

## Fourth Follow-Up Report for the Kingdom of Bahrain

### Application to Move from Follow-Up to Biennial Updating

#### A. Introduction

1. The 4<sup>th</sup> Plenary Meeting adopted the mutual evaluation report (MER) of the Kingdom of Bahrain on 14 November 2006. As a result of the content of that report, Bahrain was under regular follow-up according to the paper on mutual evaluation process procedures. Bahrain submitted its 1<sup>st</sup> follow-up report in May 2009 and its 2<sup>nd</sup> follow-up report in November 2010. The 3<sup>rd</sup> follow-up report was presented by Bahrain in November 2011 to the 14<sup>th</sup> Plenary Meeting where it expressed its hope that the Plenary Meeting examines its desire to exit the regular follow-up process to updating biannually. The Plenary Meeting decided to discuss Bahrain's application to be moved from regular follow-up to biennial updating during the 15<sup>th</sup> Plenary Meeting, but because the report was submitted one month before the Plenary Meeting, it was decided to be discussed in the 16<sup>th</sup> Plenary Meeting.

2. This paper is based on the procedure for removal from the regular follow-up, as agreed by the 12<sup>th</sup> Plenary Meeting in November 2010. The paper contains a detailed description and analysis of the measures taken by Bahrain in respect of the core<sup>1</sup> and key<sup>2</sup> Recommendations rated Non Compliant (NC) and Partially Compliant (PC) in the MER. It also contains a description and analysis of the other Recommendations rated PC or NC. In Annex 1, we are including a list of the major laws and documents relating to AML/CFT regime in the Kingdom of Bahrain. The procedure requires that the Plenary Meeting considers the removal of the country from the regular follow-up if it has, in the opinion of the Plenary Meeting, an effective AML/CFT system in force, under which the country has implemented the core and key recommendations at the level essentially equivalent to a C (Compliant) or LC (Largely Compliant) taking into consideration that there would be no re-rating.

3. Bahrain was rated C and NC on a total of 25 recommendations:

Core Recommendations rated PC or NC
R1, R5, R13, SRII, SRIV
Key Recommendations rated PC or NC
R3, R23, R35, SRI, SRIII
Other Recommendations rated PC
R6, R8, R9, R11, R12, R15, R16, R20, R21, R28, R31, R32, SRVIII
Other Recommendations rated NC
R24, SRIX

<sup>1</sup> The core Recommendations as defined in the FATF procedures are: R1, R5, R10, R13, SRII and SRIV.

<sup>2</sup> The key Recommendations as defined in the FATF procedures are: R3, R4, R23, R26, R35, R36, R40, SRI, SRIII and SRV.

4. As prescribed by the procedures of exiting the regular follow-up, Bahrain provided the Secretariat with a full report on its progress. The Secretariat has drafted a detailed analysis of the progress made by Bahrain for the core and key recommendations rated NC or PC, as well as an analysis of the other Recommendations rated NC or PC.

5. As a general note on all applications for removal from regular follow-up: the procedure is described as a paper based desk review, and by its nature is less detailed and thorough than a mutual evaluation report. The analysis focuses on the Recommendations that were rated NC or PC, which means that only a part of the AML/CFT system is reviewed. Such analysis essentially consists of looking into the main laws, regulations and other material to verify the technical compliance of domestic legislation with the FATF standards. In assessing whether sufficient progress had been made, effectiveness is taken into account to the extent possible in a paper based desk review and primarily through a consideration of data provided by the country. Any conclusions in this report do not prejudge the results of the future assessments, as they are based on information which was not verified through an on-site process and was not as comprehensive as would exist during a mutual evaluation.

## **B. Main conclusion and recommendations to the Plenary**

### *Core Recommendations*

6. **R1 (Criminalization of money laundering):** Deficiencies relating to this recommendation were addressed with regard to the criminalization of some acts mentioned in the glossary of designated classifications of predicate offences, which were not criminalized at the time of conducting the mutual evaluation process. It is noted that Bahrain adopted the wider range approach in designating the predicate offence including the crimes of terrorist financing, insider trading and market manipulation, piracy of products and piracy. Additionally, four convictions were made in money laundering crimes.

7. **R5 (Customer due diligence):** Deficiencies relating to due diligence measures in financial institutions were addressed with regard to technical aspect by amending and publishing rulebooks issued by the Central Bank of Bahrain. These rulebooks set out in detail the requirements for the identification and verifications of customers and beneficial owners. However, it should be noted that part of the deficiencies mentioned in the MER is related to the effectiveness of application of the necessary measures, which cannot be verified without doubt through offsite review of the available information.

8. **R13 and SR4 (Suspicious transaction reporting):** The rulebooks issued by the Central Bank of Bahrain fulfilled the requirements of reporting transactions suspected of being

associated to ML/TF. Statistics also show that there is gradual increase in reporting rates. However, the contribution of insurance companies and capital market institutions remain relatively limited in this aspect in comparison to the number of these institutions in the Bahraini financial sector.

9. **SR2 (Criminalization of terrorist financing):** Bahrain addressed most deficiencies in this recommendation as terrorist financing was criminalized through the legislative amendment in Law no. (54) of 2006. This criminalization was largely in line with the Terrorist Financing Convention as it included forms of collecting and providing funds to be used in a terrorist act or by a terrorist organization or group or one of their affiliates. Therefore, it is worth mentioning the occurrence of the condition of affiliation with a terrorist gang or organization with regard to the terrorist. A judgment on terrorist financing was passed in 2011.

10. As a general result, it can be said that the level of compliance of Bahrain in these Core Recommendations can be rated as equivalent to LC.

#### *Key Recommendations*

11. **R3 (Confiscation and provisional measures):** Bahrain addressed the deficiencies in this recommendation as the sanction of confiscation for terrorist financing crime was stipulated with regard to the natural and legal person.

12. **R23 (Control and Supervision):** The Secretariat viewed forms of inspection reports prepared by inspectors from the Central Bank of Bahrain. They show follow up on compliance of the financial institutions with implementing the requirements imposed on them by virtue of the AML/CFT Law and the Financial Crimes Module of the CBB Rulebooks. They also show the occurrence of some violations by these institutions. On the other hand, disciplinary sanctions were imposed on some institutions as the authorities reported for violating their obligations in this field. In addition, the authorities informed that the number of specialized inspectors in the AML/CFT field increased to 12 inspectors (knowing that the number of FIs in Bahrain exceeds 400 institutions). The authorities informed that they conduct onsite inspection on 30 FIs annually, but the FIs are required to submit annual reports to the Central Bank showing the extent of their compliance with laws and legislations related to AML/CFT to be prepared by external auditors. The authorities informed that they conduct onsite inspection based on a risk-based approach relying on reports of the external auditors.

13. **R35 (Conventions):** Bahrain stipulated the implementation of international conventions by virtue of the legislative provision mentioned in Law no. (54) of 2006 including the United Nations International Convention for the Suppression of the Financing of Terrorism and Palermo Convention, but the deficiencies set out with regard to the terrorist financing crime could affect compliance with this recommendation.

14. **SR1 (Implementation of UN instruments):** Bahrain addressed deficiencies relating to this recommendation by implementing the Terrorist Financing Convention. However, deficiencies mentioned with regard to the terrorist financing crime could affect compliance with this recommendation.

15. **SR3 (Freezing and confiscating terrorist assets):** Deficiencies relating to this recommendation were addressed through the establishment of a committee to follow up on the execution of the Security Council resolutions.

#### ***Other Recommendations***

16. Bahrain addressed a large part of the deficiencies relating to other recommendations. It is noteworthy that making the decision for the removal of Bahrain from the follow-up process is primarily based on the core and key recommendations. This report does not provide a detailed analysis with regard to other recommendations.

#### ***Conclusion***

17. The follow-up procedures indicate that, for a country to have taken sufficient action to be considered for removal from the process, it must have an effective AML/CFT system in force, under which it has implemented the core and key recommendations at a level essentially equivalent to C or LC, taking into account that there would be no re-rating. The Plenary does, however, retain some flexibility with regard to the key recommendations if substantial progress has also been made on the overall set of Recommendations that have been rated PC or NC.

18. With regard to core Recommendations, it can be said that the level of compliance of Bahrain on these recommendations can be rated at a level equivalent to LC, at a minimum.

19. With regard to key Recommendations, it can be said that the level of compliance of Bahrain on the overall Recommendations can be rated at a level equivalent to LC.

20. With regard to other recommendations where Bahrain was rated NC or PC, it can be said that the level of compliance of Bahrain on these recommendations is generally equivalent to a level of LC, at a minimum.

21. With regard to effectiveness, Bahrain issued 4 convictions in money laundering and a conviction in terrorist financing. With regard to STRs, statistics show that there is increase in the levels of reporting by various institutions and entities but it is limited with regard to some sectors (insurance and stock) Moreover, the available data does not show the number of reports related to terrorist financing. Additionally, it is hard to verify the effectiveness of supervision on DNFBPs.

22. As a result, since the level of compliance of Bahrain with the core Recommendations is rated at a level equivalent to LC at a minimum and the level of compliance with the key Recommendations is rated at a level equivalent to LC at a minimum, the Plenary Meeting may decide to approve Bahrain's application to be removed from the follow-up process to biennial updating.

### **C. Overview of the development of the Kingdom of Bahrain**

#### *Overview of the main changes since the adoption of the MER*

23. Since the adoption of the MER, the Kingdom of Bahrain has focused on amending Law no. (4) of 2001 to correct deficiencies indicated in the MER.

#### ***The legal and regulatory framework:***

24. The AML/CFT regime in Bahrain is based on Law no. (4) of 2001 on the prohibition and combating of money laundering to which Bahrain introduced some amendments in 2006<sup>3</sup> with regard to the criminalization of the act of terrorist financing and adopting the disclosure system for the cross-border transportation of cash. It is noteworthy that Bahrain has also passed a law on protection society from terrorist acts<sup>4</sup>. The law includes an intensification of the penalty for money laundering crimes<sup>5</sup> if the crime is committed on purpose to execute a terrorist purpose. It is worth mentioning that a committee was formed to develop AML/CFT policies in December 2005 headed by the Central Bank of Bahrain and the committee has been re-formed recently where members represent persons of high administrative positions.

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<sup>3</sup> The decree in Law no. 54 of 2006 amending some of the provisions of the decree in Law no. 4 of 2001 with the prohibition and combating of money laundering.

<sup>4</sup> Law no. 58 of 2006 with regard to protection of society against terrorist acts passed on 12 August 2006.

<sup>5</sup> Article 2 Clause 9 of Law no. 58 of 2006 with regard to protection of society against terrorist acts.

25. Moreover, the Central Bank of Bahrain issued and amended rulebooks issued for various FIs which set out in detail the obligations of these institutions in the AML/CFT field.

- Rulebook no. (1) for conventional banks (issued in 2005 and amended several times last of which in 2012);
- Rulebook no. (2) for Islamic banks (issued in 2005 and amended several times last of which in 2012);
- Rulebook no. (3) for the insurance sector (issued in 2005 and amended several times last of which in 2012);
- Rulebook no. (4) for investment companies (issued in 2006 and amended several times last of which in 2012);
- Rulebook no. (5) for specialized licensees (issued in 2010 and amended several times last of which in 2012);
- Rulebook no. (6) for capital markets (issued in 2010 and amended several times last of which in 2011).

26. The Minister of Justice and Islamic Affairs issued the Ministerial Decree no. (2) of 2008 in March 2008 on obligations with regard to procedures of prohibition and combating of money laundering in the law profession and foreign law firms. Moreover, the Minister of Industry and Commerce issued Decree no. (126) of 2011 then Decree no. (6) amending the former decree in 2012 with regard to application of AML/CFT requirements by institutions affiliated with the Ministry.

27. It is worth mentioning that the Kingdom of Bahrain revised the AML Law in November 2010 and drafted a bill to amend the law. The bill includes an amendment relating to the approach followed with regard to predicate offences by adding a list of these offences. The Bahraini authorities informed that the amendment bill was raised to the Cabinet which approved the bill. It was raised to the Shura Council and the Council of Representatives in February 2012 in preparation to be passed by His Majesty the King.

## D. Review of the measures taken in relation to the Core Recommendations

### Recommendation 1 – Rating (PC)

*RI: Deficiency 1:* The scope of money laundering does not fully conform to Vienna and Palermo Conventions. Terrorist Financing is not considered a predicate offence of money laundering.

28. Article (2) of the decree in law no. (4) of 2011 on the prohibition and combating of money laundering indicated that a person shall be considered a perpetrator of money laundering crime if he: (a) conducts any operation related to crime proceeds ..., (b) conceals the nature, source, or location of proceeds ... (c) acquires, receives or moves ... (d) keeps or possesses the crime proceeds ... The evaluation team considered that the indicated forms of money laundering do not fully comply with the provisions of Vienna and Palermo Conventions since the use or conversion of property is not considered a form of money laundering. But the report indicated that the confusion occurred through the translation of the law into English. The report indicated that after discussions with the Ministry of Justice, the team agreed to deem the law inclusive of the form of conversion based on the fact that the phrase “Conducting any operation” refers to a wide notion in Arabic. It is noteworthy that the law itself explicitly refers to that in Article (1) as “operation” is defined as any disposition of funds including, for instance: purchase, lending, mortgage, gift, **conversion**, delivery, deposit, withdrawal, transfer between accounts, currency exchange and credit extension.

29. With regard to the scope of predicate offences of money laundering, Bahrain followed, in designating predicate offences, the wide range approach based on considering any activity constituting a crime punishable in Bahrain or any other country a predicate offence of money laundering. But it is noteworthy that regardless of the approach followed in designating predicate offences of money laundering, the State must criminalize, at a minimum, all designated classifications of crimes as identified in the FATF glossary. Therefore, the MER indicated that there are predicate offences that were not criminalized in Bahrain including market manipulation, insider trading, piracy of products and piracy in addition to the terrorist financing crime. But it is worth mentioning that these crimes are considered criminalized acts in Bahrain as Bahrain joined the Convention for the Suppression of Unlawful Acts against the Safety of Maritime Navigation and the Protocol for the Suppression of Unlawful Acts against the Safety of Fixed Platforms Located on the Continental Shelf by virtue of Law no.

(15) of 2005<sup>6</sup>. Law no. (22) of 2006<sup>7</sup> with regard to protection of authors' and neighboring rights also included the criminalization of piracy of products. With regard to the terrorist financing crime, through the legislative amendment that was done on Law no. (4) of 2001 with regard to the prohibition and combating of money laundering by virtue of Law no. (54) of 2006<sup>8</sup>, the terrorist financing act was criminalized. Because Bahrain relied in the approach stating that all crimes are deemed a predicate offence of a money laundering crime as mentioned above, therefore, the terrorist financing act is a predicate offence of money laundering. With regard to transactions of insiders and market manipulation, the Central Bank of Bahrain and Financial Institutions Law no. (64) of 2006<sup>9</sup> included the criminalization of the violation of insider transaction rules and market manipulation. The following table shows method of criminalizing the said acts.

Relevant Articles	The law criminalizing these acts	Predicate offences not previously criminalized
Ratification of the convention	Law no. (15) of 2005	Piracy
Article 65	Law on protection of authors' and neighboring rights no. (22) of 2006	Piracy of products
Articles 97, 98, 167 & 168 Articles 106 & 107	The Central Bank of Bahrain and Financial Institutions Law no. (64) of 2006	Transactions of insiders and market manipulation
Article 2	Law no. (54) of 2006	Terrorist financing

***R1: Deficiency 2: Legal electronic or digital documents and charters proving ownership are not considered part of identification of ownership.***

30. With regard to definition of funds, it includes movable and immovable, tangible and intangible funds, but the MER indicated that this definition does not cover the physical or moral notion and does not particularly cover documents or legal deeds including electronic or digital ones which prove the ownership right. In this case too, the Ministry of Justice informed the evaluation team that the confusion is a result of translation as the law defined funds as "all things of value" in addition to Clause (e) which indicates "anything used in money laundering".

<sup>6</sup> Issued on 4 June 2005.

<sup>7</sup> Issued on 25 June 2006.

<sup>8</sup> Issued on 8 August 2006.

<sup>9</sup> Issued in Law no. (64) on 6 September 2006.

***Effectiveness:***

31. With regard to the application of the AML Law, four convictions were made in this regard with punishment ranging from one to five years in prison and a fine ranging from BHD10,000 to BHD 30,000.

**R5: Rating (PC)**

***R5: Deficiency: Customer identification due diligence systems must be enhanced for the licensees in the capital markets and application efforts must be exerted, in particular with regard to the licensees in the capital markets and licensed insurance companies.***

32. Rulebook (3) issued by the Central Bank of Bahrain underwent several updates since it was issued in May 2005. These updates included correcting the deficiencies included in the rulebook which were mentioned in the MER adopted in October 2006 (at the time of the onsite visit during the second half of April 2005). On the other hand, the Central Bank of Bahrain issued Rulebook (4) for the capital markets (investment companies) in April 2006 which also underwent many updates since then to address the deficiencies mentioned in the MER. In general, it is noticed that the rulebooks issued for all entities subject to supervision of the Central Bank of Bahrain were updated to be largely consistent and to cover all due diligence requirements (and other requirements) in line with international standards.

33. On the other hand, developing and improving the efforts of various FIs including the insurance sector and capital market institutions, with regard to the application of these obligations is extremely unclear, especially that the inspection plans of the bank might not be sufficient to ensure the sufficiency of these efforts (see the below analysis with regard to R23). On the other hand, the FIs are obliged annual reports prepared by external auditors certified by the Central Bank for these institutions on the compliance with AML/CFT requirements. Neither the inspection reports nor the relevant information provided by the Bahraini authorities reflected the presence of any evidence that these reports include major violations in this field.

**R13: Rating (PC)**

***R13: Deficiency: Application efforts must be enhanced. There is also a need to promote more awareness about the need to report suspicious transactions with regard to entities licensed to operate in the capital markets and licensed insurance companies.***

34. By reviewing the requirements in the rulebooks issued for all FIs in Bahrain, it was clear that they cover the reporting requirements with regard to money laundering including cases of attempting to perform transactions. The Bahraini authorities provided statistics on the suspicious transactions reports (STRs) submitted by the FIs during the period from 2009 to June 2012, which show gradual increase in the reporting rates. However, the contribution of insurance companies and capital market institutions remain relatively limited in this aspect in comparison to the number of these institutions in the Bahraini financial sector.

**A table showing the number of STRs over the past four years as per the reporting entity**

2009					
Other	Insurance Companies	Credit Card Companies	Ministry of Industry and Commerce	Foreign Exchange Companies	Banks
4	3	1	4	116	140
268					
2010					
Other	Insurance Companies	Credit Card Companies	Ministry of Industry and Commerce	Foreign Exchange Companies	Banks
-	7	3	4	123	229
366					
2011					
Other	Insurance Companies	Credit Card Companies	Ministry of Industry and Commerce	Foreign Exchange Companies	Banks
-	-	11	-	150	170
331					
Until June 2012					
Other	Insurance Companies	Credit Card Companies	Ministry of Industry and Commerce	Foreign Exchange Companies	Banks
-	3	4	3	130	60
200					

35. On the other hand, the Bahraini authorities informed that the Central Bank of Bahrain holds periodic educational meetings with the compliance officers in the FIs.

**SR2: Rating: (NC)****SR2: Deficiency: Terrorist financing has not been criminalized.**

36. Bahrain criminalized terrorist financing by virtue of the legislative amendment in Law no. (54) of 2006 of the provisions of the decree in Law no. (4) of 2001 with regard to prohibition and combating of money laundering. Article 3 Clause 1 (amended) stipulated the punishment of "any person who collects, gives or allocates property, funds or proceeds of these property or funds for a group, organization, agency or gang performing a terrorist activity having headquarters inside the country or abroad or one of their affiliates or performed any operation for their interest or provided them with support or funds in any way knowing of its performance of terrorist activity". Therefore, the terrorist financing act shall extend to include forms of provision or collection of funds in any way knowingly. This article includes the financing of funds to be used (1) by a group or organization, (2) to perform a terrorist act, (3) by one of the affiliates of the group, organization or gang performing a terrorist act. Therefore, this definition was largely consistent with the features specified in SR2 with exception to non-punishment of the financing of terrorists not affiliated with a group or gang performing terrorist activity. It is noteworthy that the law does not include definitions of the organization or gang except for the definition related to terrorism<sup>10</sup>. It is worth mentioning that Law no. 58 of 2006 in relation to protecting society against terrorist acts includes a definition of terrorism<sup>11</sup> that is not fully compatible with the definition mentioned in the abovementioned Law no. 54.

37. With regard to the definition of funds, the definition set out in the decree in Law no. 4 of 2004 is the applicable one. It stipulates that funds are "all things of value of whatever type, description or nature, movable or immovable, tangible or intangible. They include for

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<sup>10</sup> The definition of terrorism in Law no. 54 stipulated that "each act of violence or threat of violence regardless of motivation or purpose, which is committed in execution of an individual or collective criminal project with the aim to terrify people, causing fear of hurting them or exposing their life, reputation, freedom, security or rights to danger or causing harm to the environment or one of the public or private facilities or properties or occupying or expropriating them or exposing one of the national resources or international facilities to danger or threatening stability, regional safety, political unity or sovereignty of the independent countries without prejudice to the definition of terrorism set out in the Convention of the Organization of the Islamic Conference on Combating International Terrorism or in relevant laws.

<sup>11</sup> Law no. (85) of 2006 with regard to protection of society against terrorist acts stipulated in Article One thereof that terrorism is defined as "the use of force or threat to use it or any other illicit technique that constitutes a crime punishable by law that is used by the offender to execute an individual or collective criminal project with the purpose of disturbing public order or exposing the safety of the Kingdom and its security to danger or harming the national unity or security of the international community if this shall cause harm to people, terrify them and cause them fear and expose their life, freedom or security to danger or causing harm to the environment, public health, national economy or public facilities or property or expropriating them and hinder their performance or preventing and hindering the performance of public authorities, places of worshipping or academic institutes.

instance: Anything used in ... terrorist financing. Therefore, the provision was comprehensive without any limitation.

38. Law no. 54 of 2006 has not stipulated the need for actual use of funds for the terrorist financing crime to apply but was unlimited in this regard. Add to that, the provision has not drawn a link between funds and a certain terrorist act but was unlimited.

39. With regard to attempt, Law no. 54 of 2006 explicitly stipulated the punishment of attempting to commit a terrorist financing crime. With regard to collaboration, Law no. 54 did not mention it, therefore, the Bahraini Penal Law can be referred to in this regard being the general law which designates cases of criminal collaboration in Article 44 therein. By virtue of Article 45, the Bahraini Penal Law punishes collaboration in crimes by the same penalty stipulated for the offender; therefore, collaboration in terrorist financing is punishable in Bahrain.

40. With regard to the terrorist financing crime being a predicate offence of money laundering, it was mentioned above that Bahrain adopted the wide range approach in designating predicate offences, therefore, when criminalizing the terrorist financing act, it is deemed a ML predicate offence.

41. With regard to the application of criteria 2-2 until 2-5 to the terrorist financing crime, Article 253 of the Criminal Trials Law allows inferring the intentional element in committing the crime from the objective factual circumstances. The terrorist financing crime can be applied to legal persons as the amended law stated that in cases where a crime ... and terrorist financing is committed, the legal person, without prejudice to liability of the natural person, shall be punished by a fine ... and confiscation of the funds, subject of the crime.

42. With regard to application of the penal liability in terrorist financing crimes to the legal person, according to the legislative amendment in decree no. (54) of 2006, an amendment was made to Article (3-3) which stipulated that in cases where a ML/TF crime is committed by a legal person, without prejudice to liability of the natural person, the legal person shall be punished by the fine stipulated in this law and the funds, subject of the crime, shall be confiscated. Article (3) Clause 3-1 stipulates the penalty of life imprisonment or imprisonment for a term not less than ten years and a fine not less than BHD100,000 and not exceeding BHD 500,000 for the person committing the terrorist financing crime in addition to the confiscation of funds, subject of the crime, or any funds belonging to the person, their spouse or their minor children that are equal in value to the funds, subject of the crime. It also stipulates the confiscation of these funds and properties in case of lapse of the criminal

lawsuit due to death of the suspect and when his inheritors did not prove the legitimacy of their source. . Therefore, the terrorist financing penalty can be deemed dissuasive and proportionate if compared to the penalties imposed on crimes of terrorist acts.

43. Effectiveness: A conviction was made in 2011 in a terrorist financing case and the person was punished by life imprisonment and confiscation of the seized items.

**SR4: Rating: (PC)**

**SR4: Deficiency: There is no obligation for licensed capital markets, foreign exchange offices and brokerage offices to report suspicious transactions related to terrorist financing.**

44. The rulebooks issued by the Central Bank of Bahrain for all FIs, including licensed capital market companies, foreign exchange offices and brokerage offices, which were updated several times since adoption of the MER, included obligations of reporting suspicious transactions related to terrorist financing according to the SR4 criteria, but the statistics submitted by the authorities have not clarified the number of reports submitted with regard to suspicion of terrorist financing.

**E. Review of the measures taken in relation to the Key Recommendations**

**R3: Rating (PC)**

***R3: Deficiency 1: There is no confiscation in terrorist financing cases.***

45. According to the legislative amendment in Law no. (54) of 2006, an amendment was made to the order of clauses of Article (3) of Law no. (4) of 2001 from clauses (3-1) until (3-7) to become (3-2) until (3-8) respectively. In addition to what was stated in Clause no. (5) of Article (5) (repeated) by adding the phrase (and terrorist financing) after the phrase of money laundering whenever it was mentioned in the law. Therefore, Clause (3-3) of Article (3) stated the penalty of confiscation for the natural person and the confiscation of the funds, subject of the crime or any other funds owned by them, their spouse or their minor children that are equivalent in value to the funds, subject of the crime. It also stipulates the confiscation of such funds and properties in case of lapse of the criminal lawsuit due to death of the suspect and when his/her inheritors did not prove the legitimacy of their source. Article (3-4) has also stipulated that in cases where a ML/TF crime is committed by a legal person, without prejudice to liability of the natural person, the legal person shall be punished by the

fine stipulated in this law as well as the confiscation of funds, subject of the crime. Therefore, the amended law established the penalty of confiscation for the natural and legal person in a terrorist financing crime.

***R3: Deficiency 2: Misinterpretation of the prerequisite for confiscation and absence of clarification of the notion of penal liability of legal persons can impact on effectiveness. No orders of confiscation have been issued so far on cases of money laundering.***

46. The Court in Bahrain had passed confiscation judgments in cases of money laundering, as it ruled by the confiscation of individual accounts.

**R23: Rating (PC)**

***R23: Deficiency: No inspections were done at entities licensed to operate in capital markets and licensed insurance companies. The entities licensed to operate in the capital markets should be subject to accurate adequacy criteria as well as other licensed entities by Bahrain Monetary Agency (BMA).***

47. The Bahraini authorities reported that the Central Bank of Bahrain conducts periodic onsite inspection on companies operating in capital markets and insurance companies, but the authorities have not provided sufficient statistics on the inspections they conducted in each sector separately or their findings in the years following the adoption of the MER. The authorities informed that their onsite inspection plan for each year includes nearly 30 FIs. They also informed that 12 specialized inspectors work in the Central Bank of Bahrain to ensure compliance of the various FIs with the AML/CFT requirements bearing in mind that there is no more than 400 FIs operating in Bahrain across all sectors. On the other hand, the Bahraini authorities informed that in context of monitoring compliance of the FIs with the AML/CFT requirements, they oblige the various FIs to submit annual reports prepared by external auditors on the level of compliance with these requirements according to the requirements of the Financial Crimes Module of the rulebook of the central Bank of Bahrain. The authorities informed that they have not imposed any penalties with regard to any violations identified according to this mechanism or the regular inspection and control mechanism with exception for one case in 2007 where a penalty was imposed on a foreign exchange office. The sanction was a fine in the amount of BHD 20,000 and prevention from transferring money to a certain country. Additionally, the authorities informed that disciplinary measures were taken against some violating institutions by means of official warnings and directions but no statistics were available on these measures.

**R35: Rating (PC)**

**R35: Deficiency: Implementing the International Convention for the Suppression of the Financing of Terrorism and stressing the full implementation of Palermo Convention with regard to criminalizing organizations of criminal nature.**

48. The Terrorist Financing Convention was ratified by virtue of Royal Decree no. 8 of 2004. At the time of evaluation, the ratification was still under execution. It was also ratified by virtue of Law 54 of 2006 with regard to protection of society against terrorist acts by virtue of which terrorist financing was criminalized. It can be said that it complied with the execution of the Convention and it should be noted that the mentioned deficiencies in relation to SR2 can affect the recommendation.

49. With regard to full implementation of Palermo Convention, Bahrain addressed the deficiencies with regard to the ML crime in addition to the possibility of punishing the legal person for a ML crime.

**SR1: Rating (PC)**

**SR1: Implementing the International Convention for the Suppression of the Financing of Terrorism:**

50. The Terrorist Financing Convention was ratified by virtue of Royal Decree no. 8 of 2004. At the time of evaluation, the ratification was still under execution. It was also ratified by virtue of Law 54 of 2006 with regard to protection of society against terrorist acts by virtue of which terrorist financing was criminalized. It can be said that it complied with the execution of the Convention and it should be noted that the mentioned deficiencies in relation to SR2 can affect the recommendation.

**SR3: Rating: (PC)**

**SR3: Deficiency:** Terrorist financing is not criminalized and there is no designated agency that can give fast and binding designation to the Kingdom of Bahrain.

51. The AML/CFT Policy Committee was established by virtue of administrative decision no. (2) of 2007 to follow up on the execution of the Security Council resolutions related to AML/CFT. The Bahraini Cabinet issued its decision no. (05-2153) on 8 April 2012 approving the expansion of competencies of the Committee concerned with following up on compliance of the Kingdom of Bahrain with all SC resolutions which is formed by virtue of decision of the Cabinet no. (08-2122) to also include all matters related to combating terrorism and to re-form the Committee to be chaired by the Ministry of Foreign Affairs and

constituted of members representing the Ministry of Interior, National Security Agency, Ministry of Human Rights and Social Development, Central Bank of Bahrain, Ministry of Justice, Islamic Affairs and Endowments, Customs Affairs, Civil Aviation Affairs and the General Organization of Sea Ports (GOP). The Committee may seek the assistance of any other entity it deems appropriate.

52. The duties of this Committee focus on reviewing and examining all correspondences and requirements of SC resolutions by virtue of chapter seven of the United Nations Charter in relation to AML/CFT including the freezing or confiscation of funds present in the Kingdom of Bahrain or under its disposal in coordination with the relevant Ministries and government bodies as well as directions and recommendations relating to economic crimes and taking the necessary action to execute these requirements. The Committee shall also determine the official stance of the Kingdom of Bahrain with regard to the execution of these resolutions and recommendations issued by the Security Council and handling them in a way that is commensurate with the stance of the Bahraini government in coordination with the entities concerned with the implementation of these resolutions and responding to them via official channels in coordination with the Ministry of Foreign Affairs.

53. It is worth mentioning that the rulebooks directed to the FIs include provisions relating to ensuring that there are no names matching those on the SC lists related to Resolution 1267 and the obligation to inform the Central Bank of that.

54. Effectiveness: The Central Bank of Bahrain froze the account of a Filipino person whose name was found on the lists related to Resolution 1267.

**F. Review of the measures taken in relation to the other Recommendations rated PC or NC.**

**R6:Rating:(PC)**

***R6:Deficiency: There must be conditions in place for the Politically Exposed Persons (PEPs) in all FIs, currently banks and insurance companies only, by virtue of the rules manual in May 2005. There are no conditions in place for the entities licensed to operate in the capital markets to verify the PEPs.***

55. The rulebooks issued by the Central Bank of Bahrain for the FIs fulfilled the requirements of R6 in relation to PEPs including developing risk-based systems to designate this category of clients, obtain information about the source of wealth and funds and obtain

the approval of senior management to establish a business relationship with this category of clients.

**R8: Rating:(PC)**

***R8: Deficiency: Measures must be put in place to prevent ML/TF risks resulting from modern technology. Systems for entities licensed to operate in the capital markets and licensed insurance companies must also be developed for opening indirect accounts.***

56. The rulebooks issued by the Central Bank of Bahrain for various FIs require developing systems for protection against potential risks from exploiting modern technology in ML/TF.

**R9: Rating:(PC)**

***R9: Deficiency: The entities licensed to operate in the capital markets, foreign exchange offices and brokerage offices must be subject to the conditions set out in the guides for banks.***

57. The rulebooks related to capital markets, stock brokers and specialized licensees (including foreign exchange offices) included comprehensive obligations consistent with requirements of R9.

**R11:Rating:(PC)**

**R11: Deficiency: Conditions for entities licensed to operate in the capital markets, exchange offices and brokerage offices must be put in place. It is also expected that FIs examine the designated transactions and note down in writing the conclusions they reached.**

58. The rulebook directed to institutions operating in the capital markets included the obligation to report transactions if suspected of being associated with ML/TF or if they were unusual or suspicious transactions. This obligation covers requirements of R11 partially only as it does not cover large and complex transactions and does not impose the obligation to study these cases sufficiently and maintain the findings of the analysis making them accessible to authorities and auditors for five years at least.

**R12:Rating:(PC)**

**R12: Deficiency: There are several gaps related to customer due diligence and record keeping measures. There is no unified understanding among lawyers that they should identify and verify the identity of their clients and maintain identity proof documents of their clients for five years at least as of termination of relationship with the client.**

59. The Minister of Justice and Islamic Affairs issued the Ministerial Order no. (2) of 2008 in March 2008 with regard to obligations related to AML procedures in the law practice profession and foreign law firms in the Kingdom of Bahrain which authorizes the Ministry to supervise and conduct onsite inspection on the law practice sector and explain the AML/CFT monitoring requirements. However, the authorities have not provided any proof explaining the nature of the Ministry's role in monitoring the compliance with these requirements, how this role is performed and the findings of any monitoring operations that might have been conducted in this field.

**R15: Rating:(PC)**

**R15: Deficiency: The requirements of training on terrorist financing and subsequent application with regard to all FIs are deemed necessary. High employment criteria must also be a prerequisite for entities licensed to operate in the capital markets.**

60. Requirements set out in the rulebooks issued by the Central Bank of Bahrain to various institutions in the financial sector in Bahrain fulfill the requirements of R15 with regard to training of employees and developing appropriate basis for screening when hiring them.

**R16: Rating:(PC)**

**R16: Deficiency:It seems that the DNFbps do not know much about their duties to send STRs to the AML Unit. The law and some systems were put in place but there is lack of clear understanding by lawyers of their obligations to send reports.**

61. The Bahraini authorities reported that the guide issued by the Ministry of Industry and Commerce has been updated and that it includes procedures of reporting suspicious transactions. The Ministerial Order no. (126) of 2011 issued by the Minister of Industry and Commerce also includes procedures of reporting suspicious transactions pursuant to Article Nine. On the other hand, in March 2008, the Ministerial Order no. (2) was issued by the Minister of Justice and Islamic Affairs with regard to obligations in relation to AML procedures in the law practice profession and foreign law firms in the Kingdom of Bahrain. Despite the above, it seems that the DNFbps still suffer from non-compliance with the requirements of reporting suspicious transactions as statistics provided by the Bahraini authorities on sources of STRs did not show that any of the STRs was submitted by one of the DNFbps. Over the past years, 11 reports were submitted by the Ministry of Industry and Commerce.

**R20: Rating:(PC)**

**R20: Deficiency: Weaknesses are associated with absence of provisions on the risk constituted by modern technology and provisions of the Ministerial Decree 7/2001.**

62. As previously mentioned under R8, risks constituted by modern technology were dealt with in the rulebooks issued for the FIs by the Central Bank of Bahrain including the licensees in the capital markets.

**R21: Rating:(PC)**

**R21: Deficiency: More details should be given to entities licensed to operate in the capital markets. Onsite inspections must be done at entities licensed to operate in capital markets and licensed insurance companies. Counter measures must be developed in the system.**

63. The rulebooks issued by the Central Bank of Bahrain include requires the FIs to give special attention when dealing with other institutions in a country listed on the list of non-cooperating countries and regions issued by the FATF or in countries designated by the Central Bank of Bahrain. It was not clear whether the authorities designated any country for the FIs as one that does not apply the AML/CFT criteria for the benefit of the FIs. Moreover, it was not clear what the authorities did after the said list was no longer in use after the FATF stopped issuing it a while ago. On the other hand, the authorities did not provide any information on the level of compliance of the FIs with the application of this recommendation based on the inspections they conducted since the adoption of the MER. It was not also clear the occurrence of any kind of counter measures that can be applied towards countries that continue not to apply the FATF Recommendations. .

**R24: Rating (NC)**

**R24: Deficiency: There are no legal arrangements with regard to DNFBPs and the regulatory arrangements of the DNFBPs are dissatisfactory.**

64. The Minister of Industry and Commerce issued Ministerial Order no. (126) of 2011 then Ministerial Order no. (6) to amend the former Order in 2012 with regard to the application of the AML/CFT requirements by the institutions affiliated with the Ministry by virtue of Law 2011 amended in 2006 which provides the obligation elements for these requirements. However, the law does not designate the competent monitoring entities with regard to the DNFBPs in a clear manner. On the other hand, there was no sufficient information on the size of the different sectors subject to the Ministry's supervision and the available capabilities of the Ministry to monitor these sectors for the AML/CFT purposes.

**R28: Rating:(PC)**

**R28: Deficiency: There is no independent or predicate terrorist financing crime constituting a legal basis for investigation procedures or compulsory measures.**

65. By virtue of the legislative amendment in Law no. (54) of 2006 to Law no. (4) of 2001, terrorist financing was independently criminalized and deemed a predicate offence of the money laundering crime, therefore, Bahrain addressed all the deficiencies related to this recommendation.

**R31:Rating:(PC)**

**R31: Deficiency: There are no gates between the law enforcement authorities and supervisory authority for mutual assistance. There is need for more coordination and cooperation among ministries.**

66. The Bahraini authorities informed that they had enhanced coordination among the law enforcement authorities by establishing the AML/CFT Policy Committee as the Minister of Finance issued Ministerial Order No. (8) of 2012 restructuring the Committee so that it is constituted of representatives of the competent ministries in their professional capacities. It included the Under Secretary of Foreign Affairs, the Public Prosecution Head, Director General of the General Directorate of Anti-Corruption and Economic and Electronic Security in the Ministry of Interior, Director General of the General Directorate of Customs Clearance and Inspection, Director of Company Affairs Directorate in the Ministry of Industry and Commerce, Director of External Economic Relations Directorate in the Ministry of Finance Director of the Labor Relations Directorate in the Ministry of Labor, Director of National Non-Governmental Organizations Directorate in the Ministry of Human Rights and Social Development, Director of the Legislation and Gazette Directorate in the Legislation and Legal Opinion Commission, Director of Compliance Directorate in the Central Bank of Bahrain, Director of the Financial Analysis and Information Division in the National Security Agency, Director of the AML/CFT Unit in the Ministry of Interior and Director of the Settlement and Central Depository at Bahrain Bourse. This Committee is chaired by the Executive Director of Financial Institutions Supervision in the Central Bank of Bahrain. As previously mentioned, a legal subcommittee was formed to be in charge of reviewing all regulations and legislations and preparing final drafts before relaying them to the concerned entities for final approval and a committee was also formed to follow up on the execution of the SC resolutions. It is noteworthy that the legislative amendment in Law no. (54) of 2006 expanded the competencies of the AML/CFT Policy Committee to include coordination with competent entities with the aim to execute the United Nations Convention against Illicit

Traffic in Narcotic Drugs and Psychotropic Substances, the International Convention for the Suppression of the Financing of Terrorism and the United Nations Convention against Transnational Organized Crime and the Protocols Thereto and other relevant and applicable conventions, charters, systems and decisions as well as the AML/CFT FATF Recommendations.

**R32:Rating:(PC)**

**R32: Deficiency: There is no information on the total criminal profits that were seized and confiscated. Therefore, the effectiveness of systems should be reviewed.**

67. The Bahraini authorities reported that statistical information are available on the Bahraini Ministry of Interior website.

**SR8:Rating:(PC)**

**SR8: Deficiency: The Ministry of Social Development reviewed the legal and regulatory framework of the non-profit organizations (NGOs) and made a number of changes to address the weaknesses with regard to the financing of terrorism. However, during the visit of the evaluation team, the Ministry of Social Development did not have an effective framework to evaluate the progress made in these legal and regulatory conditions.**

68. The Ministry of Social Development created a directorate for monitoring and inspecting NGOs. The accounts of the organizations were inspected and audited through a certified legal accounting company as of January 2009 and the professional cadre of the directorate was enhanced reaching 36 employees who perform supervision, monitoring and follow up. The Ministry received 565 audited financial reports of NGOs until the end of February 2012. The Ministry also conducted 851 onsite inspection visits in 2011 in addition to 497 inspection visits until the end of June 2012. On the other hand, the Ministry issued a procedures manual and the guide to prepare financial reports of these organizations. The Ministry also executed the items of the articles set out in the Law of monitoring charity and non-profit organizations with regard to money transfers in coordination with the Central Bank of Bahrain. The Central Bank of Bahrain's rulebook requires banks to obtain an official letter from the Ministry of Social Development authorizing the receipt or remittance of the funds prior to accepting or processing such funds on behalf of charity and non-profit organizations. During the period from January 2011 to June 2012, the Ministry also referred 7 cases to the courts against a number of charity and non-profit organizations for violating the laws and procedures. Verdicts were passed in two cases.

**SR9:Rating:(NC)**

**SR9: Deficiency: No declaration or disclosure system or full regulation was put in place for the arrest powers of the customs.**

69. By virtue of the legislative amendment in Law no. (54) of 2006, “illicit cross-border transportation of cash” was defined. The definition set out in the law stipulated that it is “a criminal act committed by any natural or legal person using any technique, direct or indirect, by transporting cash across international borders if it is not disclosed in violation of the disclosure system or was a transportation for the purpose of money laundering or terrorist financing”. The said amendment added an article authorizing the Minister of Finance to designate the maximum limit of funds allowed to enter or depart the country without the need to disclose them. In case of issuing a decision designating it, funds exceeding the maximum limit shall be subject to the disclosure system issued by a decision of the Minister of Finance pursuant to suggestion of the AML/CFT Policy Committee. The Minister of Finance issued his decision no. (6) of 2008 with regard to the disclosure system of funds in customs departments which included stipulation of the definition of funds according to the definition set out in Law no. (4) of 2001 amended in Law no. (54) of 2006 and stipulation of the authority of the customs employees to take the necessary action to monitor the transported funds from and to the Kingdom of Bahrain through ports and within range of the customs departments and to ask travelers to disclose the funds in their possession and take all procedures with regard to inquiring about the suspicious funds inside the range of the customs departments and make the necessary reports and coordinate with other concerned entities. The regulation also included its application on legal persons who transport funds in shipments or mail packages and stipulation on punishing every person who violates the provisions of this regulation by the sanctions stipulated in Law no. (4) of 2001 amended in Law no. (54) of 2006.