TYPOLOGY REPORT ON THE STUDY ON MONEY LAUNDERING THROUGH THE SECURITIES MARKET IN THE ESAAMLG REGION

September 2015
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**ACRONYMS**

<table>
<thead>
<tr>
<th>Acronym</th>
<th>Description</th>
</tr>
</thead>
<tbody>
<tr>
<td>AML</td>
<td>Anti-Money Laundering</td>
</tr>
<tr>
<td>AML/CFT</td>
<td>Anti-Money Laundering/Counter Financing of Terrorism</td>
</tr>
<tr>
<td>CDD</td>
<td>Customer Due Diligence</td>
</tr>
<tr>
<td>CIS</td>
<td>Collective investment scheme</td>
</tr>
<tr>
<td>CFT</td>
<td>Counter Financing of Terrorism</td>
</tr>
<tr>
<td>CSD</td>
<td>Central Securities Depository</td>
</tr>
<tr>
<td>ESAAMLG</td>
<td>Eastern and Southern Africa Anti-Money Laundering Group</td>
</tr>
<tr>
<td>FATF</td>
<td>Financial Action Task Force</td>
</tr>
<tr>
<td>FIU</td>
<td>Financial intelligence unit</td>
</tr>
<tr>
<td>LEA</td>
<td>Law Enforcement Agency</td>
</tr>
<tr>
<td>LCR</td>
<td>Large Cash-transaction Reporting</td>
</tr>
<tr>
<td>IPO</td>
<td>Initial Public Offer</td>
</tr>
<tr>
<td>IOSCO</td>
<td>International Organization of Securities Commissions</td>
</tr>
<tr>
<td>KYC</td>
<td>Know Your Customer</td>
</tr>
<tr>
<td>ML</td>
<td>Money Laundering</td>
</tr>
<tr>
<td>ML/TF</td>
<td>Money Laundering/Terrorism Financing</td>
</tr>
<tr>
<td>MLRO</td>
<td>Money Laundering Reporting Officer</td>
</tr>
<tr>
<td>MMOU</td>
<td>Multi-party Memorandum of Understanding</td>
</tr>
<tr>
<td>MOU</td>
<td>Memorandum of Understanding</td>
</tr>
<tr>
<td>NRA</td>
<td>National Risk Assessment</td>
</tr>
<tr>
<td>OTC</td>
<td>Over the Counter</td>
</tr>
<tr>
<td>PEP</td>
<td>Politically Exposed Person</td>
</tr>
<tr>
<td>RBA</td>
<td>Risk Based Approach</td>
</tr>
<tr>
<td>Abbreviation</td>
<td>Description</td>
</tr>
<tr>
<td>--------------</td>
<td>-----------------------------------</td>
</tr>
<tr>
<td>REIT</td>
<td>Real-Estate Investment Trust</td>
</tr>
<tr>
<td>RTGS</td>
<td>Real Time Gross Settlement System</td>
</tr>
<tr>
<td>SMR</td>
<td>Securities Market Regulator</td>
</tr>
<tr>
<td>SROs</td>
<td>Self Regulating Organisations</td>
</tr>
<tr>
<td>STR</td>
<td>Suspicious Transaction Report</td>
</tr>
<tr>
<td>TF</td>
<td>Terrorist financing</td>
</tr>
</tbody>
</table>
ACKNOWLEDGEMENTS

The study was carried out by Zimbabwe, Swaziland, Zambia, Kenya, Mauritius, South Africa and Tanzania. The project team was chaired by Zimbabwe.

The project team would like to thank the ESAAMLG Council of Ministers for providing them the opportunity to carry out this typology study. It also acknowledges the valuable assistance and support provided by the ESAAMLG Secretariat, the South African Financial Intelligence Centre, which housed the project team meetings and the ESAAMLG member countries.
EXECUTIVE SUMMARY

The 13th ESAAMLG Council of Ministers Meeting held in Swakopmund, Namibia, in September 2013 approved the typology research on, “ML/TF through the securities market in the ESAAMLG Region”.

The purpose of the study is to analyse the main sources of funds being invested in the ESAAMLG securities market and the possible linkages to ML/TF activities; risks and red flags that are prevalent in the securities market. Further, to raise awareness of the ML/TF risks in the securities market to local, regional and international stakeholders by identifying possible methodologies used by money launderers in the securities market to launder proceeds of crime, measures being undertaken by countries to mitigate identified ML/TF risks in securities markets, and more importantly to make recommendations on appropriate measures for combating ML/TF through the securities market in the ESAAMLG region.

There exist a literature gap on whether the ESAAMLG securities industry is vulnerable to money laundering. However, previous studies carried out by the Financial Action Task Force (2003 and 2009), MONEYVAL (Eastern Europe) (2008) and Asia/Pacific Group (2009) established that securities markets can be used as one of the vehicles for money laundering and the financing of terrorism. This adds to the need for this study to establish whether securities in the ESAAMLG region are being used to launder money or financing of terrorism.

The study was commenced in September 2014 and the due date for completion was September 2015. The Project Team started with the collation for readily available information and drafted a questionnaire that contained both open and close ended questions which was circulated to the 18 ESAAMLG member countries from the 4th of

1 Public information from the website of the different Ministries of Finance, LEAs and Relevant Regulatory bodies, previous typologies reports, etc.
November 2014 until the 1st of February 2015. In light of the information submitted the project team requested further clarifications from compliant jurisdictions and a further extension was provided to submit the missing information by 30 April 2015.

The collected data was analysed using available tools and reliable information from reputable organisations\(^2\) contained in public information reports. The study indicators are summarized as follows: (i) Overview of ESAAMLG’s securities sector; (ii) Licensing, supervision, preventive measures and sanctioning system of securities investment service providers in the ESAAMLG member countries; (iii) Current and planned mitigation measures; (iv) ML/TF threats; (v) Law enforcement and investigative authorities; (vi) International Cooperation; and (vii) Overall securities sector risk assessment.

Further, the study concluded that the clearing and settlement frameworks in almost all the member country jurisdictions do not address AML/CFT issues and that the most common predicate offence related to the sector is the fraudulent change of ownership of shares which has potential to create proceeds which can be laundered. The study did not find any incidences of TF related to the securities market.

The study revealed that there are indicators of AML/CFT risks in the securities market which renders the sector vulnerable, however, these can be mitigated. The study has proposed recommendations to assist member countries in mitigating the risks identified and also encourages member countries to adopt regional and international best practices.

The following list highlights the salient findings of this typology study: (i) jurisdictions need to request for and verify the sources of funds upon application for a license, or registration, or transactions involving amounts above the set threshold; (ii) jurisdictions should ensure that accountable institutions have an automatic system whereby STRs are identified and reported automatically and without delay; (iii) jurisdictions should increase the level of awareness of AML/CFT domestically; (iv) jurisdictions should

\(^2\) FATF Typology Report 2009, etc.
through legislation, strengthen KYC and CDD requirements and introduce mechanisms to ensure effective implementation of such requirements; (v) jurisdictions should have dedicated specialised units within their law enforcement authorities to carry out investigation on cases relating to the securities market sector; (vi) jurisdictions should have cash thresholds reporting requirements, and (vii) should implement a RBA to supervision in respect of their securities market sector.

REPORT STRUCTURE

The report consists of the following structure:

**Chapter 1** is divided into Part A and Part B. Part A, gives the contextual background of the study. It outlines the research objectives, questions, scope and focus and benefits of the study. Part B, outlines the research methodology and approaches that were used in gathering research data.

**Chapter 2** presents research findings, analysis and discussion of findings.

**Chapter 3** is a critical review of existing literature on ML/TF through the securities market, main sources of funds, risks and red flags, methodologies, awareness and mitigating measures.

**Chapter 4** provides recommendations and conclusion for the securities market sector and other stakeholders.
1. CHAPTER 1: INTRODUCTION

1.1. PART A: INTRODUCTION AND BACKGROUND

This section provides an overview of the status of the securities market sector in the ESAAMLG region, with a special focus on its eighteen (18) member countries, namely Angola, Botswana, Comoros, Ethiopia, Kenya, Lesotho, Malawi, Mauritius, Mozambique, Namibia, Rwanda, Seychelles, South Africa, Swaziland, Tanzania, Uganda, Zambia and Zimbabwe. Furthermore, it provides background information regarding: the nature of the securities market products/types of securities, problem statement, research objectives, questions, scope and focus and benefits of the study.

1.1.1. Background of the study

The dawn of financial globalization owing to technological developments, financial innovation and opening up of several economies has resulted in the huge cross-border flow of funds and scrip between jurisdictions. The sophisticated and complex financial assets being traded, the chain of transactions and payments changing hands on frequent basis has increased the risks of the securities markets being used by participants whose goal is not only to optimise returns on their savings but also to launder illicit proceeds and, in certain instances, finance terrorist activities.

The securities market is where equities, bonds, derivatives, commodities and other financial instruments are traded. The market also involves movement of dual and cross listed shares between jurisdictions.

Most of the ESAAMLG member countries have securities exchanges, with the exchanges at various levels of development and the type of products traded varying from one jurisdiction to another. ESAAMLG member countries securities markets are not developing as fast as expected having only South Africa where the volume of derivative transactions has been growing. South Africa and Botswana also have commodities exchange markets, with Botswana trading on OTC system and South Africa having the largest bond exchange in the ESAAMLG region.
Securities in the ESAAMLG region are defined as: Shares; Debt Securities; Government and Public debt securities; Warrants; Depository receipts; Options, futures, forwards or other derivatives; participatory interests in a Collective Investment Scheme (CIS); and other instruments.

In some jurisdictions there are exclusions in the definitions. These include: treasury bills with original maturity of less than one year, promissory notes, certificates of deposit issued by a bank, securities of a private company other than asset backed securities, and bills of exchange. Out of the 18 member countries assessed, Lesotho is the only country that does not trade in equities and the only jurisdiction having Government Bonds, Treasury Bills and Unit Trust being traded as securities.

1.1.2. Problem statement

There exists a literature gap on the vulnerabilities and risks associated with ML/TF through the securities market in the ESAAMLG region. This is unfortunate if regard is taken that a number of research projects have already been conducted in respect of ML/TF in the securities markets by other regions and organisations such as FATF (2003 and 2009), MONEYVAL (Eastern Europe) (2008) and Asia/Pacific Group (2009). In short, the research done in these projects established that securities markets can be used as one of the vehicles for ML/TF. This adds to the need for this study to establish if securities in the ESAAMLG region are being used for ML/TF activities. The fact that ESAAMLG securities markets’ trading platforms are manual or semi-automated, also raises the possibility of illicit proceeds being laundered through the sector, undetected.

1.1.3. Research objectives, scope and focus

The scope of the study is from a regional perspective and focus is on the current eighteen (18) ESAAMLG Member countries. These are Angola, Botswana, Comoros, Ethiopia, Kenya, Lesotho, Malawi, Mauritius, Mozambique, Namibia, Rwanda, Seychelles, South Africa, Swaziland, Tanzania, Uganda, Zambia and Zimbabwe. The scope of the study was covered through questionnaire which was designed to focus on the following areas:

3 The definition: Various securities legislation from the ESAAMLG member countries
• Overview of ESAAMLG’s securities sector;
• Licensing, supervision, preventive measures and sanctioning system of securities investment service providers in the ESAAMLG member countries;
• Current and planned mitigation measures;
• ML/TF threats;
• Law enforcement and investigative authorities;
• International Cooperation;
• Overall securities sector risk assessment

The study was informed by input from ESAAMLG member countries’ various securities market stakeholders such as policy makers, regulators/competent supervisory authorities, SROs, LEAs, FIUs and securities market participants (stockbrokers, dealers, custodians, settlement agents, stock exchanges), among others.

In addition, the research analysed a series of operations taking place in the ESAAMLG regional financial markets in order to point out the vulnerabilities existing in the securities markets.

Some of the questions that were posed to member countries which informed this project included the following:

• What are the main sources of funds being invested in the securities market in the ESAAMLG region?
• What is the predominant mode of settlement for securities transactions?
• Which ML/FT risks and red flags are prevalent in the ESAAMLG region’s securities markets?
• What are the ML/FT risk prevention mechanisms?
• What awareness raising measures are being put in place in respect of mitigating the ML/FT risks in the securities industry?
• In what ways are illegal proceeds of crime being laundered through the securities market in the ESAAMLG region?
• What measures are being undertaken by ESAAMLG member countries to counter ML/TF risks in the securities industry?
1.1.4. Benefits of the study

As stated under the problem statement, the region has not undertaken any research in the area of ML/TF in the securities market. The study intended to identify ML/TF risks that existed in the ESAAMLG securities industry. The identification of risks and means which money launderers may be using was to assist local, regional and international stakeholders to appreciate the extent of vulnerability in this sector. This was in turn to assist responsible authorities in developing informed and effective ML/FT counter measures to ensure regional financial stability.

Specific benefits of the study include the following:

- Securities market intermediaries will be able to develop appropriate tools for combating ML/TF through the sector;
- The study will assist in developing supervision manuals for the securities market and the adoption of a risk based approach to AML/CFT supervision;
- Results of the study will help Governments in coming up with informed policy decisions and prioritized allocation of resources;
- Ensure member states appreciate the ML/TF vulnerabilities inherent in the securities industry; and
- The study findings will serve as a sector specific risk assessment, which may provide input to member states when they are conducting their national risk assessment during the Second Round of Mutual Evaluation exercises.

1.2. PART B: RESEARCH METHODOLOGY

Part B describes the methods that were adopted in gathering information for the study. It discusses the research philosophy; the methods and instruments used in the study to obtain information. Further, it explains the limitations, validity and reliability of the study.

1.2.1. Research Philosophy

Exploring of money laundering and terrorism financing concepts, conditions and relevance is mostly qualitative but in this study quantitative aspects relating to
availability of company systems were also considered. A descriptive survey was used to improve on the qualitative information analysed for the study.

1.2.2. Research Method

1.2.2.1. Desk research/Archival records
AML/CFT case studies, previous typologies, and jurisdictional publications regarding ML/TF in the securities market were studied to provide a basis to work from. This aspect will be elaborated on in Chapter 2 below.

1.2.2.2. Questionnaire
The study used the questionnaire to gather information and to investigate ML/TF activities, risks and trends in the securities sector of ESAAMLG member countries. The questionnaire had both structured4 and unstructured5 questions. The questions were styled in a non-technical manner so as to avoid ambiguity and increase the turnaround time. The covering note to the questionnaire provided the objectives of the research and an explanatory note to all the sections of the questionnaire. The detailed questionnaire was circulated through the ESAAMLG Secretariat to expert executives of the securities sector in the ESAAMLG member countries through their regulatory authorities.

1.2.3. Analysis
The questionnaires, AML/CFT case studies, previous typologies, and jurisdictional publications were analysed with the view to address the focus of the typology project as stated above. With regards to the quantitative analysis, the project team utilized Microsoft Excel to sort, interpret and display data in the report. Therefore, the presentation of data in this study is a descriptive narration, which is a qualitative analysis of data. The quantitative techniques included using tables and bar graphs to present data.

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4 Structured questions are precise questions that require a “Yes” or “No” answer or where the respondent choose between a number of options like ‘agree’ or ‘do not agree’
5 Unstructured questions gave the member countries room to explain their answers in terms of context
1.2.4. Limitations

The Project Team faced limitations in the study especially at the data collection stage as other member countries were reluctant to contribute sensitive information in relation to their AML/CFT experiences and case studies related to the securities sector.

1.2.5. Validity and Reliability

To safeguard against invalid or unreliable data, the project team used a sample of 7 responses to the questionnaire provided to the project team member countries to test the validity and reliability of the questionnaire. Pre-testing helped in correcting errors and improving the quality of the responses to the questionnaire. This enabled data collection to be done using only the improved tool to ensure validity and reliability of information collected.
2. CHAPTER 2: ANALYSIS AND FINDINGS

2.1. INTRODUCTION

This chapter presents the findings derived from the analysis of the data provided in response to the questionnaires distributed to countries as well as the examination of archival records. Out of 18 administered questionnaires, a total of 14 questionnaires were completed and returned, thus showing a response rate of 78% which is a fair representation of the region.

In the sections that follow, the findings of the project team will be dealt with under separate headings as per the questionnaire.

2.2. OVERVIEW OF THE SECURITIES SECTORS IN THE ESAAMLG REGION

In most ESAAMLG member countries, the following securities investment service providers operate: CIS managers, Securities Exchanges, Securities Dealers, Stock Brokers or Stock Broking firms, Central Securities Depositories, Custodians, Trustees, Asset Managers and Investment Advisers. Kenya is the only jurisdiction in the region that offer specific additional securities facilities namely REIT manager and Investment Banks.

The securities market structure in the ESAAMLG region is shown in Table 1.
Table 1. Securities Market Structure in ESAAMLG Region

There are a number of securities investment service providers in the region. The study indicates adequate supervision of these securities investment service providers by their competent supervisory authorities on AML/CFT to prevent proceeds of ML/TF from entering the sector. In terms of the FATF Recommendations 6 the competent supervisory authorities should ensure that these financial institutions are adequately supervised on AML/CFT to prevent illicit money from entering the sector.

Securities investment service providers that conduct their services through agents are as illustrated in Figure 1.

![Figure 1: Securities investment service providers conducting services through agents](image)

The study reveals that 43% of the countries in the ESAAMLG region that responded to the questionnaire use agents to conduct business and for the remaining 57% of the countries, their respective laws prohibit the use of agents. In this regard, the project

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6 Recommendation 26: Regulation and supervision of financial institutions and Recommendation 27: Powers of supervisors-
team noted the possibility of an increased risk of ML through the use of agents in the event that the said agents are not properly monitored for purposes of AML/CFT and are not subject to AML/CFT requirements.

Furthermore, the common finding among countries that use agents indicates that there is a high frequency of agents ignoring AML/CFT requirements in an effort to earn high commissions through large numbers of clients/customers.

Table 2 depicts the Market Turnover/Gross Domestic Product of the securities markets in the various jurisdictions.

<table>
<thead>
<tr>
<th>Country</th>
<th>GDP USD</th>
<th>TURNOVER VALUE USD</th>
<th>%</th>
</tr>
</thead>
<tbody>
<tr>
<td>Botswana</td>
<td>34 377 000 000</td>
<td>265 580 004</td>
<td>0.77%</td>
</tr>
<tr>
<td>Kenya</td>
<td>125 700 000 000</td>
<td>36 356 050 000</td>
<td>28.92%</td>
</tr>
<tr>
<td>Lesotho</td>
<td>4 264 000 000</td>
<td>-</td>
<td>0.00%</td>
</tr>
<tr>
<td>Malawi</td>
<td>6 300 000 000</td>
<td>27 000 000</td>
<td>0.43%</td>
</tr>
<tr>
<td>Mauritius</td>
<td>12 066 000 000</td>
<td>515 540 000</td>
<td>4.27%</td>
</tr>
<tr>
<td>Mozambique</td>
<td>16 880 000 000</td>
<td>109 000</td>
<td>0.00%</td>
</tr>
<tr>
<td>South Africa</td>
<td>381 000 000 000</td>
<td>375 004 000 000</td>
<td>98.43%</td>
</tr>
<tr>
<td>Swaziland</td>
<td>3 388 996 139</td>
<td>2 685 317</td>
<td>0.08%</td>
</tr>
<tr>
<td>Tanzania</td>
<td>33 230 000 000</td>
<td>212 220 000</td>
<td>0.64%</td>
</tr>
<tr>
<td>Uganda</td>
<td>23 590 000 000</td>
<td>177 990 000</td>
<td>0.75%</td>
</tr>
<tr>
<td>Zambia</td>
<td>26 000 000 000</td>
<td>1 101 450 000</td>
<td>4.24%</td>
</tr>
<tr>
<td>Zimbabwe</td>
<td>14 015 000 000</td>
<td>452 900 000</td>
<td>3.23%</td>
</tr>
<tr>
<td>Namibia</td>
<td>12 340 996 000</td>
<td>765 681 692</td>
<td>6.20%</td>
</tr>
<tr>
<td>Seychelles</td>
<td>1 268 018 738</td>
<td>5 713 101</td>
<td>0.45%</td>
</tr>
</tbody>
</table>

Table 2. Securities Market Turnover/Gross Domestic Product

In terms of the data reflected in Table 2, the study findings in this table reveal that the securities market turnover as a percentage of GDP range from 0.08% to 98.43%. Thus,
in some jurisdiction it is negligible and the findings are important for the development of the securities market in the region. The securities market is one of the barometers for the performance of any economy and the development in this area goes hand in hand with efforts by supervisory authorities in putting a detailed AML/CFT policy framework in place. At the time of the study, Lesotho had not yet established a Securities Exchange and the Mozambican Securities Exchange had been established but still with limited activity.

Table 3 sets out the securities market turnover vs. foreigner participation (Bought and sold) for the year 2014.

<table>
<thead>
<tr>
<th>Country</th>
<th>Turnover (USD)</th>
<th>Foreigner participation (USD)</th>
<th>%</th>
</tr>
</thead>
<tbody>
<tr>
<td>Botswana</td>
<td>265 580 004</td>
<td>82 795 194</td>
<td>31.18%</td>
</tr>
<tr>
<td>Kenya</td>
<td>36 356 050 000</td>
<td>1 186 180 000</td>
<td>3.26%</td>
</tr>
<tr>
<td>Lesotho</td>
<td>-</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>Malawi</td>
<td>27 000 000</td>
<td>4 694 720</td>
<td>17.39%</td>
</tr>
<tr>
<td>Mauritius</td>
<td>515 540 000</td>
<td>192 595 000</td>
<td>37.36%</td>
</tr>
<tr>
<td>Mozambique</td>
<td>109 000</td>
<td>-</td>
<td>0.00%</td>
</tr>
<tr>
<td>South Africa</td>
<td>375 004 000 000</td>
<td>71 952 500 000</td>
<td>19.19%</td>
</tr>
<tr>
<td>Swaziland</td>
<td>2 685 317</td>
<td>-</td>
<td>0.00%</td>
</tr>
<tr>
<td>Tanzania</td>
<td>212 220 000</td>
<td>1 696 760</td>
<td>0.80%</td>
</tr>
<tr>
<td>Uganda</td>
<td>177 990 000</td>
<td>-</td>
<td>0.00%</td>
</tr>
<tr>
<td>Zambia</td>
<td>1 101 450 000</td>
<td>46 791 184</td>
<td>4.25%</td>
</tr>
<tr>
<td>Zimbabwe</td>
<td>452 900 000</td>
<td>239 500 000</td>
<td>52.88%</td>
</tr>
<tr>
<td>Namibia</td>
<td>765 681 692</td>
<td>-</td>
<td>0.00%</td>
</tr>
<tr>
<td>Seychelles</td>
<td>5 713 101</td>
<td>462 292</td>
<td>8.09%</td>
</tr>
</tbody>
</table>
**Table 3. Securities Market Turnover vs. foreign participation (bought and sold) for the year 2014.**

It is the project team’s view that there is a disparity in the participation of foreigners in the various securities markets. In some countries, it is low and in others relatively high, with one country having a relatively high rate of over 50%. In addition, the study also reveals that there are three jurisdictions where the foreign participation in value is also relatively high. For example, in SA this is USD71 952 500 000. The common study findings reveal that, the level of foreign participation is high in value in the region. The supervision by SMRs was considered to be adequate considering the nature and way of trading allowed by most countries. To enforce and strengthen AML/CFT supervision of trading by foreigners and to prevent any possible ML/TF activities by foreigners, jurisdictions allow movement of money for trading in securities to be done through normal banking channels with strict KYC and CDD requirements.

Figure 2. indicates the number of dual/cross listed companies per individual jurisdiction.

![Figure 2. Dual listed /Cross listed Companies](image)
Indications from the study depicted in the graph in Figure 2 show that majority of the member countries have a low level of dual listings, which creates the impression that ML through the transfer of shares from one jurisdiction to another could still be of low risk in the Region.

2.3. MARKET ENTRY REQUIREMENTS AND SUPERVISION FRAMEWORK

2.3.1. Licensing

The study findings establish that all the countries make it mandatory that securities investment service providers be licensed with the local SMRs before they can operate. A few jurisdictions still have the regulatory functions falling under the ambit of the Central Bank/Reserve bank. All countries have enacted legislation to regulate the activities of securities investment service providers, including regulations. Further findings indicate that there are basic requirements for licensing each class/category of securities investment service providers/intermediaries.

The requirements for licensing securities investment service providers for most countries in the region seem to be generic requiring at minimum:

- Fit and proper requirements, for example: qualities of honesty and integrity, competence, operational ability, financial soundness;
- Management and Governance Structure, for example: Board Charter, Organizational Structure; and
- Internal Controls, for example: procedure manuals and risk management framework.

The study reveal that most of the countries did not require the applicant for business to indicate sources of funds to be used or used in establishing the business as part of requirements at initial licensing stage. This raises concern as it leaves possibilities of bringing in businesses which could have been fully or partly funded by illicit proceeds from crime. Integrity issues concerning funding should not only apply to the business activity as a company investment service provider but should also be fully scrutinised at
the licensing stage to determine the credibility of the capital funding of the business entity.

2.3.2. AML Supervision

Most member countries have supervisory frameworks that assist in detecting, deterring and mitigating ML/TF risks in the sector. A high level of appreciation of the AML/CFT framework was exhibited in all jurisdictions as they have in place AML/CFT laws that require securities investment service providers to have internal policies and controls around AML/CFT enforcement. Staff members are required to be aware of the said policies and controls. It was noted that coverage of the training area varies across different investment entities.

The securities investment service providers are obliged to:

- Identify their customers;
- Verify their identity;
- Request a standard identification document or method;
- Keep records of identification for a period of 5 years at minimum;
- Keep records of transaction documents for a period of 5 years at a minimum;
- Monitor transactions;
- Train their staff on AML/CFT measures;
- Have an internal AML/CFT control function so as to enhance supervision.

Follow ups and periodic compliance checks on licensed securities investment service providers are being done through offsite and onsite surveillance and monitoring, submission of returns, compliance with respect to the conduct of business requirements, continuous compliance with respect to corporate governance requirements, and continuous compliance with respect to AML/CFT obligations, among others. These are the measures that are in place in most member countries in the region to ensure effective AML/CFT supervision.
The study further reveals that AML/CFT supervision is done by FIUs and the SMRs. In most jurisdictions, securities investment service providers are designated as accountable institutions for AML/CFT purposes. The supervision of securities investment services providers in all jurisdictions is carried out by the SMR, and the FIU is responsible for overall AML/CFT regulation by all financial institutions including the securities sector. This arrangement has enabled the SMR and the FIU to at times carry out joint inspections on the securities sector designated institutions. The study also reveals that in the event that an accountable institution makes use of an agent to fulfil some of its obligations, the responsibility for adherence with the provisions of AML/CFT remains that of the accountable institution.

**AML Preventative measures**

The study also shows that the majority of securities investment service providers in the ESAAMLG Region have employed a number of preventative measures to combat ML/FT activities. Some of the preventative measures put in place include:

- Development and implementation of robust AML/CFT policies and procedures;
- Enhanced CDD mechanisms;
- Employing MLROs to develop appropriate AML/CFT compliance systems & procedures,
- Implementing a RBA to supervision,
- Assessing and mitigating AML/CFT risks;
- Increasing and enhancing capacity and skills of staff members through targeted training done within their jurisdictions and internationally.

The findings indicate that, the preventative measures are more or less the same as identified in chapter 3, literature review section 3.6. The ESAAMLG securities sector preventative measures comply with the requirements of FATF Recommendations as explained in the said section 3.6

**2.3.3. Challenges hindering efforts to combat ML/TF activities**
The factors identified in some countries as challenges hindering efforts to combat ML/TF activities in the securities investment service sectors include:

- Limited awareness on SMRs, LEAs (i.e. units dealing with specialized crimes), Securities Services Investment Providers;
- Increased cost of AML/CFT compliance;
- Verification of additional KYC requirements;
- Transition to a RBA to supervision by other member countries;
- The regulatory authorities are still at their early stages;

2.3.4. **Source of funds invested in the securities market**

In most countries the funds invested in the securities market are being derived from pension funds, institutional companies, insurance companies, high net worth clients, small and medium enterprises, savings and foreign investors. However, some jurisdictions indicate that they do not request details on the source of funds invested.

2.3.5. **Participation of Foreign Investors**

Most Countries' laws permit foreign investors to participate in the local securities market but with enhanced CDD applicable to them.

2.3.6. **Cross–border funds transfers**

For most countries in the Region, cross border funds transfers are monitored by the Exchange Control divisions in their Central Banks/Reserve Banks. Further, in jurisdictions where there is a CSD, there is a dual role of monitoring the cross border movement of securities transactions and the securities exchange. The dual monitoring role strengthens the ML/FT requirements since these institutions are recognised as competent supervisory authorities by their respective country laws.

2.3.7. **Penalties**

The study reveals that for most countries, penalties which include fines and/or imprisonment may be imposed on securities investment service providers for non-compliance with the AML/CFT laws. Furthermore, the SMRs themselves have the
power to suspend or revoke licenses for contravening AML/CFT laws. However, jurisdictions were reluctant to provide statistical data on the number and amount of penalties imposed to securities investment service providers on ML/TF offences committed for the past five (5) years.

2.3.8. Payment Methods

The study indicates that the most prevalent payment methods acceptable for securities market transactions during normal trading for most jurisdictions are cash, wire transfer, bank deposit, cheque, electronic funds transfer, and of late the use of mobile payments.

Furthermore, only a few countries have regulations/rules that restrict acceptance of payments made from third party bank account(s) for securities market transactions. Third party payments are seen to have potential to conceal ML/TF activities.

2.3.9. Clearing and Settlement

The study also shows that Botswana, Kenya, Mauritius, South Africa, Malawi, Uganda, Zambia and Zimbabwe have a CSD. South Africa and Mauritius have each two CSD’s in place. In the countries where a CSD is operational, the CSD is relied upon to monitor and supervise AML/CFT adherence measures on securities settlement. However, in most countries onsite and offsite inspections by the Securities Market Regulator are done to ascertain compliance with legal and regulatory requirements, including putting measures in place to prevent money laundering and terrorism financing related to the securities settlement system.

The prevalent mode of settlement for securities transactions is electronic; however Botswana and Zimbabwe have both physical and electronic settlement systems. Malawi only has a physical system as the mode of settlement.

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7 The CSD is the entity that clears and settles securities trades.
The settlement cycle in most jurisdictions is at T+3\(^8\), with only a few at T+5 or T+7 with respect to certain securities-fixed income securities.

2.3.9.1. **Challenges on the clearing and Settlement**

According to the study, in some jurisdictions where the CSD is operational, challenges experienced include:

- The securities settlement system having been designed some years back to facilitate clearing and settlement of securities only, with no other modules envisaged to address AML/CFT issues;
- The difficulty of picking/identifying AML/CFT issues as the CSD records rely heavily on the information from the trading platform and the brokers, hence the CSD has no opportunity to conduct its own CDD;
- Reporting of suspicious transactions as the transactions are initiated at the stage of engaging a broker and dealer. The settlement system is the final part of the transaction.

In a few countries where no CSDs are present, the system in place is manual, and it is not linked to an FIU reporting system. In most of the jurisdictions the settlement system is not linked to a Real Time Gross Settlement System (RTGS). However, where some of these jurisdictions are supervised by the competent authorities, they have appropriate systems for reporting and settlement of securities.

2.3.9.2. **Mitigating measures on the clearing and settlement**

The study indicate the following as mitigating measures being taken in some of the member jurisdictions to enhance their clearing and settlement regimes:

- Upgrading of the system to make it more effective in the clearing and settlement of securities;
- Enhancement of automation of the KYC/CDD process;

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\(^8\) T+D “means trade date” in our case T+3 is trade date plus three days. When an investor buys securities, payment must be received by a brokerage firm no later than three business days after the trade is executed.
• Putting in place a clearing house with structures which can be subjected to AML/CFT requirements;
• Enhancement of surveillance of the CSD by the SMR and the CSD participants who undertake transactions on behalf of brokers.

2.4. CURRENT AND PLANNED MITIGATING MEASURES IN RESPECT OF STRS

2.4.1. Monitoring and reporting mechanisms for STRs
The study establish that most member countries have monitoring mechanisms such as monitoring of client transactions, client sources of funds, supervision and surveillance of securities trades.

It further reveals that seven (7) countries use electronic reporting mechanisms for reporting STRs whilst one country has a manual mechanism and five (5) countries do not have any mechanism in place.

The study notes that SMRs for purposes of AML/CFT are not STRs reporting institutions. However, MLROs for securities investment service providers are required to report STRs to their respective FIUs.

2.4.2. Transaction records
The study reveals that transaction records that facilitate AML/CFT screening and monitoring are available in many jurisdictions. In addition, in the ESAAMLG region records are kept between five (5) to ten (10) years. This could be a contributor as to why according to the study ML/TF in the securities market sector was generally found to be low.

2.4.3. STRs filed over the last five (5) years from the securities market
The study findings indicate that eight (8) countries that include Botswana, Kenya, Lesotho, Mozambique, Swaziland, Uganda, Seychelles and Zambia did not report STRs from the securities sector over the last five years and even prior to that. Mauritius did not disclose. The countries that reported STRs from the securities sector were as follows:
• South Africa reported 231 with unknown amounts.
• Malawi reported 21 cases worth USD 150,000;
• Zimbabwe reported 15 STRs cumulatively worth USD 3,315,074.4;
• Namibia reported 8 STRs worth USD 2,316,400.58; and
• Tanzania reported 1 STR worth USD 947.42.

Table 4 indicates the total number of STRs reported in the ESAAMLG region for the past five (5) years.

<table>
<thead>
<tr>
<th>SECURITIES SERVICE PROVIDERS</th>
<th>NO OF STRs</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>2010</td>
</tr>
<tr>
<td>CIS</td>
<td>0</td>
</tr>
<tr>
<td>Brokerage firms</td>
<td>21</td>
</tr>
<tr>
<td>Asset Management Firms</td>
<td>1</td>
</tr>
<tr>
<td>Securities Exchange</td>
<td>0</td>
</tr>
<tr>
<td>Custodian</td>
<td>0</td>
</tr>
<tr>
<td>Securities Transfer Secretaries</td>
<td>0</td>
</tr>
<tr>
<td>Total</td>
<td>22</td>
</tr>
</tbody>
</table>

Table 4. Number of STR’s reported

The study findings indicate that, of the 276 STRs reported to FIUs in the past five years, no STR related case has been prosecuted and convicted. In all the jurisdictions, the prosecutions and convictions are low due to inadequate training, inadequate forensic facilities and expertise in handling securities related cases. The main perpetrators are: individual investors, securities intermediaries, organized crime syndicates and shareholders.

The observations made from the study are that the increase in the number of STR’s in 2012 might have been due to the coming into effect of the new FATF
Recommendations which could have increased awareness on AML/CFT requirements to the securities market sector

2.4.4. Money laundering methods

The study’s findings indicate that the following methods are used to launder money through the securities industry:

- High value bank transfer deposits into asset management company, which is a possible Layering method;
- Fraudulent change of ownership of shares, fraudulent misrepresentation and connivance on transfer of securities of listed companies.

The STR information made available to the study, indicate the possible ML activities through the securities sectors to include:

- Series of (repetitive) transactions;
- Use of familiarity with brokers;
- Irregular high value investment through Asset Management; and
- Fraudulent change of share ownership.

The study also establishes that there are no ML/TF linkages across borders from the available STR information. Furthermore, there was no extra-territorial assistance on STRs sought from competent supervisory authorities (FIUs, etc) in other countries.

The following case studies were provided by some of the jurisdictions:

2.4.4.1. Case study: A

High Value cash deposits, multiple deposits and transfer in various accounts (possible Layering method)

Description of Activity:

Staff member employed by a Bank. The pattern of transactions through the account were characterised by high value cash deposits, multiple deposits and transfers to the Asset Management Company unit trust High Interest account. Upon enquiry, the staff member advised that she is into commodity broking which conflicted with information she had given to the Asset Management team which reported that she was in the transport business together with the
husband. Transactions through the staff account amounted to USD 137,000.00 during a one year period.

**Reasons for Suspicion:** High value transactions through the staff account and multiple deposits. The inconsistency between staff salary and account activity and the use of staff account for business transactions

**Action Taken:** Staff member advised to desist from using staff account for business transactions. An STR was filed with the FIU.

**Date Reported:** 15 January 2014

2.4.4.2. Case study: B

**High Value Deposit into Asset Management**

**Description of Activities:**

Client employed by a local University as a salaries and benefits administrator. The client invested USD 135,000.00 between March 2012 and September 2013 through Asset Management. During April 2013, a subpoena was issued advising the bank to freeze accounts of the salaries and benefits administrator and to provide statements covering the period September 2009 to April 2013 to which the bank complied.

**Reason for Suspicion:** High value deposits inconsistent with source of funds declared upon account opening. High value deposits inconsistent with current salary as a Salaries and Benefits Administrator. Failure by the client to explain his sources of funds upon enquiry by the bank. A court order was issued compelling restitution of funds to the university.

**Action Taken:** The bank complied with both the subpoena and court order. An STR was filed with the FIU. The jurisdiction did not disclose the nature of the case.

**Date Reported:** 20 September 2013

2.4.4.3. Case study: C

**Fraudulent change of ownership of shares**

**Description of activities:**

An employee allegedly connived with an outsider (relative) to transfer shares of shareholders who had their mails returned due to their mail boxes being closed. Fictitious documents were created to facilitate the transfer of the shares including fake IDs, forged signatures. The total prejudice of the 3 cases in 2013 was discovered at the same time and a total amount of USD253, 603 was involved. One of the parties defrauded was an ex- Football official now based in a Foreign Country.
**Action Taken:** The matter was reported to the police for further investigation and the trial is ongoing. The matter was reported to FIU and the Competent Supervisory Authority.

**Type of Instrument:** Ordinary shares

2.4.5. **Underlying crimes or predicate offences**

The study points out from the few cases available, the crimes of tax evasion and corruption as the main underlying crimes or predicate offences in the securities sector. It should be noted in this regard that, the literature review indicated that, predicate offences for ML/FT include insider trading, market manipulation and offering fraud through Ponzi schemes.

This sector may be attractive to criminals to launder their illicit proceeds due to the use of cash, large values of transactions, possibility of omitting CDD measures, complex products, speed of execution of transactions and international nature of securities market through participation of foreign investors.

The following AML/CFT weaknesses create opportunities for money launderers to exploit the securities market sector:

- Lack of compliance with KYC principles due to lack of a national identification system;
- High volumes of transactions;
- Use of cash as payment mode;
- Lack of modern AML/CFT software and limited AML/CFT awareness; and
- The lack of appropriate planning in residential areas making verification of physical addresses difficult.

However, results of the study show the threat of ML on average to be low in the region. Certain factors which were apparent from the study seem to be minimizing the threat. These factors include:

- The level and size of securities market development at ESAAMLG region level;
- Problems with the liquidity of some securities traded (low demand for them);
• Strict regulations;
• Adherence to international standards when adopting the regulations; and
• Robust and consistent implementation of AML/CFT supervision program.

The study indicates, based on the above factors, most of the monitoring systems in the ESAAMLG region to be relatively effective.

2.4.6. Large cash transactions

Ten (10) countries that include: Botswana, Kenya, Lesotho, Malawi, Mauritius, Mozambique, Namibia, South Africa, Uganda, and Zimbabwe have a requirement for LCR which also covers securities market sector. Seychelles, Swaziland and Zambia do not have a requirement for LCR. Tanzania has a requirement for banks but not securities investment service providers. For the member countries that do not have such requirements in place, it creates gaps in applying the same level of monitoring of LCRs in the region. For those countries that have LCRs requirements in place the LCR limit is pegged at a minimum of USD 2,500 upwards, and the securities market sector in most of the countries file LCRs with their respective FIUs.

2.5. ML/FT THREATS

2.5.1. Frequent investors

The study findings indicate that most frequent clients in the securities industry in majority of the countries are: individuals in general, PEPs, foreign investors, high net worth individuals, clients with offshore business interests, fund managers, pension/provident funds, investment clubs, and insurance companies. This finding is an indication of the literature review reported section 3.3, below.

2.5.2. Predicate offences
The most common predicate offences to money laundering as cited in the literature review on section 3.2 are those involving insider trading, market manipulation, fraud and corruption. However, the extent of the above mentioned problem was found to be minimal, in that fewer jurisdictions reported incidences of fraud and none reported incidences of insider trading, market manipulation and corruption in the securities market.

2.5.3. **Incidences of terrorism**

From the information submitted, the risk of terrorism/terrorist financing related to the securities market was found to be very low. The study further reveals that, where incidents of terrorist activities were recorded in some jurisdictions, they were not related to the securities sector. In light of this, hereinafter, this aspect is not considered further in the body of this report. However, the analysis of the relevant section of the questionnaire on TF is attached as **Annexure 1**.

2.6. **LAW ENFORCEMENT AND INVESTIGATIVE AUTHORITIES**

The law enforcement/investigative authorities in the securities market should have the authority to investigate accountable and reportable institutions.

2.6.1. **Dedicated Securities Sector specialised investigations units**

Most of the jurisdictions within the region either have dedicated LEAs or specialised units within an LEA dedicated to investigate ML / TF cases in the securities market.

The relevant investigative units of all the jurisdictions that participated in the project indicated that they have multi-disciplinary groups specialising in investigations aimed at combating ML/TF in the securities investment sectors. However, upon closer scrutiny it appears that some jurisdictions’ investigative resources in this area form part of the more general mandate of criminal investigative authorities such as the Police Force and commercial crime units of LEAs within jurisdictions.

2.6.2. **Special Investigative techniques**
Most of the jurisdictions utilise special investigate techniques to combat ML/TF in the securities investment service sectors. The techniques most used are: 60% of the jurisdictions indicated tracing and recovery of proceeds of crime and 58% of the jurisdictions highlighted monitoring of money remitted/currency exchanged transactions. The techniques are illustrated in figure 3.

![Figure 3. Special Investigative Techniques](image)

2.6.3. Other investigative powers

The aforementioned special investigative techniques are complimented by the wide ranging investigative powers the LEAs and investigative authorities of the ESAAMLG member jurisdictions have when carrying out investigations on ML/TF related to the securities service sectors. These powers include

- Power of access to premises and to examine records;\(^9\)
- Power to freeze assets;\(^10\)
- Power to examine witnesses;\(^12\)

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\(^9\) The powers listed under this section were recorded as provided by the various jurisdictions in their specific responses to this question.

\(^10\) Uganda, South Africa, Seychelles, Malawi, Kenya and Botswana reflected this power in their questionnaire.

\(^11\) Uganda, South Africa, Seychelles, Kenya and Zambia reflected this power in their questionnaire.
- Power to seize assets;\textsuperscript{13}
- Search and seizure powers;\textsuperscript{14}
- Power to forfeit assets.\textsuperscript{15}

Figure 4. LEAs Other Investigative Powers

\textbf{2.6.4. Collaborative approach in respect of investigations}

There is strong collaborative approach within the various jurisdictions in respect of investigations. Almost all the jurisdictions confirmed that their LEAs co-operate with the FIUs and regulatory authorities with the investigation of cases.

\textbf{2.6.5. Challenges when conducting investigations}

Figure 5 below, sets out the percentage of jurisdictions that indicate that they are experiencing a particular challenge when conducting investigations related to ML/TF in

\textsuperscript{12} South Africa, Kenya, Tanzania and Mauritius reflected this power in their questionnaire.
\textsuperscript{13} Uganda and South Africa reflected this power in their questionnaire.
\textsuperscript{14} South Africa, Zambia, Tanzania, Mauritius and Zimbabwe reflected this power in their questionnaire.
\textsuperscript{15} Uganda and South Africa reflected this power in their questionnaire.
the securities investment service sectors. Of note are the following two major challenges: inadequate training and expertise listed by 100% of the jurisdictions and 80% of the jurisdictions indicated inadequate forensic facilities.

![Challenges on conducting investigations](image)

**Figure 5: Challenges on conducting investigations**

The main challenges that the securities industry in the ESAAMLG region face are the complexity of the products traded and the different methods used in the settlement of these products with each having specific settlement dates. The securities sector requires specialist knowledge, which few FIU and LEAs currently have, given the fact that the securities market industry in the ESAAMLG region is still not highly mature and sophisticated. The challenges encountered are further enhanced with the few exchange of information that has been noted between jurisdictions.

The study also notes that in some jurisdictions, predicate offences related to the securities market are not adequately defined and moreover the reporting obligations of suspicious transactions have to be submitted on a first rank basis to the relevant regulator, which eventually submit same to the law enforcement authority. The
channelling of the relevant information is delayed due to the double reporting obligations.

Under these instances, it is not clear whether the reporting institutions are aware of the possibility that there might also be a requirement to report a suspicion of money laundering since the predicate offences are not appropriately defined.

The observation made from the above analysis based on the information submitted by the jurisdictions shows a potential gap in reporting of STRs in member countries' securities sector. This might partially explain the relatively low levels of ML/TF STRs reporting in the securities sector. Furthermore, with limited resources and facilities, the gathering of information is impacted negatively since there is heavy reliance on the regulator who may interpret/analyse the information submitted differently. In addition, there may not be effective mechanisms for the sharing of information with the LEAs interacting only with the regulator and not with the originator of the suspicious transaction. There's a need for a greater understanding of the expectation of all parties involved when filing of STRs and poor coordination are often thought to impede enforcement actions.

2.6.6. Investigations, prosecutions and confiscations of assets

Only two jurisdiction to wit Zambia and Zimbabwe indicate that they have carried out investigations, prosecutions and confiscations of assets in this area. However, same seem to have been carried out in respect of offences other than ML / TF. In the case of Zambia, they recorded one (1) matter in respect of securities fraud with a confiscation value of USD293 000. Zimbabwe recorded 17 and 12 fraud investigations and prosecutions respectively and one (1) successful confiscation matter with a value of USD 137 000.

Except for Botswana and Uganda who did not provide a response, none of the other jurisdictions carried out investigations, prosecutions and confiscations of assets in this area.
Having regard to the aforementioned, it is apparent that the jurisdictions within ESAAMLG’s region have not carried out any notable investigations, prosecutions and confiscations in respect of ML / TF cases related to securities investment sector. Except for one country, none of the jurisdictions provided reasons for not having conducted any notable investigations, prosecutions and confiscations in respect of ML / TF cases. The study reveals that the following factors may have contributed to this:

- AML/CFT regulation in most of the jurisdictions is still at its early stages. This contributes to the lack of comprehensive information available on money laundering through the securities market for the ESAAMLG region;
- Major challenges which jurisdictions experience in carrying out investigations related to the sector, for example inadequate training, expertise and forensic facilities.

2.7. INTERNATIONAL CO-OPERATION

The FATF Recommendations\(^{16}\) require that countries should ensure that competent authorities effectively provide the widest range of international cooperation in relation to money laundering, associated predicate offences and terrorist financing.

2.7.1. International co-operation in the securities market

As can be seen from Table 5, only two countries indicated that their relevant LEAs and authorities have not dealt with requests for exchange of information from international counterparts in respect of ML/TF cases in the securities investment service sectors. It was also seen that AML/CFT legislation in the ESAAMLG region is still at the developmental stage. This contributes to a lack of comprehensive information available on money laundering through the securities market. Note is also taken that only one country reported notable data in respect of exchange of information. The study did not create the impression of member countries’ failure to keep records of requests for international co-operation as being the reason why statistics provided in this area is low.

\(^{16}\) FATF recommendation 2.
Table 5: International Cooperation

As can be seen from Table 6, the nature of the requests dealt with by the two countries that reported such exchanges relate mainly to exchange of information (request for information).

<table>
<thead>
<tr>
<th>Year</th>
<th>Country A Sent</th>
<th>Received</th>
<th>Country B Sent</th>
<th>Received</th>
</tr>
</thead>
<tbody>
<tr>
<td>2010</td>
<td>1</td>
<td>1</td>
<td>2010</td>
<td>1</td>
</tr>
<tr>
<td>2011</td>
<td>1</td>
<td>1</td>
<td>2011</td>
<td>32</td>
</tr>
<tr>
<td>2012</td>
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<td>1</td>
<td>2012</td>
<td>33</td>
</tr>
<tr>
<td>2013</td>
<td>4</td>
<td>59</td>
<td>2013</td>
<td>42</td>
</tr>
<tr>
<td>2014</td>
<td>34</td>
<td>42</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Table 6: Request for information

From table 6, it was noted that a request of information is sent on the first instance and further to that request a joint investigation is coordinated, hence the low incidence of
joint investigation. However, based on the statistics submitted above, there is concern that a joint investigation could raise other issues than ML/TF related and which might have negatively impacted on the statistics submitted.

2.7.2. Challenges on information request

Only Kenya and Mauritius indicated that their relevant LEAs and securities authorities have dealt with requests for exchange of information from international counterparts in respect of ML/TF cases in the securities investment service sectors. Furthermore, Kenya and Mauritius were the only jurisdictions that provided details of challenges they experience in respect of this area. Although, it may not be seen as a representative sample of the region, the challenges noted by these jurisdictions are stated below:

- Differing operating standards, and powers of individual FIUs/LEAs. In other words, there is a need for harmonisation/standardisation;
- Differing quality and credibility of information exchanged.
- Late or no responses to requests, insufficient/low quality of responses, rejected requests;
- Lengthy and complicated (time-consuming) procedures for implementation of MoUs and other agreements on international cooperation;
- Lack of proactive/spontaneous information exchange;
- Disparity in resources between larger and smaller jurisdictions – cooperation should take on the form of joint investigations;
- Concerns that the untimely release of sensitive unsubstantiated regulatory and ongoing investigation data could jeopardize an investigation and existing sources of information;
- Concern as to the varying degrees to which each jurisdiction is obligated to protect regulatory information - the release of regulatory data to entities or individuals without regulatory authority.

The following case studies were provided:

2.7.2.1. Case Study: D
USE OF INTERNATIONAL COOPERATION FOR COMBATING ML/TF IN THE SECURITIES INVESTMENT SERVICE SECTORS

Description of Activities
Following an investigation conducted into the business affairs of a collective investment scheme (CIS) licensed by the relevant regulator, it was noted that the licensee has failed to comply with the Code on the Prevention of Money Laundering and Terrorist Financing, as the Company has not applied appropriate customer due diligence measures. The investigation also revealed that large portions of the funds pooled from investors have been loaned to entities based in other jurisdictions.

Action Taken: The licensee was directed to draw a list of all loans granted by each cell and provide an explanation; conduct a comprehensive CDD exercise on the applicants for business and their principals including the promoters, beneficial owners and ultimate beneficial owners as the case may be of all the cells of the Company in accordance with the provisions of the Code; and not to accept any new investors in the Company until further directions from the Regulator.

Cooperation Sought: The relevant regulator has sought the assistance of several international jurisdictions to gather evidence on the source of funds and to identify the identities of the beneficial owners of the funds being channelled through the CIS.

2.7.2.2. Case Study: E

USE OF DOMESTIC COOPERATION FOR COMBATING ML/TF IN THE SECURITIES INVESTMENT SERVICE SECTORS

Description of Activities
Further to the reports from other LEA and competent authorities, the securities market regulator decided to call upon the directors on first case basis to probe into the business affairs of an intermediary. The directors were requested to provide details of the operations of the company. From the explanations provided, the securities regulator concluded to carry an on-site inspection to verify the operations of the intermediary. The intermediary was licensed to manage a portfolio of securities and to provide advisory services. From the documents reviewed at the time of the inspection, the securities regulator noted that the company intends to invest in securities and for diversification purposes in gold. However, the relevant regulator could not trace any investment carried out as per its mandate.

Cooperation sought: After exchange of information with the domestic authorities and foreign counterparts, it was noted that huge sums were deposited in an offshore bank account and were transiting through several bank accounts of the directors of the Company. A court order was issued to disclose the bank accounts and all the bank transactions of the company.
Action taken: The intermediary was directed to stop taking new clients and to draw a table for the reimbursement of the funds taken from investors.

2.8. OVERALL SECURITIES SECTOR RISK ASSESSMENT

The study reveals that there is awareness on all ESAAMLG member countries on the need to conduct NRA at country level, that supervisors should use RBA to supervision and that at entities/sector level specific RBA should be applied. However, the countries’ legislation has not been amended to make it mandatory.

2.8.1. National risk assessment / Risk based supervision program

The study reveals that, only three jurisdictions to wit Malawi, Namibia and Zimbabwe have conducted an NRA. Most of the jurisdictions which responded have neither completed a NRA nor implemented sector specific risk assessment. Consequently, the implementation of preventative measures such as risk based supervision/assessment which is sector specific is impeded.

Except for five jurisdictions: Lesotho, Mozambique, Seychelles, Tanzania and Zambia, all the other jurisdictions have a risk based supervision program.

In the absence of NRA or sector specific risk assessment, the kind of risks highlighted in response to the questionnaire appear to be based on experience from practicing in the sector which might not necessarily be accurate. However, analysis of the submissions from the few countries that have done NRA provides guidance on some of the risks identified.

2.8.2. ML/TF risks.

As only a few jurisdictions provided details of the types of ML/TF risks that are prevalent in their securities market, said risks were not considered representative of the region. The risks that have been identified by the few member countries include:

- The relative ease of securities transfer;
• The securities industry is also used as a vehicle for generating illicit assets that would eventually have to be laundered;
• Securities fraud and company embezzlement.

2.8.3. Mitigating measures
Analysis of the questionnaire responses indicate that not all jurisdictions have implemented measures which have been taken to address the ML/TF risks associated with the securities market sector and are applying the measures according to the risk identified. These findings are similar to those found in the literature review. Only a few countries implemented mitigating measures such as:

• The establishment of the legal and regulatory framework to meet the ML/TF mandate;
• Enhanced compliance monitoring and surveillance and training of staff;
• Introduction of CSD addresses all the KYC deficiencies through vetting all clients and customers by submitting all the needed documents; and
• General measures.

Having regard to the aforementioned, it appears that most of the jurisdictions have not implemented systems or measures that are able to assist in identifying and detecting the types of risks that can lead to ML/TF through the Securities Markets Sector. Also, most of the jurisdictions have not put in place measures that can mitigate and prevent ML/FT from occurring, which makes these countries susceptible to ML/TF activities.

2.8.4. ML / TF risk ratings in the Securities Market Sector
Figure 6 depicts the general risk ratings in the securities markets of most jurisdictions that rated ML/TF risks. The majority reported that they rate ML/TF risks low and only one rated the risks as medium. No jurisdiction reported a high ML/TF risk. However, Lesotho, Mauritius, Mozambique and Seychelles did not provide the ratings or
assessment of ML/TF risks. The ML/TF risks appear to be based on each jurisdiction’s peculiar circumstances.

Figure 6: ML/TF Risk Ratings

The following are some of the reasons for justifying the responses in respect of the general risk ratings in the securities markets as depicted in the graph above:

- **Low rating:**

  South Africa, Uganda and Zambia indicated a lack of reported cases as the justification for rating ML/TF low in their securities market, with Uganda making special reference to the low reported cases in the areas of fraud, market manipulation and insider trading. Unfortunately, the said jurisdictions did not motivate why the lack of reported cases translates to a low risk rating considering the myriad of reasons that may exist for the lack of reporting.

  Botswana justified their low ratings due to most of their Non-Banking Financial Institutions (NBFIs) that are subsidiaries of international companies that have AML risk management and they are subject to AML compliance locally and internationally, and also the large number of their institutional investors being pension funds whom the source of funds are easily traceable. Namibia has not had any TF threats or suspicion, let alone threats to the securities sector, hence their low rating of ML/FT risks. The low rating given by Tanzania is due to the lack of a national identity card that makes it difficult to identify a person. This will be addressed by introducing the national ID. Another country reported that its NRA preliminary report point out low risk.
The observation above is based on the information submitted; however, this low rating could be linked to the low statistics or reporting of cases in the securities sector.

- **Medium rating:**

  Kenya is the only jurisdiction which reported a medium risk. The justification for the medium rating comprises of the following factors: capital market development, AML/CFT supervision regime, corporate governance, etc.

Except for Mauritius and Mozambique, all jurisdictions reported, the general rating of ML/TF risks that is associated with each securities product being traded in their respective securities market. However, it should be noted that not all jurisdictions rated ML/TF risks in respect of each type of security product traded. Figure 7 illustrates the rating of the ML/TF risks associated with each securities product being traded in the ESAAMLG region:

![ML / TF risks per product](image)

**Figure 7. ML/TF risk ratings per product**

The following are the salient findings of the analysis of the jurisdictions’ responses in respect of the aforementioned graph:

ML/TF risks appear to be low for most of the security products traded in the jurisdictions’ security market. The main reason being that most of the securities aforementioned are not freely traded and have to go through regulated entities/intermediaries that have
robust compliance procedures which is part and parcel of the AML/CFT framework in the relevant jurisdiction.

- Ordinary shares: Malawi, Namibia, South Africa, Uganda, Zambia and Zimbabwe;
- Debentures: Malawi, Namibia, South Africa, Uganda, Zambia and Zimbabwe;
- Unit trusts: Malawi, South Africa, Uganda, Zambia and Zimbabwe;
- Corporate bonds: Malawi, Namibia, Uganda, Zambia and Zimbabwe;
- Government bonds: Kenya, Malawi, Namibia, South Africa, Uganda, Zambia and Zimbabwe;
- Preference shares: Malawi, Namibia, South Africa, Uganda, Zambia and Zimbabwe.

Kenya, Malawi and Namibia rated ordinary shares, unit trusts, corporate bonds, depository receipts and government bonds as being of medium ML/TF risk.

Tanzania is the only jurisdiction that rated ML/TF risks high in securities such as ordinary shares, unit trust, corporate and government bonds. The jurisdiction cited the large cash payments as providing an opportunity for money launderers to channel illegally obtained funds into securities investments, particularly during IPOs. The risk is aided by lack of national identification requirements as well as poor planning of urban settlements/towns/cities making it difficult to trace people's addresses.

2.8.5. Actions to reduce the overall risk of ML/TF

Most of the jurisdictions apply specific types of actions to mitigate the risk of ML/TF through the securities industry. Most of the common measures being applied by the jurisdictions include:

- On-going on-site inspections to assess and monitor compliance
- Capacity building of market intermediaries, regulators and the members of the public.
- Inclusion and recognition of AML/CFT for securities market sectors.
- Collaboration and/or cooperation with stakeholders and regulators;
The identification of clients and citizens through national payment and identity systems. These systems are being used to facilitate the implementation of CDD and KYC measures and this has assisted in the recording and reporting of suspicious transactions.

2.9. RED FLAGS IN THE SECURITIES MARKET SECTOR

The study noted the following red flags:

- Clients refusing to provide information to complete CDD/KYC;
- Funds Transfer and deposit activities that are unexplained; repetitive and unusually large activities;
- Activity that is inconsistent with the customers’ business objective or profile;
- A customer making a large purchase or sale of securities shortly before news is issued that affect the share price;
- A customer engaging in large trading of securities that are illiquid;
- The opening of numerous accounts for different legal entities that the customer controls;
- Acquisition and settlement of bonds using large cash amounts;
- Foreign nationals using locals to acquire securities;
- Foreign nationals using locals as proxies for corporate actions;
- The customer is associated with his/her securities trading activities with that of a PEP or a senior political official;
- The customer withdraws cash or funds after a very short period;
- A broker or customer practicing Churning\(^\text{17}\);
- A holding company listing a shell company;

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\(^{17}\) In the context of securities, churning occurs when a broker engages in excessive buying and selling of securities in a customer’s account chiefly to generate commissions that benefit the broker. Churning also occurs where financial services providers advise their clients to replace an existing financial product with another financial product mainly with the purpose to generate commission and not because such replacement is in the interest of the client.
- Accounts that have been inactive suddenly experiencing large investments that are inconsistent with the normal investment practice of the client or their financial ability;
- Client using securities or futures brokerage firm as a place to hold funds that are not being used in trading of securities or futures for an extended period of time and such activity being inconsistent with the normal investment practice of the client or their financial ability;
- Client wishing monies received through the sale of shares to be deposited into a bank account rather than a trading or brokerage account which is inconsistent with the normal practice of the client;
- The entry of matching buying and selling of particular securities or futures contracts (called match trading), creating the illusion of trading;
- Transfers of funds or securities between accounts not known to be related to the client;
- Several clients open accounts within a short period of time to trade the same stock.
3. CHAPTER 3: REVIEW OF RELATED LITERATURE

3.1. INTRODUCTION

AML/CFT case studies, previous typologies, and jurisdictional publications regarding ML/TF in the securities market (related literature) were studied to provide a basis to work from.

In essence, this section reviews related literature on main sources of funds being invested in the ESAAMLG securities market and possible linkages with ML/TF activities, ML/TF risks and red flags that are prevalent in the securities market, awareness of the ML/TF risks in the securities market to local, regional and international stakeholders, and methodologies used by money launderers in the securities market to launder proceeds of crime. It first focuses on the definitions of money laundering and the money laundering designated offences in the securities market. The chapter also addresses the measures being undertaken by countries to mitigate identified ML/TF risks in securities markets.

3.2. MONEY LAUNDERING DESIGNATED OFFENCES IN THE SECURITIES SECTOR

The FATF glossary includes among the “designated categories of offences”, three offences that are predicate offences to money laundering: insider trading, market manipulation, and fraud. Insider trading and market manipulation are particularly related to the securities market, as is securities-related fraud.

3.3. SOURCES OF FUNDS INVESTED IN THE SECURITIES MARKET AND POSSIBLE LINKAGES TO ML/TF

The main sources of funds invested in the Securities Market include the following:

- Institutional investors both local and international;
- Individual investors both wholesale and high net worth clients;
- Pension Funds both local and international;
- CIS (Unit Trust Funds);
• Hedge Funds both local and international;
• Government treasury departments; and
• Government departments and parastatals.

3.4. **ML/ FT RISKS AND RED FLAGS PREVALENT IN THE SECURITIES MARKET**

According to MONEYVAL (2008) the red flags prevalent in the Securities Market include the following:

3.4.1. **At Account Opening Stage**

- The Customer exhibits unusual concern regarding the firm’s compliance with government reporting requirements and the firm’s anti-money laundering policies, particularly with respect to his or her identity, type of business and assets, or is reluctant or refuses to reveal any information concerning business activities, or furnishes unusual or suspect identification or business documents.
- The information provided by the customer that identifies a legitimate source of funds is false, misleading, or substantially incorrect.
- Upon request, the customer refuses to identify or fails to indicate any legitimate source for his or her funds and other assets.

3.4.2. **Regarding funds for investment**

- The customer attempts to make frequent or large deposits of currency;
- The customer settles in cash close to or at the settlement deadline;
- The customer insists on dealing only in cash equivalents, or asks for exemptions from the firm’s policies relating to the deposit of cash and cash equivalents;
- The customer has unexplained or sudden extensive electronic transfer activity especially in accounts that had little or no previous activity.
3.4.3. When executing transactions

- The customer wishes to engage in transactions that lack business sense or apparent investment strategy, or are inconsistent with the customer’s stated business strategy;
- The customer exhibits a lack of concern regarding risks, commissions, or other transaction costs;
- The customer engages in transactions involving cash or cash equivalents or the other monetary instruments that appear to be structured to avoid the mandatory reporting requirements, especially if the cash or monetary instruments are in an amount just below reporting or recording thresholds.
- The customer requests that a transaction be processed in such a manner to avoid the firm’s normal documentation requirements.

3.5. METHODS USED TO LAUNDER PROCEEDS OF CRIME THROUGH THE SECURITIES MARKET

The three most distinct methods used to launder proceeds of crime are placement, layering and integration.\(^{18}\)

The most common methods used in securities transactions are layering and integration since most law-abiding brokers do not accept cash transactions. During layering the launderer purchases securities with illicit funds transferred from one or more accounts and use the proceeds from selling the securities as legitimate money. (Reuter and Truman, 2006)

\(^{18}\textbf{Integration} \text{ involves reintroducing the illegal funds into the legitimate economy. The funds now appear as clean income. The purpose of the integration of the funds is to allow the criminal to use the funds without raising suspicion that might trigger investigation and pursuit. This is accomplished through the purchase of assets, such as securities or other financial assets, or luxury goods.}

\textbf{Layering} occurs after the ill-gotten gains have entered the financial system, at which point the funds, securities or insurance contract are converted or moved to other institutions, further separating them from their criminal source. The funds can be used to purchase either securities or other easily transferable instruments and then sold through yet another institution.

\textbf{Placement} involves the initial injection of the illegal funds into the financial system or carrying of cash across borders. This can be accomplished by depositing cash into a bank account where large amounts of cash are broken into smaller, less conspicuous amounts and deposited over time in different offices of a single financial institution or in multiple financial institutions. The placement may be accomplished by the cash purchase of a security or a form of an insurance contract.
In reality, the three stages often overlap and the benefit from many crimes including most financial crimes does not need to be ‘placed’ into the financial system. The securities sector is characterized by frequent and numerous transactions and several mechanisms can be used to make proceeds appear as legitimate earnings from the financial market.

Money laundering through the securities market can also be characterised by structuring and breaking down cash deposits into amounts just below the reporting threshold, often referred to as structuring and smurfing.

The establishment of front or shell companies and trusts, and the use of tax havens to disguise beneficial ownership and the purchase of existing business with laundered money for a nominal sum is one of the modern methods used by criminals to pass the funds on to an innocent third party for the original purchase price (McDonnell, 1998).

3.6. ML/FT RISK PREVENTION MECHANISMS IN THE SECURITIES INDUSTRY

The IOSCO has not established separate customer identification or due diligence requirements for the securities firms, brokers or collective investment entities, the customer identification requirements of the FATF Recommendations do apply to the securities (Schott, 2006). In the 40 Recommendations, the FATF has established a number of preventative measures that a country should adopt in the anti-money laundering (AML) area. These are:

- Enhanced KYC and CDD requirements;
- Record Keeping Requirements;
- Suspicious Transaction Reporting;
- Cash Transaction Reporting;
- Balancing Privacy Laws with Reporting and Disclosure Requirements;
- Internal Controls;
- Strong regulation and supervision.
3.7. CHALLENGES ASSOCIATED WITH COMBATING ML/TF IN THE SECURITIES MARKET

Lack of face-to-face interaction between the intermediary and the customer when the account is opened pose a particular challenge which prevents the ability to have an appropriate customer profile. Jurisdictions may permit intermediaries to rely on third parties to perform CDD.

3.8. EFFECTIVE WAYS OF RAISING AWARENESS OF ML/TF THREATS IN THE SECURITIES SECTOR

3.8.1. Appointment of a ML and Compliance Officer (‘MLCO’)  
Accountable and reporting institutions should create, implement, maintain and monitor procedures of the operating systems and control in order to identify risks arising and take the necessary steps.

3.8.2. Having an AML Manual and Employee Training  
Accountable and reporting institutions’ AML and TF practices, procedures and measures and appropriate training should be dispensed to the relevant staff.

3.8.3. Reporting of internal and external STRs  
Accountable and reporting institutions and employees are obliged to comply with internal and external reporting requirements as well as cash transaction reporting to the appointed and relevant authorities.

3.8.4. Implementing a risk based approach  
Accountable and reporting institutions should incorporate into their policies and procedures a RBA in order to manage risks in an effective and affordable way. The RBA includes the identification, recording and evaluation of a combination of triggers and indicators of various risks which may be related to ML and TF.
4. CHAPTER 4: RECOMMENDATIONS AND CONCLUSION

4.1. CONCLUSIONS

The report concluded that:

- Jurisdictions do not establish sources of funds when institutions apply for initial licenses or registration;
- There is limited awareness on AML/CFT by supervisory authorities and LEAs;
- Lack of risk based supervision and increased cost of compliance are the main challenges hindering efforts to combat ML/TF;
- The clearing and settlement modules do not address AML/CFT issues;
- The common method of ML appears to be fraudulent change of ownership of shares;
- Member countries did not report on any incidences of TF in the securities market sector;
- There is a lack of information with regards to reporting of suspicious transactions in the securities sector. It was noted that jurisdictions have limited resources and facilities, hence the gathering of information is impacted negatively;
- The jurisdictions within the ESAAMLG Region have not carried out any notable investigations, prosecutions and confiscations in respect of ML / TF cases related to securities investment services sector. Except for one country, none of the jurisdictions provided reasons for not having conducted any notable investigations, prosecutions and confiscations in respect of ML / TF cases;
- AML/CFT regulation in the securities market sector in most of the jurisdictions is still in its early stages. This has contributed to the lack of comprehensive information being provided by member countries on money laundering through the securities market for the ESAAMLG region;
- Most jurisdictions have not implemented systems or measures that are able to assist to identify and detect the types of risks that can lead to ML/TF through the securities market sector. Also, most of the jurisdictions have not put in place
measures that can mitigate and prevent ML/FT from occurring, which makes these countries vulnerable to possible ML/TF activities.

4.2. RECOMMENDATIONS

Based on the findings of the analysis as set out in Chapter 2, the project team makes the following recommendations:

- **Regulation**: With reference to the countries that are still regulated under the umbrella of the central bank, there should be sector specific legislation;
- **KYC and CDD**: Jurisdictions should ensure that securities market intermediaries put in place appropriate CDD policies, which should include customer acceptance and KYC norms, including prescribing a standard list of documents which can be accepted as evidence for identity and place of residence of the customer;
- **Source of funds**: Member countries should require the identification and verification of the source of funds prior to the granting of the licence, including verification of source of funds on investment;
- **STRs Reporting**: Jurisdictions should automate their systems for filing of STRs with the FIU;
- **Cash Transaction**: The use of cash to transact on the stock markets should be discouraged;
- **Training and Awareness**: Training and awareness raising and more guidance should be given to the securities sector especially on CDD including STR’s;
- **Cash threshold**: Jurisdictions should enact, as a matter of urgency, cash threshold reporting requirements for the securities market sector;
- **UNSCRs 1267 and 1373**: Jurisdictions should put in place, without delay, procedures and establish structures for freezing the funds or other assets of suspected terrorists. Further, the countries should be encouraged to have mechanisms which enable them to do their own domestic listing when it becomes necessary;
- **Specialised Unit**: Jurisdictions should have dedicated LEAs or specialised units within a LEA dedicated to investigate ML / TF and other financial crimes, including
having the necessary skills and knowledge to adequately investigate cases emanating from the securities market sector;

- **Collaboration between LEAs and competent authorities:** Jurisdictions should enhance collaboration between FIUs, LEAs and other competent authorities on reporting STRs and predicate offences related to the securities market sector.

- **National and international cooperation related to the securities markets:**
  - **Proactive Information Exchange** - There is a need to encourage jurisdictions to sign MoUs to formalize frameworks for sharing information related to the securities market sector.
  - **Joint investigations:** Smaller jurisdictions should adopt policies which allow carrying out of joint investigations with agencies that have the relevant technical skills and the necessary legal authority to give such assistance. Further, joint investigations should be used to control untimely release of information on an open investigation that could jeopardize the investigation & existing sources of information and possibly expose the Regulators to unnecessary liability concerns.

- **RBA:** Countries should implement AML/CFT as a Risk Based Supervision (RBS) program at Regulator and entity level without delay as part of their RBS programme.

- **Measures to identify ML/TF risks:** Jurisdictions should implement systems or measures that are able to assist to identify and detect the types of risks that can lead to ML/TF through the securities market sector.
REFERENCES

Asia/Pacific Group (2008)


MONEYVAL (2008). Eastern Europe


ANNEXIS

ANNEXTURE 1: INCIDENCE OF TERRORISM FINANCING / STRs related to TF / UNSCR 1267 & 1373

The study reveals that the incidences of terrorism financing happened in one jurisdiction during the period under review. In that particular country, the government closed a number of NGOs for alleged fund raising for terrorism. However, there is no evidence indicating that the closed NGOs raised and/or is raising funds through the Securities Market Sector.

The study found that there are no STRs relating to TF that were reported to any of the FIU or the LEA within the ESAAMLG region. In this regard, there were no referrals, prosecutions and/or convictions of STRs related to TF.

The study also found that there is no information available at hand regarding the identity of names of terrorist groups (or those supporting TF activities) involved in TF activities through the Securities Investment Service Sectors.

Further, the study could not identify methods that can be used to finance or advance TF activities within the ESAAMLG securities sectors because there were no STRs related to TF that were reported. As a result the study could not describe the indicators, methodologies, and trends related to possible TF activities through the Securities Markets Sector.

Information provided by member countries for the study did not indicate on whether there are any member countries where there are TF activities through the Securities Market Sector. Further, analysis of the information provided member countries did not indicate underlying sources from which proceeds of crime are derived and channelled through the Securities Investment Service Sectors to advance TF activities.

From the literature, the study noted that the Securities Industry offers a vast array of opportunities for transforming money into a diverse range of assets. For liquid assets, they allow a high frequency of transactions which aid the layering process. Hence,
capital markets has the capacity to attract persons engaged in ML/TF to find a point of entry for their illicit proceeds for eventual integration into the general economy. In addition, the Securities Industry is global in nature and with the increasing developments in technology, payment systems, and other direct gateways into the markets, the speed and the relative anonymity of these avenues make them an option for persons engaged in money laundering and terrorism financing to use with limited chances of direct identification links.

The study further reveals that there are no case studies related to the TF in securities sector. In addition, the threat of TF related to the securities sector could be low due to the mitigating measures most countries are taking which include conducting regular checks on the names of new customers, as well as regular checks on the names of existing customers and potential customers, against the names contained in the UNSCR 1267 list.

The study findings indicate that most countries in the ESAAMLG region have in place procedures/measures which cover including the Securities Markets Sector to freeze without delay the funds or other assets of terrorists, and to ensure that no funds or other assets are made available, directly or indirectly, to or for the benefit of, any person or entity either designated by, or under the authority of the United Nations Security Council under Chapter VII of the Charter of the United Nations, pursuant to which Resolution 1267 (1999) and its successor resolutions have been issued.

The study further reveals that one country in the ESAAMLG region has come up with a domestic list (UNSCR 1373) comprising of individuals and entities facilitating or associated with terrorism, but the listing in not related to securities market.

**ANNEXURE 2: DEFINITIONS OF TERMS USED**
- **Authorized depositories (mostly banks)/Custodians** - A firm that hold securities in custody for another person and dealing with them to the extent necessary under that custodianship.

- **Central Securities Depository** – An entity that holds and administrates securities and enables securities transfers and other transactions to be processed by entries in a record or account. The book entry can either be electronic or otherwise and the securities can be physically held. The holding of securities can either be in certificated or uncertificated (dematerialized) form, to enable the legal (book entry) transfer of securities between owners and entities acting on behalf of owners. In addition ECB Annual Report (2004) reiterates that, a central securities depository may incorporate clearing and settlement functions. It plays an active role in ensuring the integrity of securities issues.

- **Clearing houses** – A clearing house is a financial institution that provides clearing and settlement services for securities transactions.

- **Customer identification and Due Diligence** involves identifying the customer and verifying that customer's identity using reliable, independent source documents, data or information; identifying the beneficial owner, and taking reasonable measures to verify the identity of the beneficial owner, such that the financial institution is satisfied that it knows who the beneficial owner is. For legal persons and arrangements this should include financial institutions understanding the ownership and control structure of the customer and understanding and, as appropriate, obtaining information on the purpose and intended nature of the business relationship.

- **Securities dealing firms (Stockbrokers)** - A company that enters into an agreement on behalf of another person to purchase, sell or, subscribe for or finance a security.

- **Securities Exchange** – Provides a market place for securities dealers to come together to buy and sell securities on behalf of investing public. A securities exchange further provide appropriate machinery to facilitate additional offerings of stocks to the general public and it afford companies opportunities for raising new and fresh capital.
- **Securities Investment advisers**- A firm that gives advice to other persons on their investments in securities or issuing or publishing analyses or reports on securities. Furthermore, the advice will be on behalf of a client, undertaking the management of a portfolio of securities for the purpose of investment.

- **Securities Investment Managers/Fund managers**- A firm that manages another person’s portfolio of investments, where the portfolio consists of securities, money market and other securities traded products.

- **Securities Transfer Secretaries/ Agencies**- A firm that record transfers and other transactions relating to securities on behalf of an issuer of securities.

- **Securities Trustees Firms**- A firm entrusted with securities/ shares through a trustee deed. The categories of shares under a securities trustee are Employee Share Option Scheme, Management Share Option Scheme, Employee Share Trust Scheme and Community Share Trust Scheme among others.