Administrative Measure Publication Notice

This Notice is being published by the Financial Intelligence Analysis Unit (FIAU) in terms of Article 13C of the Prevention of Money Laundering Act (PMLA) and in accordance with the policies and procedures on the publication of AML/CFT administrative measures established by the Board of Governors of the FIAU.

The Notice provides select information from the FIAU's decision imposing the respective administrative measures and is not a reproduction of the actual decision.

DATE OF IMPOSITION OF THE ADMINISTRATIVE MEASURE:

27th March 2024

RELEVANT ACTIVITY CARRIED OUT:

Real Estate Agent

SUPERVISORY ACTION:

Off-site compliance examination carried out in 2021.

DETAILS OF THE ADMINISTRATIVE MEASURES IMPOSED:

Administrative Penalty of €47,533 and a Remediation Directive in terms of Regulation 21 of the Prevention of Money Laundering and Funding of Terrorism Regulations (the "PMLFTR").

LEGAL PROVISIONS BREACHED:

- Regulation 5(1) of the PMLFTR and Section 3.3 of the 2020 Implementing Procedures Part I
- Regulation 5(5)(a)(ii) of the PMLFTR
- Regulation 11 of the PMLFTR

REASONS LEADING TO THE IMPOSITION OF THE ADMINISTRATIVE MEASURE:

Business Risk Assessment (BRA) – Regulation 5(1) of the PMLFTR and Section 3.3 of the IPs Part I

The BRA provided by the Company during the examination failed to include, assess and document the risk surrounding "use of own funds" stemming from one of the 4 risk pillars i.e. 'Product, Service and Transaction' risk. The Company failed to assess and document the risk arising from the possibility that its customers could seek to launder a large amount of illicitly obtained funds through a one-time transaction by purchasing/leasing property through the "use of own funds". This as explained in further detail and substantiated with practical examples in the FIAU's Property Guidance Paper 2020[1]. Concurrently, the BRA also failed to include controls required to mitigate said risk. To mitigate such risks, subject persons should understand the source funding the transaction. The higher the exposure to own funds, the more important it becomes to obtain clarifications, including supporting documentation where necessary.

By neglecting to document the inherent risks associated with the Use of Own Funds within the Company's BRA and the controls required to mitigate such risk, it failed to account for a crucial exposure emanating from the customers being serviced. Furthermore, whilst the Company updated its BRA in subsequent years, it still failed to account for the risks emanating from the Use of Own Funds in the latest BRA version provided to the FIAU.

In light of the above, **the Company was found in breach of its obligation in terms of Regulation 5(1) of the PMLFTR and Section 3.3 of the 2020 IPs.**

Customer Risk Assessment (CRA) – Regulation 5(5)(a)(ii) of the PMLFTR

The Company's CRA methodology and template in use at the time of the examination was not deemed complete and comprehensive as it did not include an option for the Company to select whenever 'own funds' are used by the purchaser in the transaction. In this regard, the Company submitted that such weakness is more attributed to the lack of proper documentation of the assessment undertaken rather than complete disregard to said risk. However, by failing to document the risks emanating from Own Funds in the CRA undertaken for its Customers, the Company was missing a crucial element in assessing the risks emanating from its customers. Subsequently the Company failed to implement the required controls in practice, this as confirmed through the breaches identified in relation to EDD.

Hence, despite that Regulation and guidance available at the time clearly guided subject persons to ensure to assess the product/ service and transaction risk emanating from its, for all files reviewed, the Company was found to have failed to comprehensively evaluate the ML/FT risks posed its customers.

[1] Layout 1 copy (fiaumalta.org) pg.16

Enhanced Due Diligence (EDD) - Regulation 11 of the PMLFTR

For 35% of the sample of files reviewed, despite that not all files being rated as posing a high risk by the Company, there were several elements which carry a higher inherent risk of ML/FT. This including 'High Value Transactions,' the 'Use of Own Funds' and high-risk jurisdictions. In such cases the Company was found to have failed to undertake the required EDD measures to mitigate such risks. An example of this is being illustrated hereunder:

- In two files, both relating to the same purchaser, were assigned a high risk rating by the Company in view of the purchasers ties to a non-EEA jurisdiction, having obtained Maltese nationality through the citizenship scheme and in view of the high value properties purchased in Special Designated Areas (SDA) which had a combined value ranging over €2m, both purchases occurring in less than a year.

  While it was acknowledged that the Company did indeed collect detailed information on the purchaser's source of wealth, including details on the business owned within such non-EEA jurisdiction and also a copy of the financial statements of a local company the purchaser owned, this was however considered insufficient for the following reasons:

  - It was not sufficient for the Company to simply collect the SoW information, as the Company was then expected to verify the veracity of such information against documentation, this particularly in view of the risks pertaining to the two files. This could have been done by performing open source or internet checks on the purchaser to verify the information on the purchaser's wealth, occupation, and business activities, which could have served to further corroborate the declared SoW.

  - Said financial statements show that the client company was not profitable and suffered year on year losses and the fact that the client was able to inject around €200,000 as a shareholder's loan does not provide sufficient justification to account for the SoF behind an accumulated purchase of property worth of ca. 2 million Euro.

- In another file, the purchasers (spouses) were allocated a medium risk score by the Company however higher risk elements were present which required EDD to be undertaken. This particularly in view of the high value property being purchased which was in excess of €2m and that it was to be financed through the 'use of own funds'.

  For this file, the Company collected information to show that the wife was a 'homemaker' and the husband 'owned an established company which he had just sold but remains CEO'. Open-source information was also provided which shows that said company had been sold and was worth over €200m.

However, the Company did not provide any evidence to show that the husband was actually the owner of the company which was sold and that he indeed benefitted from such sale. Instead, the Company stated that it was the Company's understanding that the company "(…) was owned (or partly owned) by the (family of the purchaser) and that the sale of the company generated substantial income to the (said) family." Even so, being CEO of the Company does not entail that the customer benefited from the sale of the Company.

Hence the actions taken by the Company do not mitigate the sector-specific high-risk factors; High Value Transaction funded through the Use of Own Funds.

ADMINISTRATIVE MEASURES TAKEN BY THE FIAU'S COMPLIANCE MONITORING COMMITTEE:

When deciding on the appropriate administrative measures to impose, in addition to the specific breaches outlined above, the Committee took into consideration the importance of the obligations being breached, the level of seriousness, and at times systemic nature, of the findings identified, as well as the extent of ML/FT risk such failures could lead to. The Committee was particularly concerned with the Company's failure to include and mitigate the risk emanating from the "use of own funds" which conveys the inadequacies in the Company's understanding of the ML/FT risks portrayed by its customers.

The Committee also considered the Company's size, as well as the impact that the subject person's failures may have had on both its operations and on the local jurisdiction. The good level of cooperation portrayed by the Company throughout the supervisory process was also factored in, including the Company's commitment to remediate its failures, and its statements that it had already commenced working on some action points. This was also evidenced through documentation provided. However, overall the Committee couldn't but note that, at least up until the compliance review, the failures observed confirm that the Company has not given due regard towards its AML/CFT obligations.

After taking into consideration the abovementioned, the Committee decided to impose an administrative penalty of €47,533 with regards to the breaches identified in relation to:

- Regulation 5(5)(a)(ii) of the PMLFTR
- Regulation 11 of the PMLFTR.

In terms of Regulation 21(4)(c) of the PMLFTR, the FIAU also served the subject person with a Remediation Directive, to be able to assess the remedial actions being implemented by the subject person in view of the breaches identified. The aim of the Directive is for the FIAU to ensure that the Company enhances its AML/CFT safeguards and that it becomes fully compliant with the obligations imposed in terms of the

PMLFTR and the FIAU's IPs, as well as perform any required follow-up measures in relation to the Company's adherence to its AML/CFT legal obligations. This also in line with the Company's commitment to enhance its AML/CFT measures. In virtue of this Directive, the Company is expected to indicate the remedial actions that it has carried out and implemented since the compliance examination to ensure compliance following the identified breaches, this including but not limited to:

- Ensuring that the Company's current BRA in force is robust and tailored to address all the ML/FT threats and vulnerabilities that its business is and may be exposed to;
- Ensuring that new and existing customers are subject to an adequate customer risk assessment in line with the obligations at law;
- Ensuring that the Company has adequate EDD procedures in place to mitigate higher risk of ML/FT.

The Directive served on the Company shall ascertain that sufficient and tangible progress is achieved on the adoption and implementation of all the procedures and measures referred to above. In the event that the requested information and/or supporting documentation are not made available within the stipulated timeframes, or the Company falls short of its obligations in terms of this Directive, the Company's default will be communicated to the Committee for its eventual actions, including the possibility of the imposition of an administrative penalty in terms of the FIAU's powers under Regulation 21(1) of the PMLFTR.

The administrative penalty hereby imposed is not yet final and may be appealed before the Court of Appeal (Inferior Jurisdiction) within the period as prescribed by the applicable law. It shall become final upon the lapse of the appeal period or upon final determination by the Court.

Key Takeaways

- Subject persons should be acquainted with the terms "SoF" and "SoW" and the extent of information and documentation required to verify the same. The customer's SoW refers to the economic activity or activities that generate the customer's wealth. This may be comprised of, for instance, income through employment or business, or inheritance. The term SoF refers to the activity, event, business, occupation or employment generating the funds used in a particular transaction. This knowledge is of paramount importance especially when subject persons are dealing with situations which have higher risk elements present such as the purchase of "High Value" property and the "Use of Own Funds".

- Subject persons should be aware that the risk in "high value transactions" with the property sector is further exacerbated when purchasers use their "Own Funds" to finance the transaction as explained above. Therefore, when "use of own funds" are present, it is crucial for subject persons to thoroughly understand the source of funds used by clients to purchase immovable property. This comprehension serves as a safeguard against unwitting involvement in money laundering activities, given that understanding the SoF is critical for subject persons to prevent their business from being exploited by

criminals for money laundering purposes. By diligently scrutinising the origin of funds, subject persons mitigate the risk of unwittingly facilitating illicit transactions, thereby protecting their professional reputation and safeguarding the jurisdiction's integrity.

- The 2017 IPs outlined that in determining the risk that a customer poses, subject persons should also give weight to, "[…]Situations where the origin of wealth and/or source of funds cannot be easily verified[…]". Further to this, Section 3.2.3 of the 2019 IPs provided clearer guidance to the subject persons to ensure to assess the product/ service and transaction risk emanating from its customers. This including funding methods which are considered to present a higher risk such as the risks emanating from customers funding property transactions through the Use of Own Funds. Only through adequate consideration of such risk can subject persons determine the required controls to apply. This guidance has also been echoed in the FIAU's Guidance Paper for the Property Sector.

- Section 4.2.2.5 of the 2017 IPs introduced the obligation for subject persons to maintain records, whereby it clearly states that "it is of utmost importance that every determination and assessment taken in identifying, assessing, managing and mitigating risks, as well as the monitoring of such process is duly recorded in writing".

- In view of the above, subject persons should ensure that all the risks, especially the sector-specific high-risk elements (ex. "high value transactions such as those linked to SDAs" and "use of own funds") are included in the BRA, the CRA and the policies and procedures.

27th March 2024

APPEAL - On the 25th of April 2024, the FIAU was served with a copy of the appeal application filed by the Company before the Court of Appeal (Inferior Jurisdiction), from the decision of the FIAU.

The Company is, *inter alia,* contesting the fact that FIAU did not adequately consider and analyse the representations provided by the Company. This is mainly with respect to breaches in relation to CRA & EDD, particularly those which involve the high risks emanating from customers funding property transactions through the *Use of Own Funds.*

The Company also states that the penalty imposed upon it by the FIAU is disproportionate and excessive.

Therefore, the Company is requesting the Court to revoke and annul the decision of the FIAU in its entirety.

Pending the outcome of the appeal, the decision of the FIAU is not to be considered final and the resulting administrative penalty cannot be considered as due, given that the Court may confirm, vary or reject in whole or in part, the decision of the FIAU. As a result, the FIAU may not take any action to enforce the administrative penalty pending judgement by the Court.

This publication notice shall be updated once the appeal is decided by the Court so as to reflect the outcome of the same.

26th April 2024