CONSULTATION PAPER NO. 74

21 APRIL 2011

ANTI-MONEY LAUNDERING SUPERVISION IN THE DIFC AND ENHANCEMENTS TO THE REGULATORY LAW 2004

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Why are we issuing this paper?

1. This Consultation Paper seeks public comments on the following matters:

   (a) a joint proposal by the Dubai International Financial Centre Authority (DIFCA) and the DFSA to transfer responsibility for the Anti Money Laundering/Counter Terrorism Finance (AML/CTF) supervision of non-financial services firms from DIFCA to the DFSA;

   (b) consequential to (a) above, the DFSA also proposes certain changes to the current AML/CTF regime for non-financial services firms including, but not limited to:

      (i) amending the definition of Designated Non-Financial Businesses and Professions (DNFBP) as set out in paragraphs 17(a) and 17(b);

      (ii) implementing a registration process for DNFBPs operating in the DIFC as set out in paragraph 17(c); and

      (iii) other related enhancements set out in paragraphs 17(d) to 17(f); and

   (c) a DFSA proposal to amend the Regulatory Law 2004 to include delegation powers and to carry out other enhancements to that law in regard to the disclosure of confidential information to prescribed persons. In addition, the DFSA proposes to make certain miscellaneous, un-related amendments to other provisions of that Law

Who should read this paper?

2. The proposals in this paper would be of interest to:

   (a) DNFBPs operating or proposing to operate in the DIFC;

   (b) Single Family Offices and persons proposing to establish a Single Family Office in the DIFC;

   (c) DFSA-regulated Persons;

   (d) UAE and other regulators; and

   (e) advisors to Persons in (a), (b) and (c) above.

How is this paper structured?

3. In this paper, we set out:

   (a) a summary of our proposals (paragraphs 7 to 9);

(b) a summary of the current regime for AML/CTF for non-financial services firms (paragraphs 10 to 13);

(c) an outline of the key changes created by our policy proposals (paragraphs 14 to 22); and

(d) a summary of proposed enhancements to the Regulatory Law 2004 (paragraphs 23 to 28).

The proposed changes to the Regulatory Law 2004, the Glossary (GLO) Module and the proposed DFSA AML/CTF rules for DNFBPs as transcribed into the Rulebook (the DNF Module) are in Appendices 1, 2 and 3.

How to provide comments?

4. All comments should be in writing and sent to the address or email specified below. If sending your comments by email, please use the Consultation Paper number in the subject line. You may, if relevant, identify the organisation you represent in providing your comments. The DFSA reserves the right to publish, including on its website, any comments you provide, unless you expressly request otherwise at the time of making comments.

Comments to be addressed or emailed to:

Consultation Paper 74
Policy and Legal Services
DFSA
PO Box 75850
Dubai, UAE

e-mail: consultation@dfsa.ae

Tel: +971(0)4 3621500

What happens next?

5. The deadline for providing comments on the proposals is **21 May 2011**. Once we receive your comments, we will consider if any further refinements are required to these proposals. We will then proceed to recommend the proposed changes to the Law to the President, for enactment by the Ruler. You should not act on these proposals until the relevant changes to the legislation are made. We will issue a notice on our website telling you when this happens.

Terminology in this paper

6. In this paper, defined terms are identified throughout by the capitalisation of the initial letter of a word or of each word in a phrase and are defined in the Glossary Module (GLO) or in the proposed amendments. Unless the context otherwise requires, where capitalisation of the initial letter is not used, the expression has its natural meaning.

Summary of proposals

7. As part of its recent strategic review, DIFCA proposes to transfer its supervisory and enforcement powers in relation to non-financial services firms' compliance with relevant AML/CTF Laws to the DFSA. DIFCA currently supervises DNFBPs and Single Family Offices for AML/CTF purposes. Under this proposal, the DFSA would assume responsibility for all AML/CTF supervision in the DIFC. The DFSA currently supervises AML/CTF compliance of Financial Services firms and Ancillary Service Providers. The DFSA would become the single AML/CTF regulator in the DIFC.

8. In relation to the above, the DFSA is also proposing certain amendments to the current AML/CTF regime for non-financial services firms including, but not limited to:

   (a) Amending the definition of a DNFBP as set out in paragraphs 17(a) and 17(b);

   (b) implementing a registration process for DNFBPs operating in the DIFC as set out in paragraph 17(c); and

   (c) other related enhancements set out in paragraphs 17(d) to 17(f).

9. The DFSA proposes certain changes to the Regulatory Law 2004 to accommodate this new conferred jurisdiction and also to add a power to give and receive a delegation of power and functions. These changes follow the recent enactment of amendments to the Dubai Law No. 9 which permit such conferral and delegation. Furthermore, the DFSA has proposed some enhancements to the Regulatory Law 2004, Collective Investment Law 2010 and Markets Law 2004 to correct various anomalies.

The current AML/CTF regime

10. The United Arab Emirates (UAE) is a member of the Gulf Cooperation Council (GCC), which in turn is a member of the Financial Action Task Force (FATF). The UAE is also a member of the regional body for AML/CTF in the Middle East and North Africa, MENAFATF. Accordingly, the UAE commits to comply with the measures agreed to by the FATF members, in particular, to comply with the FATF Forty Recommendations and Nine Special Recommendations.

11. Of FATF's 40+9 Recommendations in relation to AML, four address DNFBPs and other high risk businesses and professions. The relevant requirements described within these Recommendations are materially less onerous than those which apply to financial services firms, reflecting the generally lower level of risks posed by DNFBPs. The four Recommendations are as follows:

   (a) Recommendation 12 defines DNFBPs, incorporates aspects of other recommendations stating that DNFBPs should have customer duediligence and record-keeping requirements that are the same as for financial institutions. Examples of relevant DNFBPs as defined by FATF are the following business activities:

(i) Real Estate Agents;

(ii) Dealers in Precious Metals and Dealers in Precious Stones;

(iii) Accountants, Lawyers, Notaries, and other Legal Professionals; and

(iv) Trust Service Providers and Company Service Providers;

(b) Recommendation 16 states that DNFBPs should have systems and controls, training, and audits that are designed to prevent money laundering and terrorist financing. Further, DNFBPs should be required to report suspicious activity to the relevant authorities;

(c) Recommendation 20 states that consideration should be given to applying the FATF Recommendations to businesses and professions, other than DNFBPs, that pose a money laundering or terrorist financing risk; and

(d) Recommendation 24 states that DNFBPs should be subject to risk-based regulatory and supervisory measures to ensure their compliance with money laundering and terrorist financing requirements. This may be performed by a government authority or an appropriate self-regulatory organisation.

12. In the DIFC, compliance with the relevant FATF Recommendations for DNFBPs is predominantly achieved through DIFCA's Non Financial Anti Money Laundering/Anti Terrorist Financing Regulations (the DNFBP Regulations) which were enacted on 18 July 2007. The DIFCA compliance department is responsible for administering the DNFBP Regulations which apply to the following persons provided that they are not otherwise supervised by the DFSA for AML/CTF purposes:

(a) real estate agents involved in transactions for a client concerning the buying or selling of real estate;

(b) dealers in precious metals and stones which engage in cash transactions equal to or greater than $15,000 (the designated threshold set out in the Interpretive Notes to FATF's 40+9 Recommendations);

(c) dealers in high value goods and services which engage in cash transactions equal to or greater than $15,000;

(d) lawyers, notaries, independent legal professionals, accountants and auditors which carry out certain specified transactions with their clients; and

(e) company service providers which carry out certain specified transactions with their clients.

13. Specific AML/CTF provisions for Single Family Offices are contained within DIFCA's Single Family Office Regulations (SFO Regulations).

Outline of our proposed changes

14. The following paragraphs set out the key changes and issues that the Consultation proposals raise.

AML/CTF

15. The transfer of DIFCA's supervisory and enforcement powers in relation to DNFBPs' compliance with relevant AML/CTF laws to the DFSA is proposed in order to consolidate the general supervision of DIFC entities in relation to AML/CTF into a single regulator. This will provide the following advantages to the DIFC:

    (a) the concentration of AML/CTF supervision will improve consistency of application of DIFC AML/CTF laws and policy;

    (b) the DIFC will benefit from the DFSA's existing expertise in AML/CTF matters and enforcement of AML/CTF breaches; and

    (c) all DIFC entities will have a single point of contact for AML/CTF matters and the DFSA will also act as the central DIFC contact point for UAE and international bodies.

16. The DFSA proposes to execute the transfer of DIFCA's AML/CTF powers by integrating the following:

    (a) the DNFBP Regulations and amendments to these regulations which were being considered by DIFCA;

    (b) the SFO Regulations; and

    (c) DFSA enhancements to (a) to (b) above.

17. Accordingly, the proposed new DFSA AML/CTF Rules applying to all DNFBPs will impose requirements which go beyond the DNFBP Regulations. The key proposed changes are as follows:

    (a) The DFSA proposes to include insolvency firms, real estate developers and Single Family Offices within the definition of a DNFBP for the following reasons:

        (i) it is considered appropriate that insolvency firms monitor the risk of being used by insolvents (or third parties such as purchasers of businesses and assets) to launder money;

        (ii) similar to real estate agents, real estate developers may also engage in transactions for a client concerning the buying or selling of real estate; and

        (iii) the inclusion of Single Family Offices will enable the integration of all of DIFCA's AML/CTF regulations within the same module of the DFSA rulebook;

(b) The DFSA proposes to exclude high value services providers from the definition of a DNFBP as they are not considered to pose material AML/CTF risk. This is primarily because high value services are unlikely to be tradable, thereby lowering the risk that such services will be used to disguise money laundering or terrorist financing activities. Further, it is not common practice in other jurisdictions to monitor such businesses for AML/CTF purposes;

(c) The DFSA proposes to implement a registration process (as described in DNF Rule 3.1 in Appendix 2). Under this proposal, a person designated as a DNFBP will be required to notify the DFSA when it commences or ceases to be a DNFBP;

(d) In compliance with the FATF Special Recommendations on Terrorist Financing, the DFSA proposes that a DNFBP be required to establish and maintain effective systems and controls to obtain and make appropriate use of relevant resolutions and sanctions issued by the United Nations Security Council;

(e) The DFSA also proposes that a DNFBP be required to make appropriate use of findings, guidance, recommendations or the like made by the DFSA, Central Bank of the UAE, UAE Government, UAE enforcement agencies or other government related departments in the UAE in relation to money laundering and terrorist financing matters; and

(f) It is also proposed that DIFCA's existing supervisory and enforcement powers in Parts 5 & 6 of the DNFBP Regulations be replaced with the DFSA's own supervisory and enforcement powers in the Regulatory Law 2004.

18. Due to the nature of a Single Family Office's activities, which are limited to a Single Family, the DFSA proposes to implement a lighter-touch regime for these entities than for other DNFBPs. However, the DFSA proposes the following additional requirements for Single Family Offices which do not currently exist within the SFO Regulations:

(a) to inform the DFSA if another jurisdiction's laws or regulations prevent them from complying with the new AML/CTF rules or UAE Federal Law concerning AML/CTF;

(b) to nominate to the DFSA an individual to carry out the function of Money Laundering Reporting Officer (MLRO). The nominated MLRO must also meet certain criteria in relation to their seniority, available resources and access to relevant information to perform this function. This is not considered a material change as the SFO Regulations currently assign the responsibilities for AML/CTF compliance to the Authorised Representative of a Single Family Office; and

(c) to nominate a successor within a prescribed time period should the nominated MLRO leave the Single Family Office's employment.

19. The DFSA proposes to adopt a risk-based approach to the supervision of DNFBPs. Accordingly, the DFSA will concentrate its resources on those DNFBPs which pose greater risks to the DFSA's objectives.

20. Minimal transitional arrangements will be required for existing DNFBPs and Single Family Offices as the compliance requirements will remain substantially the same. However, the DFSA proposes to give DNFBPs 90 days from the effective date to comply with the new AML/CTF Rules. To complement this process, the DFSA proposes to undertake an outreach and training programme for DNFBPs immediately before and during the 90 day period after implementation of the new regime.

21. In order to achieve the proposed transfer of AML/CTF powers, the DFSA has proposed certain consequential amendments to the Regulatory Law 2004. This includes amendments to the following Articles:

    (a) 8(3) – the Powers, Functions and Objectives of the DFSA;

    (b) 20(1) – the Powers and Functions of the DFSA Board of Directors;

    (c) 36 – the Powers and Functions of the Chief Executive;

    (d) 60 – regarding registration powers;

    (e) Part 4 – General Regulation of Financial Services; and

    (f) 70 to 72 – regarding anti-money laundering.

22. The proposed amendments extend the DFSA's objectives to include any powers or functions conferred upon the DFSA as permitted under the recent amendments to Dubai Law No.9 of 2004. This will grant the DFSA certain powers which will permit the DFSA to formulate AML/CTF policy in relation to DNFBPs and give the DFSA a power to register and make rules in relation to DNFBPs.

Issues for consideration

1. Do you have any concerns or comments about our proposed assumption of the AML/CTF supervisory powers in relation to DNFBPs?

2. Does the proposed transfer of powers create any unintended consequences?

Enhancements to the Regulatory Law 2004

23. Following the recent changes to Dubai Law No. 9 of 2004, mentioned above, we are proposing to amend Article 20(1) of the Regulatory Law 2004 to expressly permit the DFSA to accept a delegation of powers or functions from another person pursuant to Dubai Law. We are also amending Article 12(2) of the Regulatory Law 2004 to extend the scope of the DFSA's protection from liability to include the exercise of a delegated power.

24. These proposed amendments are designed to bridge an existing gap in the Regulatory Law 2004 that limits the DFSA's ability to accept a delegation from another person under Dubai Law. The acceptance by the DFSA of a delegation without an express power to do so in the Regulatory Law 2004 and without the necessary protection from liability necessary in order to carry out a delegated power or function carries an unacceptable level of legal risk for the DFSA.

25. In regard to Article 38 ("confidential information") of the Regulatory Law 2004, we are proposing an enhancement to include a gateway to permit disclosure of confidential information to a regulatory body who regulates auditors, lawyers or accountants;

26. The DFSA needs to be able to exchange information with other regulators in regard to the Ancillary Service Providers and Registered Auditors it regulates in order to carry out its functions and exercise its powers in pursuit of its objectives. However, there is some doubt about the DFSA's ability to do so and hence the proposed amendments to clarify the DFSA's ability to disclose such information under Article 38 of the Regulatory Law 2004 set out in the Appendix 1.

27. Consequential amendments are proposed to Article 39 (Exercise of powers on behalf of other regulators) of the Regulatory Law 2004.

28. Other proposed amendments to the Regulatory Law 2004 are to carry out various enhancements including removing an anomaly in Article 20(1)(c) by deleting the provision. This is because Article 20(1)(c) is now redundant in light of the detailed Financial Markets Tribunal provisions in Articles 31 to 35 and the administrative penalty provisions in the Law. Other proposals are to correct a typographical error to Article 44(5) and to correct a number of grammatical errors in Article 75(1).