</p> <p>The FIU is allowed to exchange general information with foreign “competent authorities” (Article 9.1 of DL 4/2001), which is broader than counterpart FIUs or police agencies, and also encompasses other foreign</p>		

authorities that are involved in the anti-money laundering or terrorist financing effort, such as central banks and supervisors.		
Recommendations and comments		
<ul style="list-style-type: none"> The FIU statistics should also include spontaneous referrals. 		
Compliance with FATF Recommendations		
R.32	Largely compliant	Minor lacuna in FIU statistics as to spontaneous referrals
R.40	Compliant	
SR.V	Compliant	No restrictions regarding gathering information on FT.

Other Issues

Table 2. 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)]

Forty Recommendations	Rating	Summary of factors underlying rating
Legal systems		
1. ML offence	PC	ML scope is not fully consistent with Vienna and Palermo Conventions; financing of terrorism is not a predicate offence to ML; legal documents or instruments, in electronic or digital form, evidencing title are not specifically part of definition of property.
2. ML offence—mental element and corporate liability	LC	Extend corporate criminal liability to ancillary offenses in Articles 2.6 and 3.5
3. Confiscation and provisional measures	PC	No confiscation in terrorist financing cases. Efficiency may be needlessly affected by both misinterpretation of condition to confiscation and lack of clear delineation of the corporate criminal liability concept.
Preventive measures		
4. Secrecy laws consistent with the Recommendations	LC	No on-site inspections have been completed for insurance or capital markets licensees.
5. Customer due diligence	PC	CDD regulations must be enhanced for capital markets licensees and implementation efforts must be in place, particularly for insurance and capital markets licensees.
6. Politically exposed persons	PC	Requirements for PEPs must be in place for all financial institutions; currently only banks, and insurance companies, on the basis the rulebook issued in May 2005, are covered. There are no requirements for capital markets licensees to check for PEPs.
7. Correspondent banking	LC	Requirements to assess CFT controls should be put in place.
8. New technologies & non face-to-face business	PC	Measures to deter ML/FT threats arising from new technologies must be put in place and regulations for insurance and capital markets licensees on non-face-to-face account opening must be developed.
9. Third parties and introducers	PC	Capital markets licensees, money changers, and money brokers must be brought under the requirements now in place in the rulebooks for banks and insurance companies.
10. Record keeping	LC	Although the regulation is in place, capital markets licensees and insurance licensees have not been subject to inspection to determine implementation.
11. Unusual transactions	PC	Requirements must be established for capital

		markets licensees, money changers and money brokers. All financial institutions should be expected to examine the specified transactions and put their findings in writing.
12. DNFBP–R.5, 6, 8-11	PC	There are a number of deficiencies related to CDD and record keeping measures. There is no uniform understanding by lawyers that they need to identify and verify the identity of their clients and keep client identification for all clients for a minimum of five years after the termination of the client relationship.
13. Suspicious transaction reporting	PC	Implementation efforts must be strengthened, greater awareness of the need to report is necessary for the capital markets and insurance licensees.
14. Protection & no tipping-off	LC	The immunity provision does not require good faith.
15. Internal controls, compliance & audit	PC	Requirements for FT training and subsequent implementation for all financial institutions are necessary. High hiring standards must be a requirement of the capital markets licensees.
16. DNFBP–R.13-15 & 21	PC	DNFBPs appear to have little knowledge of their obligation to send STRs to the AMLU. Law and some regulation in place but no clear understanding by lawyers of their obligation to file.
17. Sanctions	LC	There is no coordination between criminal and administrative sanctioning and no corporate criminal liability provided for DL 4/2001 infringements.
18. Shell banks	C	
19. Other forms of reporting	C	
20. Other NFBP & secure transaction techniques	PC	Weaknesses relate to the absence of provisions in respect of the threat posed by new technologies and the provisions of MO 7/2001.
21. Special attention for higher risk countries	PC	More detail must be specified for capital markets licensees. On-site inspections must be performed for capital markets and insurance licensees. Counter-measures must be established in the regulation.
22. Foreign branches & subsidiaries	LC	Requirement of all licensees to inform the BMA if one of their foreign branches or subsidiaries is unable to apply the AML/CFT regulations.
23. Regulation, supervision and monitoring	PC	No inspections have been undertaken on the insurance or capital markets licensees. Capital markets licensees must be subject to the same rigorous Fit & Proper criteria as other BMA licensees.
24. DNFBP - regulation, supervision and monitoring	NC	No legal arrangements in place for DNFBPs and regulatory arrangements for existing DNFBPs are unsatisfactory.
25. Guidelines & Feedback	LC	Capital markets regulations on AML/CFT must be enhanced to meet international standards. The AMLU should contribute actively to the awareness raising of the entities that are deficient in complying with their reporting duties.

Institutional and other measures		
26. The FIU	LC	No guidance on filing STRs has been issued by the FIU.
27. Law enforcement authorities	LC	<i>De facto</i> investigation of FT offenses. No formal regulation for postponing or waiving seizure.
28. Powers of competent authorities	PC	No autonomous or predicate FT offence as legal basis for investigative/compulsory measures.
29. Supervisors	C	
30. Resources, integrity and training	LC	Additional resources are needed in many areas including the BMA and the Public Prosecutors office.
31. National co-operation	PC	No gateways between law enforcement and supervisory for mutual assistance. Greater need for coordination and cooperation between ministries.
32. Statistics	PC	No information on the amount of criminal proceeds seized and confiscated. Overall, effectiveness of systems should be reviewed.
33. Legal persons–beneficial owners	LC	The capital markets regulations are too weak to be effective.
34. Legal arrangements – beneficial owners	NA	No trust law or instruments in Bahrain.
International Cooperation		
35. Conventions	PC	Implement the International Convention for the Suppression of the Financing of Terrorism and confirm full implementation of the Palermo Convention with regard to criminalizing organizations of a criminal nature.
36. Mutual legal assistance (MLA)	LC	No statistics received on MLA so efficiency could not be properly assessed.
37. Dual criminality	C	
38. MLA on confiscation and freezing	LC	No asset forfeiture fund considered.
39. Extradition	LC	The statistics provided did not specify the length of time required to complete the process.
40. Other forms of co-operation	C	
Nine Special Recommendations	Rating	Summary of factors underlying rating
SR.I Implement UN instruments	PC	Implement the International Convention for the Suppression of the Financing of Terrorism.
SR.II Criminalize terrorist financing	NC	FT is not criminalized.
SR.III Freeze and confiscate terrorist assets	PC	FT is not criminalized; no designated agency who can make a prompt determination that is binding on the Kingdom of Bahrain.
SR.IV Suspicious transaction reporting	PC	No obligation to report FT related STRs for capital markets, money changers, and money broker licensees.
SR.V International cooperation	LC	No FT offence, so no extradition possible. No statistics received on MLA so efficiency could not be properly assessed.
SR.VI AML requirements for money/value transfer services	C	
SR.VII Wire transfer rules	C	
SR.VIII Nonprofit organizations	PC	MSA has undertaken a review of the legal and regulatory framework for NPOs and has

		implemented a number of changes to address vulnerabilities in respect of the financing of terrorism. However, at the time of the mission, MSA did not have an effective framework for assessing compliance with these legal and regulatory requirements.
SR.IX Cash Couriers	NC	A declaration or disclosure system and full regulation of the Customs' powers of interception has not been put in effect.

Table 3: Recommended Action Plan to Improve the AML/CFT System

FATF 40+9 Recommendations	Recommended Action (listed in order of priority)
1. General	
2. Legal System and Related Institutional Measures	
Criminalization of Money Laundering (R.1 & 2)	<ul style="list-style-type: none"> • Criminalize the financing of terrorism so that it becomes a predicate offence for money laundering. • Extend corporate criminal liability to infringements of the AML requirements penalized by Articles 2.6 and 3.5 DL 4/2001. • Criminalize other predicate crimes, such as market manipulation, inside dealing, product piracy, and piracy (on the seas). • Specifically add legal documents or instruments, in electronic or digital form, evidencing title to the definition of property, particularly as Bahrain is a financial center. • Specifically add use or conversion of property to the definition of activity of money laundering.
Criminalization of Terrorist Financing (SR.II)	<ul style="list-style-type: none"> • Enact proposed legislative amendments on criminalizing terrorist financing, particularly for the case of financing terrorist organizations or terrorists who have not committed a specific terrorist act. • Form a drafting sub committee of the AML Policy Committee who can coordinate drafting of all relevant AML/CFT laws with the Legal Affairs Directorate of the Cabinet Office before the bills are submitted to the parliamentary process.
Confiscation, freezing and seizing of proceeds of crime (R.3)	<ul style="list-style-type: none"> • Criminalize corporate liability in the Penal Code and clearly state to which bodies corporate criminal liability applies. • Beside the lacuna created by the absence of an autonomous or predicate FT offence, the seizure and confiscation regime is quite comprehensive but would benefit from certain improvements • Amend Article 64, par.2 PC in respect of the condition of the property (not) belonging to the accused.
Freezing of funds used for terrorist financing (SR.III)	<ul style="list-style-type: none"> • Criminalize the financing of terrorism. • Designate a committee or agency to be the 1373 designation agency who can make a prompt and binding determination regarding terrorist targets designated by other countries. • Have systems in place whereby notification of such a designation can be disseminated to all parties who may be holding terrorist funds or assets so that such funds or assets can be frozen without delay.
The Financial Intelligence Unit and its functions (R.26, 30 & 32)	<ul style="list-style-type: none"> • The FIU should periodically review the effectiveness of its systems to combat ML and FT. • The FIU should issue guidance on filing STRs to raise awareness and to ensure consistent understanding of its role in the AML/CFT framework.

<p>Law enforcement, prosecution and other competent authorities (R.27, 28, 30 & 32)</p>	<ul style="list-style-type: none"> • Introduce an autonomous and predicate FT offence required to complete the AML/CFT regime. • Formally regulate the conditions and modalities for postponing or waiving seizure. • Create jurisprudence that will give direction to law enforcement regarding achieving efficiency in terms of convictions and asset recovery. • Reinforce the human resources of the Public Prosecutor’s Office in the expectation of increased demands related to AML/CFT and the specialization of the prosecution. • Keep statistics on the amount of criminal proceeds seized and confiscated. • Review the effectiveness of the evidence gathering process regarding anti-money laundering. • More cases have to be submitted to the courts, not limited to local events but particularly those with an international connotation where the assets appear in Bahrain but the predicate activity occurred outside the national territory. The ensuing jurisprudence will show if prosecution of ML as an autonomous offence, separated from its predicate criminality, stands a real chance for positive results.
<p>Cash couriers (SR IX)</p>	<ul style="list-style-type: none"> • Develop a disclosure or declaration system for the Bahrain borders. This is being envisaged in Article 5bis of the draft amended AML law. • Address the legal basis of the Customs interception of large cash amounts, which is open to challenge • Consider adding a legal provision to the amendments planned for DL 4/2001 regarding false declarations/disclosures and lack of declarations/disclosures under the proposed disclosure system.
<p>3. Preventive Measures–Financial Institutions</p>	
<p>Risk of money laundering or terrorist financing</p>	
<p>Customer due diligence, including enhanced or reduced measures (R.5 to 8)</p>	<ul style="list-style-type: none"> • Banks and insurance companies must implement the regulatory requirements introduced in the new rulebooks. • The BMA must verify implementation efforts related to the new rulebooks through continued (in the case of banks) and new (insurance) on-site inspection programs. • PEP requirements should be included in regulations for capital markets licensees, as well as money changers and money brokers. • Regulations for capital markets must be enhanced to meet the CDD requirements of FATF, as well as meeting the same comprehensiveness standards as applied to other financial sector licensees by the BMA. • Language should be added in the regulations to ensure that financial institutions pay attention to ML/FT risks arising from new technologies. • CDD requirements for non-face-to-face account opening

	<p>should be established for capital markets licensees, unless this type of account opening is specifically prohibited.</p> <ul style="list-style-type: none"> • FC 2 should be reviewed and updated to address TF concerns, particularly paragraphs 2.2.1(d), 2.2.1(g), 2.2.2(a), and 2.2.3.
Third parties and introduced business (R.9)	<ul style="list-style-type: none"> • Clarification is required as to the exact circumstances under which a capital markets licensee, such as a broker, could rely on an introducer. • The regulations should specify that consideration will be given to the country where the introducer is based and whether that country abides by the FATF recommendations.
Financial institution secrecy or confidentiality (R.4)	<ul style="list-style-type: none"> • Conduct on-site inspections of insurance and capital markets licensees to confirm that there is no bank secrecy in place in practice with regard to accessing information from financial institutions pursuant to their responsibility under the requirements of DL 4/2001.
Record keeping and wire transfer rules (R.10 & SR.VII)	<ul style="list-style-type: none"> • Implementation of the recordkeeping requirement should be verified for capital markets and insurance licensees through on-site inspection.
Monitoring of transactions and relationships (R.11 & 21)	<ul style="list-style-type: none"> • Requirements should be established for money changers, and money brokers to ensure that due attention is given to unusual, large or complex transactions. • Capital markets, money changes, and money broker licensees should also be required to ensure that the background of large, complex or unusual transactions, including those coming from other countries are reviewed and the that findings of those reviews are put in writing and for money changers and money brokers maintained in the financial institution's records for five years. • Counter-measures should be established for those situations involving transactions with jurisdictions that do not adequately apply the FATF Recommendations. • Capital markets licensees should be subject to stronger requirements when dealing with clients or transactions from jurisdictions that do not sufficiently apply the FATF recommendations. The BMA must also develop a mechanism to inform the capital markets licensees of the jurisdictions where greater caution should be considered.
Suspicious transaction reports and other reporting (R.13-14, 19, 25 & SR.IV)	<ul style="list-style-type: none"> • STR reporting should be clarified for capital markets licensees in two important ways: it should be made clear that all reports go to both the AMLU and the BMA; and reporting should be for both ML and FT suspicions. • The requirements for money changers and money brokers should be brought up-to-date to make clear when a report must be filed (i.e., not based on a list of examples provided by the BMA). • The BMA should assess the level of awareness and understanding of STR requirements within the capital markets and insurance licensees, given that these two groups

	<p>have never filed an STR.</p> <ul style="list-style-type: none"> • The AMLU should also work to raise awareness within the capital markets and insurance licensees regarding STR reporting, and consider applying sanctions for willful non-compliance. • The rate of forwarded cases to the Public Prosecutor should increase, irrespective of the predicate criminality being identified or not, if only to create the jurisprudence necessary to give direction to the investigations and clarify the evidentiary requirements. • The introduction of a formal predicate or autonomous FT offence is required to create the necessary legal context for related STRs. • The definition of suspicious transaction must be made a uniform one. • The immunity clause for reporting to the appropriate authorities should carry the condition of good faith. • There must be a formal and express obligation to report attempted transactions for financial institutions (excluding banks, which are already covered). • STRs should, whenever reasonably possible, be submitted to the FIU before the transaction is executed, to enable immediate law enforcement intervention.
<p>Internal controls, compliance, audit and foreign branches (R.15 & 22)</p>	<ul style="list-style-type: none"> • MLRO for capital markets licensees should be required to monitor transactions, unless that responsibility is specifically assigned to another individual. • The BMA should ensure that audit, training, and internal controls for capital markets licensees, money changers and money brokers encompass FT, as well as ML. • Capital markets licensees with foreign branches or subsidiaries should be required to inform the BMA when local requirements abroad prohibit them from implementing the BMA regulatory requirements. Implementation of this requirement for insurance companies should be verified through on-site inspection.
<p>Shell banks (R.18)</p>	
<p>The supervisory and oversight system—competent authorities and SROs (R. 17, 23, 29 & 30).</p>	<ul style="list-style-type: none"> • Extend corporate criminal liability to infringements of the AML requirements penalized by Articles 2.6 and 3.5 of DL 4/2001 • Inspections must be undertaken on the capital markets and insurance licensees. • Existing BMA resources, particularly human resources, need to be enhanced to meet its responsibilities as a consolidated supervisor. In particular, expertise in insurance and capital markets should be added to the Compliance Unit for the on-site inspection program. • Clarify or redraft Article 8.2 of MO 7/2001 to specify that the prohibition relates to information concerning the disclosure and the intervention of the FIU. • Establish clear rules and appropriate coordination regarding the criteria to either apply administrative sanctions or criminal penalties.

AML/CFT Guidelines (R.25)	<ul style="list-style-type: none"> The BMA should address the regulatory weaknesses identified in the assessment, particularly those related to capital markets licensees, since there are no current plans to enhance the existing regulatory framework for AML/CFT for those licensees.
Ongoing supervision and monitoring (R.23, 29 & 32)	<ul style="list-style-type: none"> The BMA should move forward rapidly with its plans to inspect insurance and capital markets licensees for AML/CFT.
4. Preventive Measures– Nonfinancial Businesses and Professions	
Customer due diligence and record-keeping (R.12)	<ul style="list-style-type: none"> The exemptions from customer identification requirements in Article 4 of MO 23/2002 and Article 7 of MO 7/2001 should be reviewed to make them consistent with the FATF recommendations, particularly Recommendation 9. The requirements in respect of beneficial ownership, PEPs, understanding the nature of a customer’s business, introduced business and companies that have nominee shareholders or shares in bearer form should be addressed in law regulation or other enforceable means. The guidelines on measures to be employed for PEPs should be strengthened to require that registered persons establish systems to identify customers as PEPs and that the activity of such persons be subject to enhanced monitoring. Provision should be made for persons to undertake CDD measures when there is a suspicion of ML or FT or where there are doubts about the veracity of CDD information previously obtained. Persons should be required to adopt measures to prevent the misuse of technological developments in ML or FT schemes. Persons should be required to consider filing an STR in circumstances where they are unable to complete CDD measures in respect of a customer. Provision should be made for persons to undertake on-going scrutiny of transactions during the course of a relationship to ensure that transactions are consistent with the institutions knowledge of the customer. MOIC should reinforce with all DNFBPS that the requirements for the retention of customer identification records are those found in DL 4/2001 and not MO 23/2002. MOIC should intensify its program of inspections to verify compliance with AML requirements. Lawyers should be trained on the application of the DL 4/2001 to their practice of law. Lawyers should keep client identification records on all their clients pursuant to the DL 4/2001 requirements. MOIC or Ministry of Justice should issue MO for lawyers regarding CDD and record keeping
Monitoring of transactions and relationships (R.12 & 16)	<ul style="list-style-type: none"> MOIC needs to intensify its efforts to familiarize DNFBPS with the notion of suspicious transactions and the requirements for monitoring customer activity. Registered persons should be required to report attempted

	<p>transactions that are considered to be suspicious.</p> <ul style="list-style-type: none"> • Registered persons should be required to give special attention to business relationships and transaction with persons from or in countries that do not or insufficiently apply the FATF Recommendations. • Where transactions from countries that do not or insufficiently apply the FATF Recommendations have no apparent economic or visible lawful purpose, the background and purpose of such transactions should be examined and written findings should be available to assist competent authorities. • There should be a requirement that records of suspicious transaction activity be maintained for a period of five years. • MOIC and MOJ should develop systems to advise registered persons of countries with weak AML/CFT systems. • MOIC or Ministry of Justice should issue MO to lawyers on above recommendations.
<p>Suspicious transaction reporting (R.16)</p>	<ul style="list-style-type: none"> • MOIC needs to intensify its efforts to familiarize DNFBPs with the requirements for the reporting of suspicious transactions and in particular reinforcing that STRs should be sent to the AMLU. • Ministry of Justice should issue regulations and guidance regarding the clarification of requirements to file STRs and how this requirement can be complied with in the face of legal privilege. • Urgent training for lawyers is required regarding the filing of STRs for suspicious transactions or attempted transactions by their clients. • MO should be issued to lawyers by either the Ministry of Justice or the MOIC regarding STRs; clarification needed on legal privilege and filing STRs. • Ministry of Justice and MOIC should coordinate and decide which Ministry to conduct on site inspections of lawyers.
<p>Internal controls, compliance & audit (R.16)</p>	<ul style="list-style-type: none"> • DNFBPs should be required to undertake audits to assess the effectiveness of their AML systems. • There should be a requirement for compliance officers to have timely access to customer identification information data and other CDD information, transaction records and other relevant information. • There should be a requirement for registered persons to have screening procedures to ensure high standards when hiring employees. • Either the Ministry of Justice or the MOIC should issue a MO mandating on site inspections of lawyers. • Coordination between the Ministry of Justice and Ministry of Industry and Commerce to determine who is best suited to conduct the on site inspections is critical. • On site inspections should be carried out on lawyers to ensure compliance with the requirements of the DL 4/2001. • MO should be issued to lawyers regarding the application of DL 4/2001 to their practices.

Regulation, supervision and monitoring (R.17, 24-25)	<ul style="list-style-type: none"> • For the avoidance of doubt, MOIC should have its supervisory powers in relation to MO23/2002 provided more explicitly in law. It should also ensure that all AML requirements in respect of DNFBPs are addressed through law, regulation or other enforceable means. • MOIC should develop a wider range of sanctions to make the sanction regime more effective. • MOIC and MOJ should agree on a single supervisory arrangement for lawyers as DNFBPs. • MOIC needs to generally intensify its efforts to promote awareness of AML/CFT legislative and regulatory requirements among DNFBPs. • MOIC should consider requesting DNFBPs to return their self-assessment circulars as it could be a useful input as the Ministry tries to establish a risk-based framework for its supervisory responsibility for DNFBPs. • MOIC should amend the certificate signed by compliance officers to include reference to MO 7/2001. • Appropriate civil and administrative sanctions should be created for failure to comply with the DL 4/2001 and any consequent Ministerial Order.
Other designated non-financial businesses and professions (R.20)	<ul style="list-style-type: none"> • Registered persons should be required to pay attention to the threats posed by new technologies.
5. Legal Persons and Arrangements & Nonprofit Organizations	
Legal Persons–Access to beneficial ownership and control information (R.33)	<ul style="list-style-type: none"> • The capital markets regulations should be enhanced with respect to their approach to beneficial ownership. The regulations should mirror the approach taken in the bank rulebooks, which establishes a more robust requirement for licensees to know the beneficial owners of legal persons.
Legal Arrangements–Access to beneficial ownership and control information (R.34)	
Nonprofit organizations (SR.VIII)	<ul style="list-style-type: none"> • In terms of its program to address the potential for the abuse of charities for the financing of terrorism, DDLS should develop a more risk-based approach that focuses on potential vulnerability to this risk. • The BMA should consider revising FC 1.5 of the Financial Crimes module of the rulebook for banks to reflect the provision of Article 85 of RD 21/89 (i.e. that charities are required to obtain the approval of MSA before making a foreign transfer of funds in excess of BD 3,000).
6. National and International Cooperation	
National cooperation and coordination (R.31)	<ul style="list-style-type: none"> • Clear gateways should be created regulating communication between FIU and supervisory, especially in cases of non-compliance. • Policy Committee should take a policy lead on revisions of DL 4/2001 and the Terrorism Law.

	<ul style="list-style-type: none"> • Policy Committee should take a lead in coordination and cooperation matters between ministries. • Appropriate Ministries should coordinate on the issue of inspecting lawyers for AML compliance.
The Conventions and UN Special Resolutions (R.35 & SR.I)	<ul style="list-style-type: none"> • Fully implement the 1999 International Convention on the Suppression of Financing of Terrorism. • Provide legal mechanisms to allow law enforcement to share information regarding AML/CFT and terrorism issues.
Mutual Legal Assistance (R.32, 36-38, SR.V)	<ul style="list-style-type: none"> • Devise arrangements for coordinating seizure and confiscation • Consideration should be given to the utility of creating an asset forfeiture fund. • Statistics should be kept on the MLA requests (investigation, seizure and confiscation) pertaining to ML and predicate offenses in order to periodically review the efficiency of the system.
Extradition (R.32, 37 & 39, & SR.V)	<ul style="list-style-type: none"> • Introduce the offence of financing terrorist activities, terrorist organizations and/or terrorists in criminal law to enable extradition on these specific grounds. • Statistics should detail the extradition grounds and the length of time to complete the MLA process.
Other Forms of Cooperation (R.32 & 40, & SR.V)	<ul style="list-style-type: none"> • The FIU statistics should also include spontaneous referrals.

Authorities' Response to the Assessment

The government of Bahrain welcomes the acknowledgement in the report that AML/CFT issues are taken very seriously in the Kingdom and that authorities have worked hard over the past few years to implement an extensive AML framework. The report notes that virtually all the major concerns expressed in the last evaluation, conducted in 2000, have since been addressed. Similarly, the Government of Bahrain will address the areas identified for further improvement in this assessment, as part of its efforts to ensure an AML/CFT regime that is compliant with evolving international standards.

Amongst other things, with respect to the *legal system and related institutional measures*, the Government of Bahrain will review the proposed changes to the draft anti-terrorist financing law, which is currently before parliament. In the meantime, CFT efforts will continue, based on existing legal powers. The government is also in the process of strengthening the role and membership of its national policy committee, in order to enhance coordination between relevant ministries and other agencies involved in AML/CFT efforts. This is likely also to include formally tasking the committee as the UNSCR 1373 designation agency. The range of relevant statistics collected will be developed, and on-going efforts to implement a declaration system in line with Special Recommendation IX will be finalized.

As regards *preventive measures for financial institutions*, work to update regulations in line with the revised FATF 40 Recommendations will be completed by the end of 2005, with remaining licensees brought up to the same standards as those applied to banking and insurance licensees. Capital market licensees (i.e. stock exchange brokers) will be brought into the BMA Rulebook structure, and their existing AML requirements upgraded in line with the recommendations. Since the assessment was undertaken, focused AML/CFT on-site examinations of capital market licensees have started, and will be extended to insurers from September 2005 onwards.

With regards to *preventive measures for non-financial businesses and professions*, the Ministry of Industry and Commerce will address all the issues raised in the report, including amending legislation to make its powers to enforce AML/CFT measures explicit - even though the Ministry is of the opinion that its existing enforcement powers are sufficient in this respect. As regards *non-profit organizations*, the Ministry of Social Affairs has already increased budgeting to recruit additional staff, and will be working to implement effective on-site examination of NPOs. Lastly, as regards *national and international cooperation*, clearer legal gateways for the exchange of information at the domestic level, between supervisory and law enforcement agencies, will be developed.

Annex 1

Authorities and Organizations Met on Mission

Anti-Money Laundering Policy Committee

Anti-Money Laundering Unit (FIU)

Bahrain Investors Centre

Bahrain Monetary Agency

Bahrain Stock Exchange

Bankers' Society of Bahrain

Customs Directorate

Directorate of Legal Affairs

Ministry of Finance

Ministry of Foreign Affairs

Ministry of Industry and Commerce

Ministry of Justice

Ministry of Social Affairs

National Security Agency

Office of the Public Prosecutor

Private Sector Institutions including:

- Accountants
- Financial Institutions (multiple)
- Jewelers
- Lawyers
- Real Estate Agencies

Annex 2

Bahrain Laws and Regulations Reviewed

The Constitution of Bahrain, 2002

Criminal Procedure Code of 1966 as amended

Decree law 1/1961 Commercial Registration Law

Decree 21/1973—Agreement on Extradition Amongst The Arab League Member States

Decree Law 23/1973 as amended—The Bahrain Monetary Agency Law

Decree Law 15/1976—The Penal Code

Decree 17/1983—Agreement of the Arab Organization of Social Defense Against Crime

Decree Law 4//1987—The Bahrain Stock Exchange Law

Decree Law 7/1987— Law of Commerce (as amended)

Decree Law 7/1987 as amended by Decree Law 35 /1996—The Insurance Companies and Organizations Law

Decree 10/1989—Judicial and Legal Cooperation Agreement with the Arab Republic of Egypt

Decree Law 17/1989—Concerning the Ratification of the United Nations Convention against Illicit Traffic in Narcotic Drugs and Psychotropic Substances.

Regulatory Decree No. 21/1989—Concerning the Issuance of a Law on Social and Cultural Societies and Clubs and Private Organizations Working in the Field of Sports and Youth and Private Establishments.

Regulation No. (1) of 1994 Concerning the Money Changing Business

Decree 3/1998—Judicial Cooperation Agreement on Commercial Materials and Civil and Personal Status with Morocco

Regulatory Decree 15/1998—Concerning the Ratification of the Arab Convention on Terrorism and Abatement

Decree 41/1999—Riyadh Agreement for Judicial Cooperation

Decree Law 4/2001—With Respect to the Prevention and Prohibition of the Laundering of Money

Ministerial Order 5/2001—With Respect to the Formation of a Committee to Draw-up Policies for the Prohibition and Combating of Money Laundering

Ministerial Order 7/2001—With Respect to the Obligations Governing Institutions Concerning the Prohibition and Combating of Money Laundering

Decree Law 21/2001—Commercial Companies Law

Decree 30/2001—Judicial and Legal Cooperation Agreement

Ministerial Order 102/2001—Establishing the Enforcement Unit Charged with the Implementation of Decree Law No. 4 of 2001 with Respect to Prevention and Prohibition of the Laundering of Money

Ministerial Order 18/2002 With Respect to Determining the Powers of the Enforcement Unit in Applying the Provision of Decree Law (4) of 2001 With Respect to the Prevention and Prohibition of the Laundering of Money.

Decree No. 14 of 2002—With respect to the Setting-up of a National Security Body

Decree Law 21/2002—Amending Some of the Provisions of Decree No. (4) of 1987 Establishing and Regulating the Bahrain Stock Exchange

Ministerial Order 23/2002—With respect to procedures of prohibition of and combating money laundering

Legislative Decree No. 46 of 2002—on Issuing the Code of Criminal Procedure

Decision 16/2003 - Concerning the System of Issuing Donation Collection Licenses for Social and Cultural Societies and Clubs Subject to the Ministry of Labour and Social Affairs for Charity Societies

Resolution 1/ 2004—Directives Relative to the Prevention & Prohibition of Money Laundering at the Bahrain Stock Exchange

Ministerial Order 3/2004—With Respect to Control Over Activities of Private Organizations

Decree Law 4/2004—With Respect to the Accession by Bahrain to the United Nations Convention against Transnational Organized Crime.

Decree Law 8/2004—With Respect to Approving Accession by Bahrain to the International Convention for the Suppression of the Financing of Terrorism

BMA Rulebook, Volume 1 (conventional banks), Volume 2 (Islamic banks), Volume 3 (insurance) April 2005