FATF & PAKISTAN

PILDAT Training Course

Why are we still on the Grey-List?
How can we avoid the APG/FATF grey-list in the future?

A BANKER'S PERSPECTIVE

26th August 2021

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President & CEO, The Bank of Punjab

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CHAPTER 1

Is it in Pakistan's interest to tackle Money Laundering & Terrorist Financing ?

Menace of Illicit Financial Flows
How much money flows out of Pakistan?
What is the impact of grey-list on Pakistan?
Financial Sector and the grey-list

MENACE OF ILLICIT FINANCIAL FLOWS

- Illicit financial outflows of over 1 trillion[1] USD annually, flows out of developing economies through tax evasion and money laundering.
- Illicit flows of money laundering, tax evasion and bribery often reach OECD countries, as their compliance with FATF recommendations remains low[2].
- This leads to loss of revenue for the governments, a key reason for low tax to GDP ratio for developing countries.
- Developing countries must borrow to fund the deficit, leading to the unsustainable debt levels.
- Years of underinvestment in basic health and education fuel the cycle of low growth and poverty

HOW MUCH MONEY FLOWS OUT OF PAKISTAN?

- Illicit financial outflows of over 10 billion[3] USD annually, flows out of developing economies through tax evasion and money laundering.
- Over 15 billion USD invested in Dubai[4] real-estate in last ten years. Nearly, 46,058 real estate investments made by 32,083 investors in the past 10 years.
- Pakistan ranked in top 5 countries for illicit outflows into UK[5]. “Corrupt foreign elites continue to be attracted to the UK property market, to disguise their corruption proceeds”.
- Pakistan ranks poorly with a score of 6.3 in the Basel AML Index[6], ranking 28th from the bottom (out of 141 countries). The index measures ranking based on the FATF Mutual Evaluation Reports (MERs). Only countries like Afghanistan, Cayman Islands, Myanmar, Nigeria, and Cambodia ranked

1 Global Financial Integrity 2015 Report
2 OECD 2014 report Illicit Financial Flows from Developing Countries
3 US State Department’s International Narcotics Control Strategy Report 2017
4 Based on the Dubai Land Department (DLD) records
5 UK National risk assessment of money laundering and terrorist financing report 2020
6 https://baselgovernance.org/basel-aml-index

worse than Pakistan.

- Pakistan scores poorly in the WB World Governance Indicator on Control of Corruption[7]. The score of 21 out of 100 is a poor reflection of our ability to control corruption.

- Pakistan ranks 124 out of 179 countries in the Transparency International Corruption Perceptions Index[8].

WHAT IS THE IMPACT OF GREY-LIST ON PAKISTAN?

- Reputational damage from grey-listing adversely affects the country and its financial system by reducing its attractiveness for investors and corporates, ultimately leading to capital outflows and weaker economic performance.

- A country going into the grey-list faces higher cost of borrowing, higher risk premium for banks and downgrade of ratings. It also effects the potential borrowings from the IMF and other global financial institutions.

- The four macroeconomic variables that are most likely to be affected by FATF interventions include:
    - Gross domestic product,
    - Final consumption expenditures,
    - Exports,
    - Inward foreign direct investment.

- In Pakistan, the adverse economic effects of grey-listing are evident with a significant slowdown in FDI inflows since 2008, higher trade deficits with stagnant exports, heavy devaluation of currency and rise in inflation. All of this has translated into higher costs of doing business.

- Estimated cumulative GDP losses worth USD 38 billion , over 2008 to 2019 through reduction in consumption expenditures, exports, and FDI.

- Importantly, Pakistan's removal from the grey-list has at times led to the

7 https://info.worldbank.org/governance/wgi/
8 https://www.transparency.org/en/cpi/2020/index
9 https://www.tabadlab.com/wp-content/uploads/2021/02/Tabadlab-Working-Paper-07-Bearing-the-Cost-of-Global-Politics.pdf

revival of the economy, as evident from an increase in GDP growth during 2016 to 2018, after exiting the grey-list.

FINANCIAL SECTOR AND THE GREY-LIST

- Penalties imposed by U.S. and European regulators on global banks since 2009 for non-compliance with money laundering rules are estimated at USD 400 billion[10].

- HSBC fined USD 1.9 billion in 2012, BNP Paribus USD 9 billion in 2014, Credit Suisse USD 2.6 billion in 2014, and Goldman USD 2.9 billion in 2020.

- Banks holding more than 75% assets of financial sector act as largest channel for processing financial transactions and need to have effective systems in place to fight financial crime and limit illicit flow of funds to our financial system.

- Multiple factors contributed to Pakistan's inclusion in the grey-list

- It is argued that banks demonstrated low level of compliance with international standards and low investments in systems to curb the emerging threats posed by financial crimes.

- Banks perhaps need to make efficient use of technology for assessment of risk, controls, and ongoing monitoring of financial transactions and to enhance capacity by continuous training of its employees.

- We collectively need to focus on developing innovative solutions that may improve regulators' abilities to conduct due diligence on customers and to detect suspicious financial activities more effectively.

- In this era, we cannot ignore the power and utility of technology. It helps identify the potential risk exposed to various sectors more efficiently and provides sophisticated tools to monitor the movement of funds, from its origination to its final beneficiary by ensuring transparency for regulators and financial transitions.

10 https://www.spglobal.com/marketintelligence/en/news-insights/blog/bank-ma-revival-market-disruption-warning-venture-capital-funding-soars

CHAPTER 2

What are the FATF recommendations?

Introduction to FATF
FATF 40 Recommendations & the Benefits of Implementing them
FATF Assessment Methodology
Major changes in the FATF standards and framework
The 40 Recommendations in Relation to Financial Institutions (FIs)

INTRODUCTION TO FATF

- Established in 1989, the FATF is an inter-governmental policy making body, that has a ministerial mandate to establish international standards for combating money laundering and terrorist financing.

- Over 180 jurisdictions have joined the FATF or a FATF-style regional body and committed at the ministerial level to implementing the FATF standards and having their Anti-Money Laundering (AML)/ Counter-Terrorist Financing (CFT) systems assessed.

- FATF is seen as a "transnational public policy network" — consisting of 39 members. It has also established nine regional bodies which have fully endorsed their recommendations.

- So, between FATF members, its regional bodies, observer states and international organizations, around 205 countries and jurisdictions around the world have committed themselves to implement FATF recommendations.

- It must be noted that the FATF's role in global financial governance has become more prominent over the last few decades as it expanded its mandate in October 2001 after 9/11, by adding "terrorist financing" to its list.

- FATF is the main decision-making body, and its regional bodies provide support and assistance in those decisions. Every year in February, June, and October; a plenary meeting is held in Paris at the FATF secretariat.

- FATF categorizes countries with a fragile AML/CFT regime as 'jurisdictions under increased monitoring' (grey-listed), while countries with significant strategic deficiencies are labelled as 'high-risk jurisdictions' (blacklisted).

- Pakistan is a member of the FATF-style regional body called the Asia Pacific Group on Money Laundering (APG), which it joined in 2000.

- In 2012, due to non-compliance with the United Nations Security Council

Resolution (UNSCR) 1267, which called on countries to freeze assets, impose travel bans and arms embargos on any terrorist/militant groups linked with al-Qaeda, Pakistan was placed on the grey-list.

- It was removed from the list following amendments to the Anti-Money Laundering and Anti-Terrorism Act of 2015, in which measures were enacted to "confiscate the properties of the affiliated groups, as well as act against the financers of terrorist activities within the state".

- The FATF mandate is to set international standards to combat money laundering and terrorist financing. It monitors compliance with the FATF standards. It also responds to new and emerging threats.

FATF 40 RECOMMENDATIONS & THE BENEFITS OF IMPLEMENTING THEM

- FATF monitors compliance of member states against its 40 main recommendations on implementing effective measures against money laundering and terrorist financing.

- Implementation of the 40 recommendations increases transparency of the financial system (making it easier to detect criminal activity) and gives countries the capacity to successfully act against criminals.

- To demonstrate compliance, countries must successfully investigate and prosecute criminal acts of money laundering and terrorist financing.

- Criminalize money laundering and terrorist financing.

- Train law enforcement and legal authorities and equip them with sufficient powers and resources.

- Deprive criminals of their ill-gotten proceeds and resources needed to finance their illicit activities.

- Implement effective mechanisms to freeze, seize and confiscate criminal assets

- Require financial institutions and other businesses and professions to implement effective measures to detect and prevent money laundering and terrorist financing.

- Ensure that the required range of persons and entities in both the financial and non-financial sectors implement the AML/CFT preventative measures listed below:

  a. Customer due diligence (CDD): Prevent criminals from operating anonymously or under false identities by accurately identifying customers and knowing enough about their business to be able to differentiate between legitimate business and criminal activity.

  b. Record keeping: Keep accurate customer identification and transaction records that can be accessed by the authorities and enable transactions to be traced.

  c. Suspicious transaction reporting: Monitor customer relationships and promptly report any suspicious transactions to the financial intelligence unit for analysis and possible dissemination to law enforcement authorities.

- Ensure that financial institutions and other businesses and professions comply with AML/CFT requirements.

- Implement monitoring and supervision mechanisms, including powers to sanction financial institutions and other businesses and professions that do not comply with AML/CFT requirements.

- Enhance the transparency of legal persons and arrangements.

- Prevent legal persons and arrangements from being abused by criminals by ensuring that the appropriate authorities have timely access to accurate and current information concerning the ownership and control of the legal persons and arrangements.

- Implement mechanisms to facilitate cooperation and co‐ordination of AML/CFT efforts at the international and domestic level.

- Ensure that there are no safe havens for criminals by implementing mechanisms for effective cooperation countries in a timely manner when investigating and prosecuting money laundering and terrorist financing.

- Effective cooperation and coordination should also take place amongst domestic authorities (including law enforcement, prosecutorial and supervisory bodies, and the financial intelligence unit and policy makers).

Benefits of Implementing Recommendations

Stable & transparent financial system is more attractive to foreign investors

Financial institutions are less vulnerable to abuse by organized crime groups

Increased capacity to fight terrorism, trace terrorist money, & improve law & order

Increased compliance with international obligations

Avoid becoming a haven for criminals

Recommendations pertaining to National Risk Assessment, Monitoring, Feedback	R1: Assessing risks and applying a risk-based approach
	R2: National cooperation and coordination
	R3: Money laundering offense
	R4: Confiscation and provisional measures
	R33: Statistics
	R34: Guidance and feedback
Money Transfer	R14: Money or value transfer services
	R16: Wire transfers
	R32: Cash couriers
Designated Non-Financial Businesses	R8: Non-profit organizations
	R22: DNFBs: Customer due diligence
	R23: DNFBs: Other measures
	R28: Regulation and supervision of DNFBs
Terrorism, Terror Financing	R5: Terrorist financing offense
	R6: Targeted financial sanctions related to terrorism and terrorist financing
	R7: Targeted financial sanctions related to proliferation
Domestic Financial Institutions	R9: Financial institution secrecy laws
	R10: Customer due diligence
	R11: Record-keeping
	R12: Politically exposed persons
	R15: New technologies
	R17: Reliance on third parties
	R20: Reporting of suspicious transactions
	R21: Tipping-off and confidentiality
	R26: Regulation and supervision of financial institutions
	R29: Financial intelligence units

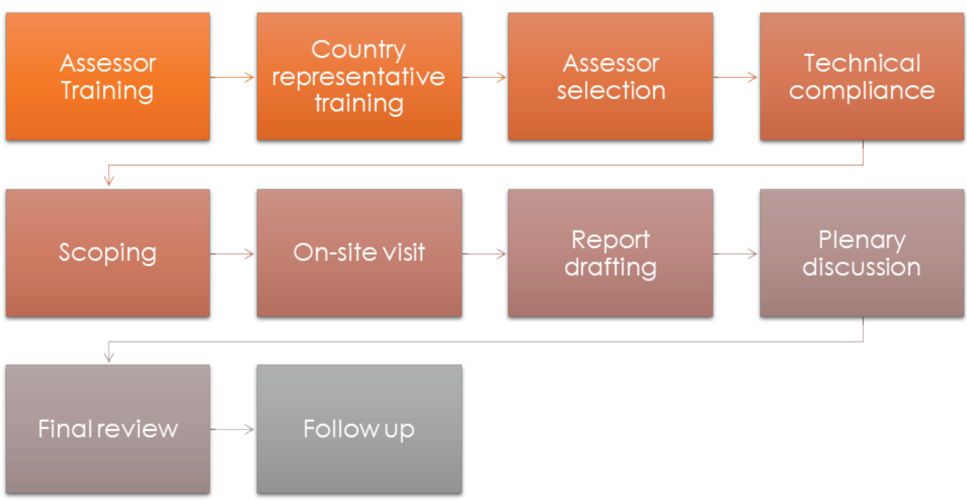
C	Compliant
LC	Largely compliant
PC	Partially compliant
NC	Non-compliant
MER	Mutual Evaluation Report
FUR	Follow-Up Report

Pakistan's ratings on FATF 40 Recommendations

C	LC	PC	NC
8	27	3	2

International Financial Institutions, International Cooperation	R13: Correspondent banking
	R18: Internal controls and foreign branches and subsidiaries
	R19: Higher-risk countries
	R36: international instruments
	R37: Mutual legal assistance
	R38: Mutual legal assistance: Freezing and confiscation
	R39: Extradition
	R40: Other forms of international cooperation
Law Enforcement Agencies, Investigative Authorities, Legal Persons and Arrangements	R24: Transparency and beneficial ownership of legal persons
	R25: Transparency and beneficial ownership of legal arrangements
	R27: Powers of supervisors
	R30: Responsibilities of law enforcement and investigative authorities
	R31: Powers of law enforcement and investigative authorities
	R35: Sanctions

FATF ASSESSMENT METHODOLOGY



MAJOR CHANGES IN THE FATF STANDARDS AND FRAMEWORK

- 1990: 40 Recommendations drawn up to combat the misuse of financial systems by drug money launderers
- 1996: 1st revision; to reflect evolving money laundering trends and to widen the scope of the recommendations beyond drug money laundering.
- 2001: FATF mandate expanded to deal with the funding of terrorist acts & terror organizations (8 Special Recommendations (SRs) formulated).
- 2003: 2nd revision; Universally recognized standards for AML/CFT endorsed by 180+ countries
- 2008: Recommendations 5, 6, & 8 revised, recommendation 7 added to combat proliferation of WMDs
- 2012: The 2012 revisions combined the IX Special Recommendations into the 40 Recommendations

A summarized schedule of additional amendments to the recommendations, and to their respective Interpretive Notes, is as follows:

- Oct 2016: revision in Recommendation 5 "Funds or Other Assets", update to interpretive note for Recommendation 5
- 2017: Recommendation 7 "Designated person or entity", Recommendation 18 "Internal Controls, Offshore Transactions", Recommendation 21 "Whistle Blowers and Confidentiality" revised/updated
- Feb 2018: Amendment in Recommendation 2 "National Coordination", and Recommendation 15 "New Technologies"
- June 2019: Recommendation 15 "New Technologies" updated
- 2020: Recommendation 1 "Assessing risks and applying a risk-based

approach" updated, and Recommendation 2 "National coordination and cooperation", and its interpretive note, revised

- 2021: Interpretive note for Recommendation 7 "Targeted Financial Sanctions for Proliferation Financing" updated

THE 40 RECOMMENDATIONS IN RELATION TO FINANCIAL INSTITUTIONS (FIs)

Recommendations related to FIs	R.1 Assessing risks and applying a risk-based approach
	R.3 Money laundering offense
	R. 4 Confiscation and provisional measures
	R.6 Targeted financial sanctions related to terror financing
	R.7 Targeted financial sanctions related to proliferation
	R.8 Nonprofit organizations
	R.9 Financial institution secrecy laws
	R. 10 Customer due diligence
	R.11 Record keeping
	R. 12 Politically exposed persons
	R. 13 Correspondent banking
	R.14 Money or value transfer services
	R.15 New Technologies
	R.16 Wire transfers
	R.17 Reliance on third parties
	R.18 Internal controls and foreign branches and subsidiaries
	R.19 Higher-risk countries
	R.20 Reporting of suspicious transactions
	R.22 DNFBs: Customer due diligence
	R.24 Transparency and beneficial ownership of legal persons
	R.25 Transparency and beneficial ownership of legal arrangements
	R.26 Regulation and supervision of financial institutions
	R.29 Financial intelligence units
	R.33 Statistics

Recommendations unrelated to FIs	R.23 DNFBs: Other measures
	R.28 Regulation and supervision of DNFBs
	R.30 Responsibilities of law enforcement and investigative authorities
	R.31 Powers of law enforcement and investigative authorities
	R.34 Guidance and feedback
	R.37 Mutual legal assistance
	R.38 Mutual legal assistance: Freezing and confiscation
	R.39 Extradition
Partially related to FIs	R.2 National Cooperation and coordination
	R.5 Terrorist financing offense
	R.21 tipping-off and confidentiality
	R.27 Powers of supervisors
	R.32 Cash couriers
	R.35 Sanctions
	R. 36 International instruments
	R.40 Other forms of international cooperation

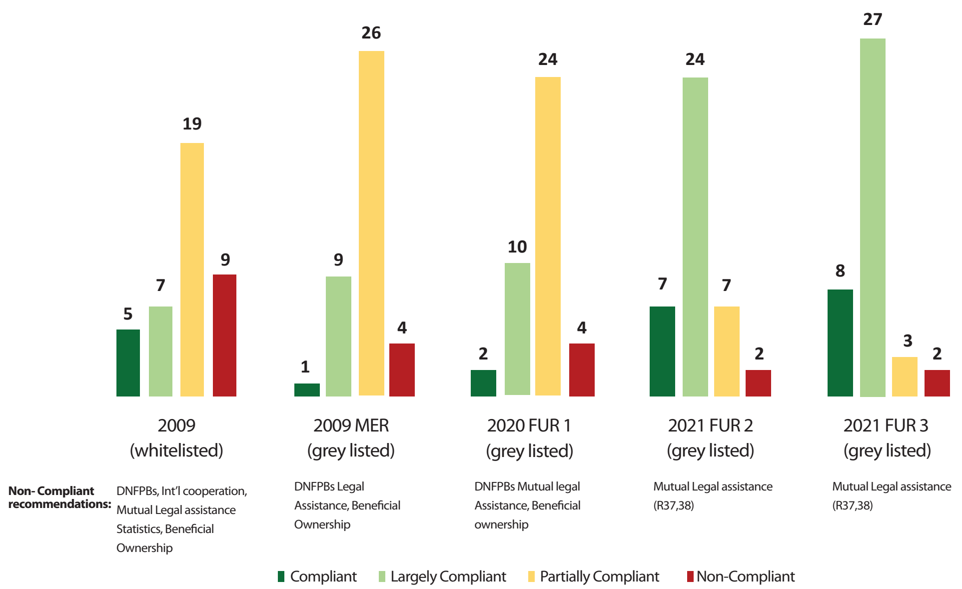
Recommendations related to FIs	**24**
Recommendations partially related to FIs	**8**
Recommendations unrelated to FIs	**8**

CHAPTER 3

Pakistan's progress on the FATF Recommendations

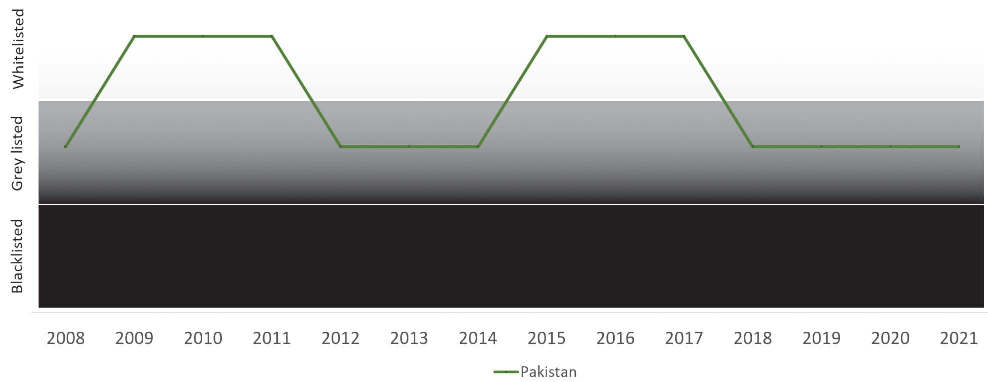
Significant progress made in last 3 years
New Laws introduced by the Parliament
Summary of SBP regulations for Regulated Entities (REs)

SIGNIFICANT PROGRESS MADE IN LAST 3 YEARS



Pakistan's history vis-à-vis its Ratings

Year	Event
2008	Pakistan is classified as high risk and non-cooperative in adopting AML/CFT legislation. Placed on the grey-list.
2009	Pakistan taken off grey-list.
2012	Pakistan is classified as high-risk and non-cooperative in adopting AML/CFT legislation. Placed on the grey-list.
2013	Pakistan remains on the grey-list until next evaluation
2014	Pakistan remains on the grey-list until next evaluation.
2015	Pakistan taken off grey-list after FATF identified progress in improving its AML/CFT regime.
2018	Pakistan was grey-listed for failure to address significant deficiencies in its AML/CFT regime.
2019	Pakistan remains on the grey-list until next evaluation.



PAST & CURRENT COMPLIANCE ON EACH RECOMMENDATION

R.	Rating
1	PC (MER2019) ↑ LC (FUR Oct 2020)
2	LC (MER 2019)
3	LC (MER 2019)
4	LC (MER 2019)
5	LC (MER 2019)
6	PC (MER 2019) ↑ LC (FUR Oct 2020)
7	PC (MER 2019) ↑ LC (FUR Oct 2020)
8	PC (MER 2019) ↑ LC (FUR Oct 2020)
9	C (MER 2019)
10	PC (MER 2019) ↑ LC (FUR July 2021)
11	LC (MER 2019)
12	PC (MER 2019) ↑ LC (FUR Oct 2020)
13	LC (MER 2019)
14	PC (MER 2019) ↑ C (FUR Oct 2020)
15	PC (MER 2019)
16	LC (MER 2019)
17	PC (MER 2019) ↑ LC (FUR Oct 2020)
18	PC (MER 2019) ↑ LC (FUR July 2021)
19	PC (MER 2019) ↑ C (FUR Oct 2020)
20	PC (MER 2019) ↑ C (FUR Oct 2020)

R.	Rating
21	PC (MER 2019) ↑ C (FUR Oct 2020)
22	NC (MER 2019) ↑ LC (FUR Oct 2020)
23	PC (MER 2019) ↑ LC (FUR Oct 2020)
24	PC (MER 2019) ↑ LC (FUR Oct 2020)
25	NC (MER 2019) ↑ LC (FUR Oct 2020)
26	PC (MER 2019) ↑ LC (FUR Oct 2020)
27	PC (MER 2019) ↑ C (FUR Oct 2020)
28	NC (MER 2019) ↑ PC (FUR Oct 2020)
29	PC (MER 2019) ↑ C (FUR Feb 2020)
30	PC (MER 2019) ↑ LC (FUR Oct 2020)
31	PC (MER 2019) ↑ LC (FUR Oct 2020)
32	PC (MER 2019) ↑ LC (FUR Oct 2020)
33	PC (MER 2019)
34	PC (MER 2019) ↑ LC (FUR July 2021)
35	PC (MER 2019) ↑ LC (FUR Oct 2020)
36	PC (MER 2019) ↑ LC (FUR July 2021)
37	PC (MER 2019) ↓ NC (FUR 2020 Oct)
38	NC (MER 2019)
39	LC (MER 2019)
40	PC (MER 2019) ↑ LC (FUR Oct 2020)

C	Compliant
LC	Largely compliant
PC	Partially compliant
NC	Non-compliant
MER	Mutual Evaluation Report
FUR	Follow-Up Report

THE BANK OF PUNJAB

NEW LAWS INTRODUCED BY THE PARLIAMENT

- Pakistan's initial response to its grey-listing consisted of a range of law enforcement measures, including a nationwide crackdown on banned terrorist outfits.

- This was followed by a series of administrative regulations and guidelines from key ministries, authorities and regulators aimed at streamlining the implementation of UNSC Resolutions 1267 and 1373 and broadly updating the AML/CFT frameworks. This enabled Pakistan to become compliant with only 5 action points on its 27 points-Action Plan.

- Pakistan enacted key legislation, including important amendments to foundational laws such as the Anti-Terrorism Act, 1997 and the Anti-Money Laundering Act, 2010, and updated its risk assessment frameworks in time for the next FATF plenary. This enabled Pakistan to become compliant on 14 of the 27 Points on the Action Plan by February 2020.

- Enacted Fifteen New Laws: In the eight months between February 2020, when the last formal decision to retain Pakistan on the 'grey-list' was taken, and October 2020, the government enacted fifteen new laws to ensure compliance with FATF's Action Plan. The latest plenary declared Pakistan largely compliant on 21 out of 27 Points, with varying degrees of progress on the remaining 6 points.

Major revisions under laws and regulations

a. Anti-Money Laundering Act,2020
b. Anti-Terrorism Act, 2020
c. Mutual Legal Assistance Act, 2020
d. United Nations Security Council Act, 1948
e. SBP AML/CFT/CPF, 2020

f. SECP AML/CFT Guidelines 2018 & 2019.
g. FBR AML/CFT Regulations for DNFBP's,2020
h. Guidelines on implementation of UNSC resolution
i. Countermeasures for High-Risk Jurisdictions Rules, 2020

SUMMARY OF SBP REGULATIONS FOR REGULATED ENTITIES (REs)

- **Risk-Based Approach to AML/CFT**: SBP RE's to ensure an entity level Internal Risk Assessment Report (IRAR), to identify, assess, and understand ML/TF/PF risks at entity level. IRAR shall consider the results of National Risk Assessment (NRA), as well as feedback from State Bank of Pakistan, Fraud Management Unit (FMU), Law Enforcement Agencies (LEAs) and other related stakeholders. SBP RE's will formulate policy for application of Simplified Due Diligence (SDD), Customer Due Diligence (CDD), and Enhanced Due Diligence (EDD) considering levels of ML/TF risks identified as low, medium, high in their IRAR. SBP will ensure that the IRAR is a dynamic and up-to-date document.

- **Customer Due Diligence**: SBP RE's are to conduct CDD of customers/occasional customers in matters set out in Section 7A (1) of the Act. RE's shall obtain additional information on the customer including occupation, volume of assets, information available through public databases, internet, among others. Additionally, RE's are required to obtain information regarding the intended nature of the business relationship and transactions, information on the source of funds or source of wealth of the customer, additional information on the reasons for intended or performed transactions and purpose of transaction. SBP RE's shall identify the beneficial owner(s) and take reasonable measures to verify the same by using reliable independent documentation. CDD also includes enhanced due diligence, simplified due diligence, ongoing monitoring of business relationships, dormant accounts, prohibition of personal accounts for business purposes.

- **Third Party Financial Institutions for CDD Measures**: although RE's are allowed to employ third party institutions for CDD, ultimately the responsibility lies on the RE.

- **Targeted Financial Sanctions (TFS)**: SBP RE's to undertake TFS obligations under UNSC act and ATA regarding Designated Persons (DPs) or Proscribed Persons (PPs), entities owned or controlled by them, individuals and entities acting on their behalf, or at their direction. No funds or other financial assets, resources, services, are made available to them unless authorized or otherwise notified in accordance with relevant provisions of the law. RE's shall identify individuals and entities acting on behalf of DPs, PPs, using risk screening databases, watch-lists, publicly known information, reliable media information, etc. If any relationship is found with a customer, RE's shall freeze without delay and prior notice, the funds, or other assets of the identified, report any assets frozen or actions taken, report freezing of assets to SBP within 48 hours, and as per Form B of the UNSC (Freezing and Seizure) Order, 2019.

- **Politically Exposed Persons (PEP's)**: Implement procedures and controls to determine if a customer is a PEP, or a close associate or family member of a PEP, prior to establishing a business relationship.

- **NGO/NPO/Charity/Trust Accounts**: RE's shall conduct Enhanced Due Diligence while establishing relationship. Individuals authorized to operate these accounts shall be subject to Customer Due Diligence separately. Personal accounts shall not be allowed for use under charity purposes. All existing NGOs, NPOs, shall be reviewed and monitored by RE's to ensure that these organizations are not linked with any DPs or PPs.

- **Reporting of transactions STRs/CTRs**: RE's shall file STRs (Suspicious Transaction Reports) and CTRs (Cash Transaction Reports) with Fraud Management Unit (FMU) as required under Section 7 of the Act.

- **Record Keeping**: RE's shall ensure compliance with record keeping instructions for maintaining records of documents and information, for CDD and other purposes. These records should be sufficient to permit reconstruction of individual transactions.

- **Money/Value Transfer Services (MVTS)**: RE's shall run awareness campaigns against illegal Money/Value Transfer Service (MVTS) businesses on an ongoing basis. RE's providing money transfer services shall ensure effective systems for monitoring and ensuring compliance with AML/CFT obligations. RE's shall ensure that none of their employees or branches are involved with conducting any illegal money transfers.

- **New Technologies**: SBP RE's shall identify and assess the ML/TF risks that may arise in relation to the development of new products and services. ML TF risk assessments shall be undertaken prior to the launch of such products and services. RE's shall update their operational models in accordance with the changing profile of various ML/TF risks.

- **Internal Controls**: Periodical IRAR shall recommend measures to Board of Directors (BoD), through time-bound action plan to ensure adequate introduction and implementation of AML/CFT controls. Internal controls also entail employee due diligence and trainings.

- **Counter measures for High-Risk Jurisdictions:** RE's shall comply with the obligations imposed in the counter measures for high-risk jurisdictions rules, 2020.

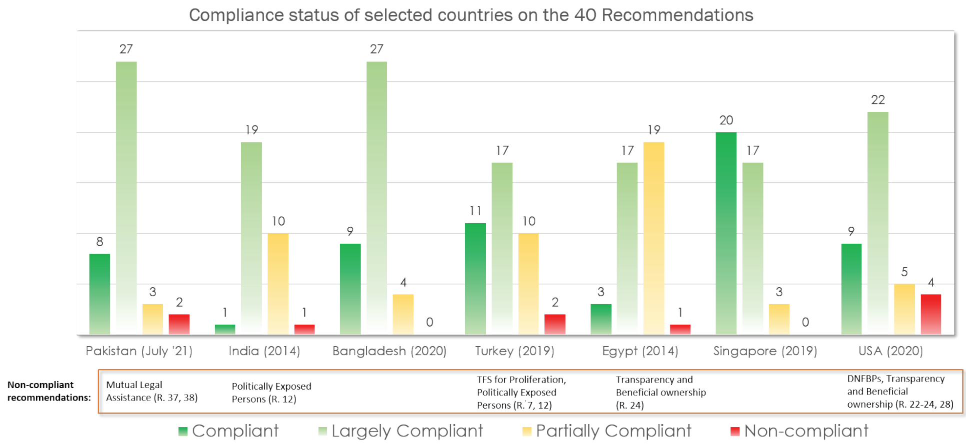
- **Regulation and Supervision**: RE's shall ensure that any person linked to any criminal activities or affiliated with any terrorist organizations shall not become part of SBP RE's. RE's shall ensure that any person subject to "Fit & Proper Test" (FPT) has been verified through NADRA, as per applicable laws and regulations.

CHAPTER 4

How does Pakistan compare to other countries?

Comparison with Selected Economies
Comparison to Muslim countries
Comparison to G20 countries
Comparison to Asia Pacific Group (APG) countries
Grey-listed & Blacklisted countries
FATF Statement on High-Risk and Other Monitored Jurisdictions

COMPARISON WITH SELECTED ECONOMIES



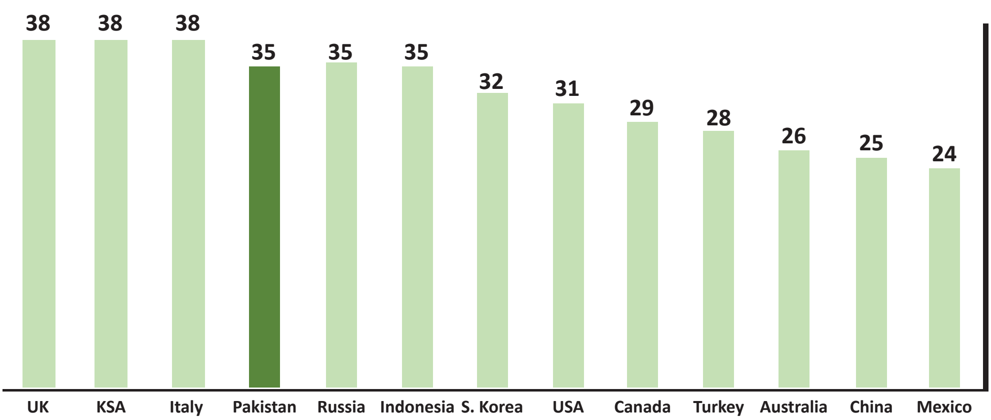
COMPARISON TO THE REGIONAL ECONOMIES

COMPARISON TO THE MUSLIM COUNTRIES

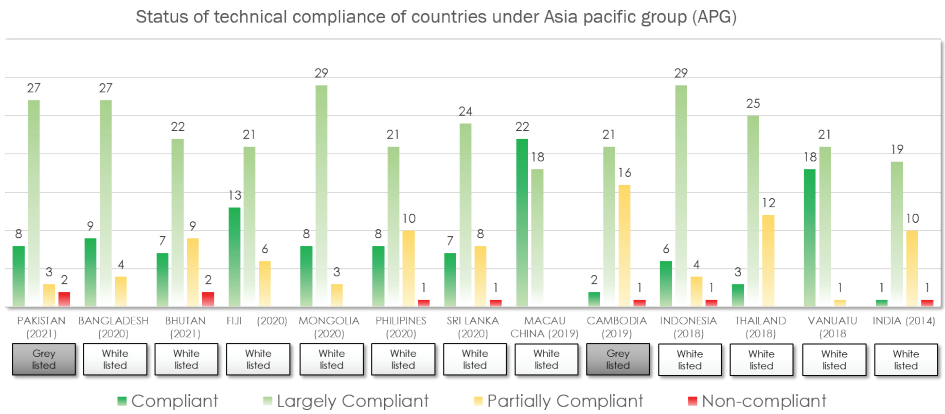
#	Country	Compliant	Largely compliant	Partially compliant	Non-compliant	Total C/LC	Listing	Non-compliant recommendations
1	KSA (2010)	17	21	2	0	38		
2	Algeria (2012)	7	30	3	0	37		
3	Tunisia (2020)	10	26	4	0	36		
4	Pakistan (2021)	8	27	3	2	35		R. 37, 38
5	Indonesia (2018)	6	29	4	1	35		
6	Bangladesh (2019)	9	27	4	0	35		
7	Egypt (2018)	9	23	8	0	34		
8	Bahrain (2018)	8	26	6	0	34		
9	Turkey (2007)	11	17	10	2	28		
10	Morocco (2020)	4	21	12	3	26		R.32, 29, 5
11	Oman (2011)	2	22	9	7	24		
12	Mali (2020)	6	15	16	3	21		
13	Jordan (2018)	4	15	15	6	19		
14	Syria (2018)	0	11	22	7	11		R. 5,13,21,23,24,25,32,
15	Qatar (2008)	1	9	20	9	10		
16	Iraq (2014)	2	7	26	5	9		
17	Afghanistan (2011)	3	5	8	24	8		
18	Iran	0	0	0	0	0		Has yet to complete 1st evaluation

COMPARISON TO G20 COUNTRIES

Recommendations rate Compliant/Largely complaint



COMPARISON TO ASIA PACIFIC GROUP (APG) COUNTRIES



GREY-LISTED & BLACKLISTED COUNTRIES

Country	Listing	No. of NC recommendations	Non-Compliant Recommendations
Albania		1	R.7 (Targeted Financial Sanctions Related to Proliferation)
Barbados		0	-
Botswana		4	R. 8 (NPOs), 14 (Money Transfer), 18 (internal controls), 21 (confidentiality)
Cambodia		1	R. 7 (Targeted Financial Sanctions Related to Proliferation)
Cayman Islands		0	-
Haiti		17	R. 1, 6, 7, 8, 16-19, 22-26, 31-33
Jamaica		2	R. 6 (Targeted Financial Sanctions for TF), 8 (NPO's)
Mauritius		1	R. 8 (Non-Profit Organizations (NPO's))
Morocco		3	R. 5 (TF Offense), 29 (Financial Intelligence Units), 32 (Cash Couriers)
Myanmar		3	R. 7 (TFS for Proliferation), 25 (Beneficial Ownership), 28 (DNFBPs)
Nicaragua		1	R. 15 (Money or Value Transfer Services)
Pakistan		2	R. 37 (Mutual Legal Assistance (MLA)), 38 (MLA: Freezing & Confiscation)
Panama		0	-
Philippines		1	R. 7 (Targeted Financial Sanctions for Proliferation)
Syria		7	R. 5,13,21,23,24,25,32
Zimbabwe		1	R. 24 (Beneficial Ownership of Legal Persons)
Iran		N/A	No evaluations undertaken
North Korea		N/A	No evaluations undertaken

FATF STATEMENT ON HIGH-RISK AND OTHER MONITORED JURISDICTIONS

- Global safeguards to combat money laundering and terrorist financing (AML/CFT) are only as strong as the jurisdiction with the weakest measures.

- Criminals can circumvent weak AML/CFT controls to successfully launder money or to move assets to finance terrorism through the financial system.

- A key objective of the FATF is to continually identify jurisdictions with significant weaknesses in their AML/CFT regimes, and to work with them to address those weaknesses.

- The FATF's process helps protect the integrity of the international financial system by issuing a public warning about the risks emanating from the identified jurisdictions.

- These public warnings also put pressure on the identified jurisdictions to address their deficiencies in order to maintain their position in the global economy.

- Public identification, and the prospect of public identification, encourages countries to swiftly make significant improvements.

NOTES

CHAPTER 5

Why is Pakistan still on the Grey-List?

Areas of Non-Compliance
Areas of Partial Compliance
Areas for Improvement
Training for Bankers
Will we ever get out of the grey-list?

AREAS OF NON-COMPLIANCE

Mutual Legal Assistance Recommendation 37: Significant Deficiency in Mutual Legal Assistance (MLA) Act. The requirement to inform the subject under investigation needs to be removed.

FATF stated that Pakistan was unable to provide MLA to foreign countries in the absence of a treaty for ML offences. There was also a lack of a legal basis to provide MLA in terrorism, TF and in most predicate offence cases. LEAs lacked powers to execute MLA requests.

Mutual Legal Assistance: Freezing & Confiscation, Recommendation 38: Pakistan needs to develop a framework to seize and confiscate assets and proceeds linked to ML/TF, and form an Asset Forfeiture Fund, wherein seized and frozen criminal proceeds can be kept. Pakistan was rated deficient with R.37, with the report finding that Pakistan was unable to provide MLA to foreign countries in the absence of a treaty for ML offences. There was also a lack of a legal basis to provide MLA in terrorism, TF and in most predicate offence cases. LEAs lacked powers to execute MLA requests.

AREAS OF PARTIAL COMPLIANCE

- **New Technologies R.15**: Pakistan included an assessment of certain ML and TF risk associated with financial inclusion products in the NRA including branchless banking, micro-finance and 'Asaan' accounts which Pakistan has rated 'low risk'. FMU did a strategic analysis on virtual currency risks and SBP issued a caution letter regarding those risks for public awareness.

- Other financial institutions outside the regulatory scope of the SBP and SECP are not required to undertake assessments as required by banks under SBP AML/CFT Regulations 2018.

- **Regulation and supervision of Designated Non-Financial Businesses & Professions (DNFBPs) R. 28**: Designated Non-Financial Businesses & Professions (DNFBPs) have a similar potential to financial institutions to be used for money laundering. Examples of DNFBPs include Auditors, external accountants, tax advisors, Company service providers, Dealers in precious metals and stones, Lawyers and notaries, Real estate agents and Trusts.

- Pakistan has taken steps to address shortcomings in relation to DNFBP supervision, including the establishment of an AML/CFT supervisory framework. Deficiencies remain with fit and proper requirements and the implementation of risk-based AML/CFT supervision for DNFBPs.

- **Statistics R.33**: The 2019 report found that not all statistics provided during the review were comprehensive and could not be broken down into meaningful and relevant information when requested. The report also noted that inconsistent statistics on the same issue were provided throughout the assessment process.

- Since the MER, FMU has started sharing a statistics report with LEAs on a quarterly basis. NACTA has developed a database of TF investigations, prosecutions, and convictions, in consultation with provincial CTDs. Pakistan is also preparing to introduce a central data management system.

AREAS FOR IMPROVEMENT

- Acquiring an enhanced understanding of ML/TF risks and predicate offenses[1].

- Increased use of financial intelligence. Easier dissemination to Counter-Terrorism Departments (CTDs)[2].

- Capacity building for investigators, prosecutors, and judges[3].

- Increased asset confiscation commensurate with Pakistan's risk profile[2].

- Enhanced cooperation between Federal Investigation Agency (FIA) & CTDs[1].

1 APG (2021), Anti-money laundering and counter-terrorist financing measures - Pakistan, 2nd Follow Up Mutual Evaluation Report, APG, Sydney https://www.fatf-gafi.org/media/fatf/documents/reports/fur/APG-2nd-Follow-Up-Report-Pakistan-2021.pdf
2 APG (2020), Anti-money laundering and counter-terrorist financing measures - Pakistan, 1st Follow Up Mutual Evaluation Report, APG, Sydney https://www.fatf-gafi.org/media/fatf/documents/reports/fur/APG-1st-Follow-Up-Report-Pakistan-2020.pdf
3 APG (2021), Anti-money laundering and counter-terrorist financing measures - Pakistan, 3rd Follow Up Mutual Evaluation Report, APG, Sydney

- Address technical deficiencies in framework for Targeted Financial Sanctions (TFS)[2].
- NPOs / NGOs enhanced and targeted risk mitigation and monitoring[3].
- Address technical deficiencies in legal framework for Terrorist Financing and Weapons of Mass Destruction (WMD) proliferation[1].
- Revised AML/CFT regulations to rectify remaining technical deficiencies (pertaining to AML supervision of Central Directorate of National Savings (CDNS), Pakistan Post and DNFBPs)[2].
- Enforcement actions against hawala/hundi including investigations and prosecutions of operators[3].
- Addressing hurdles to the provision of Mutual Legal Assistance (MLA)[3].

TRAINING FOR BANKERS

- Capacity building and trainings for bankers are another vital area which will help immensely in keeping controls tight and compliance levels high.
- The lack of awareness among bankers and authorities was one of the chief reasons Pakistan lagged in terms of complying with international standards regarding money laundering and terror financing.
- Consistent, high quality, world class on-going trainings are essential to remedy this shortcoming for the future.
- Bankers should be required to undertake international compliance related certifications under areas of AML/CFT.
- To stay current about changes in international laws and regulations, legal and regulatory trainings should be mandated.

1 APG (2021), Anti-money laundering and counter-terrorist financing measures - Pakistan, 2nd Follow Up Mutual Evaluation Report, APG, Sydney https://www.fatf-gafi.org/media/fatf/documents/reports/fur/APG-2nd-Follow-Up-Report-Pakistan-2021.pdf
2 APG (2020), Anti-money laundering and counter-terrorist financing measures - Pakistan, 1st Follow Up Mutual Evaluation Report, APG, Sydney https://www.fatf-gafi.org/media/fatf/documents/reports/fur/APG-1st-Follow-Up-Report-Pakistan-2020.pdf
3 APG (2021), Anti-money laundering and counter-terrorist financing measures - Pakistan, 3rd Follow Up Mutual Evaluation Report, APG, Sydney

- Trainings regarding changing sanction regimes and global compliance practices, as well as trainings on typology reports issued by FATF and its regional bodies would also be of significant benefit in elevating the capacity and capability of Pakistani bankers, thereby improving their performance and Pakistan's compliance as well.

WILL WE EVER GET OUT OF THE GREY-LIST?

- Absolutely, given the level of commitment and compliance across the board in Pakistan.

- Geopolitical constraints are likely to weigh heavily on the entire South Asian region, thereby having considerable implications for all our neighbouring countries, going forward.

- Technical deficiencies (non-compliance with Recommendations 37 & 38, "Mutual Legal Assistance") will need time to be implemented.

- Amendments to the Mutual Legal Assistance Act (MLAA) are awaited, so that it is in line with global standards, and does not restrict the provision of timely Mutual Legal Assistance to other countries.

- In addition to addressing areas of Non-Compliance, Pakistan must also address its areas of Partial Compliance; namely, Recommendation 15: "New Technologies", Recommendation: 28 "Regulation and Supervision of DNFBPs", and Recommendation 33: "Statistics".

- Pakistan must be prepared, both in terms of training of relevant personnel, and in terms of infrastructural/hardware requirements, to be able to effectively respond to emerging ML/TF challenges in the domain of cutting edge financial technologies and software, as well as Virtual Assets, and Digital Currencies.

- For Recommendation 28: "Regulation and Supervision of DNFBPs", Pakistan must enhance the regulatory powers of relevant authorities so that these authorities can provide effective oversight and supervision to legal and natural persons operating in the DNFBP sector (such as lawyers, notaries, dealers in gemstones and precious metals, real-estate agents, etc.).

- For Recommendation 33: "Statistics", Pakistan must invest in improving its data collection, reporting, and dissemination framework. FATF noted in 2 of its Follow-Up Reports that the data and statistics submitted for evaluation were often not consistent, accurate, or meaningful. This is a significant gap for a country with a ML/TF risk profile similar to Pakistan's.

- Additionally, Pakistan must enhance the comprehensiveness of its future National Risk Assessments (NRA). FATF reports noted a lack of comprehensiveness and accuracy in the past National Risk Assessments of Pakistan.

- Inter-Agency cooperation and coordination is another area that needs immediate attention and improvement.

- Enforcement of new laws and regulations still needs to be tested, and remaining gaps in key action items need to be filled.

- '**Do more**' demands are growing. In June 2021 the FATF issued a new 6 point 'Parallel Action' points to Pakistan.

- These points were focused on strengthening the Anti-Money Laundering framework of Pakistan. They were tailored to Pakistan's specific situation to cover existing gaps.

CHAPTER 6

Geopolitical challenges for Pakistan

Who voted for Pakistan in FATF?
Afghanistan challenge

WHO VOTED FOR PAKISTAN IN FATF?

- The FATF has granted membership to 37 countries and 2 intergovernmental organizations.
- In 2020, Pakistan required 12 out of 39 votes to exit the grey-list.
- Pakistan required 3 votes to keep from entering the blacklist. Turkey, Malaysia, and China have supported Pakistan to this end.
- A consensus among member states is required to overrule assessor ratings.

AFGHANISTAN CHALLENGE

The US government has blocked international assets of the Afghanistan central bank and western countries have categorically stated that they will not accept a Taliban government.

Afghan Govt. Assets frozen by the US

US Federal Reserve	Cash accounts	USD 0.3 billion
	U.S. bills/bonds	3.1 billion
	WB RAMP Assets	2.4 billion
	Gold	1.2 billion
	Total	7.0 billion
International Accounts		1.3 billion
BIS		0.7 billion
Grand Total		9.0 Billion

- Hence, any financial transactions between Pakistan and Afghanistan (trade, transit trade, investment, etc.) could potentially lead to sanctions, similar to the situation with Iran.

- Afghanistan is a major export market and in 2020, Pakistan exports stood at almost USD 1 billion to Afghanistan (4% of total exports).

- Pakistan and Afghanistan share a strong ethnic bond and a porous border.

- The 2010 Afghanistan-Pakistan Transit Trade Agreement (APTTA) was recently extended till December 2021. The first shipment through the Gwadar port was delivered in January this year.

- DAB (Central Bank of Afghanistan) reserves stand at USD 9.0 billion (as of 11th August 2021), held in liquid assets like Treasuries and gold.

- Due to Afghanistan's large Current Account Deficit, DAB was reliant on physical cash shipments every few weeks, which have ceased due to the security situation. Thereby bringing Afghanistan's domestic dollar cash holdings close to zero.

- Funds currently accessible by the Taliban are 0.1-0.2% of Afghanistan's total international reserves. The rest of the USD 9.0 billion has been frozen as per US sanctions policy, implemented by the US Office of Foreign Assets Control (OFAC).

- International Monetary Fund (IMF) has blocked Afghanistan's access to Special Drawing Rights (SDR's) and other resources.

- US has blocked its annual USD 3 billion military aid to the Afghan National Army.

- Up to 80% of Afghanistan’s budget was funded by the US and other international donors, prior to the fall of the government.

- Pakistan is caught in the cross hairs of the mess in Afghanistan and if not handled delicately, could lead to serious implications from the international community.

CHAPTER 7

Conclusion

CONCLUSION

- It is ultimately in Pakistan's interest to expeditiously improve the existing compliance framework to exit the grey-list. In this context, substantial and sincere efforts have been undertaken already and its continuing across all stakeholders within the country.

- Doing so will greatly benefit our economy, and halt the damaging outflow of illicit funds.

- With legislative, regulatory, and administrative mechanisms for combating Money Laundering and Terror Financing (ML/TF) in Pakistan largely in place, the next challenge is effective implementation.

- The outstanding areas highlighted by FATF in its latest statement focus on the key term 'demonstrating'.

- Thus, Pakistan will now have to effectively demonstrate that the mechanisms it has put in place for identifying ML/TF activity are bearing results; that targeted financial sanctions are quickly and directly being applied to designated entities and individuals; and that the criminal justice system is capable of enforcement of these regimes, from investigation to prosecution.

- At the same time, Pakistan must be mindful of the economic impact of legislative and regulatory regimes it develops in response to its grey-listing.

- FATF does not require countries to choke its economies by overly strict regulations but rather encourages states to pursue a risk-based approach so that measures to mitigate ML/TF are commensurate with the actual risks identified.

- This means that with the legislative, regulatory, and administrative frameworks for combating ML/TF now largely in place in Pakistan, the relevant authorities must be open to constantly reviewing and updating these frameworks so that a balance is struck between effective enforcement and vibrant economic activity and ease of doing business.

- Pakistan must also invest significantly in capacity building and capability enhancement of bankers, judges, prosecutors, investigators, etc., so that financial crime can be detected and combatted as quickly as possible.

- The Pakistani Banking Sector has played its part to the fullest in modifying Standard Operating Procedures and implementing regulations to improve compliance.

- Banks have endeavored to improve compliance without imposing costs on our clients.

- There has been timely and transparent implementation of requirements from most operators in the Banking Industry; this needs to be sustained.

- Pakistan's experiences as a frontline state in the war on terror have been of immense value to countries all over the world.

- Its successes in counterterrorism and counter-insurgency operations, from the former FATA region to Karachi, are perhaps without precedent, have been lauded globally.

- However, it did not effectively leverage its AML/CFT framework to augment its successes even further.

- In this context, the FATF grey-listing may have provided Pakistan with a historic opportunity for sustained, focused institutional reform and capacity-building which will have positive spillover effects for its economy and justice systems in the long run.

- It will also pave the way for Pakistan to eventually become a full member of FATF and contribute to the evolution of the global framework on AML/CFT as a responsible State.

- To avoid grey-list in the future, Pakistan must demonstrate the efficacy of its new legal, administrative, and legal frameworks, and ensure that these new frameworks do not impede the ease of business or hamper economic activity.

- Regulatory and supervisory bodies must perform periodic reviews and assessments to keep all ML/TF related controls updated and in-line with evolving money laundering and terror financing methods, as well as global best practices.

- It would also greatly serve Pakistan, if we were to invest effort in improving our diplomatic relations with FATF member states so that we can grow our support base, and so that more countries vouch for Pakistan in the future.

- We must also leverage positive media coverage to bring to light Pakistan's significant and impressive performance in combatting money laundering and terror financing.

- On the way forward, we must instill within ourselves and our systems a pre-emptive, future-proof, progressive approach towards combatting the emerging terror financing and money laundering challenges that will be born from new technologies like virtual and crypto currencies. Banks need to gear-up for those possibilities.

- Having said all that, given Pakistan's strategic context, geopolitics is the "Greatest Unknown", and simultaneously, perhaps the most consequential factor as well. As the popular adage (by political consultant Lee Atwater) goes: "**Perception is reality**". Similarly, how the world views us in the wake of the Taliban's ascension in Afghanistan, and other developments in the geopolitical arena are likely to have the highest weighting on the fate of Pakistan, vis-à-vis its continued exclusion from the grey-list.

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