



# COUNTERING PROLIFERATION FINANCING

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GUIDANCE FOR FINANCIAL INSTITUTIONS

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## I. PURPOSE, SCOPE, & APPLICABILITY

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- This guidance paper should be read in conjunction with Bahraini Law, CBB Rulebook, local and international standards. The paper is applicable to all licensees regulated and supervised by the CBB.
- The paper is aimed at providing guidance on the private sector's obligations under the United Nations Security Councils (UNSCR) and other elements of countering proliferation financing. In addition, the paper addresses indicators of potential proliferation financing.
- The paper was developed by consolidating relevant information relevant to preventive measures from the following guidance papers and typologies issued by FATF. In February 2018, the FATF published a revised comprehensive guidance paper focusing on the implementation of financial provisions of United Nations Security Council resolutions to counter the proliferation of weapons of mass destruction.
- This guidance paper refers to information provided in the following guidance and typologies:
  - FATF Guidance on Counter Proliferation Financing: The Implementation of Financial Provisions of United Nations Security Council Resolutions to Counter the Proliferation of Weapons of Mass Destruction issued in **February 2018**
  - FATF Combating Proliferation Financing: A status report on policy development and consultation issued in **February 2010**
  - FATF Proliferation Financing Report issued in **June 2008**
- This guidance paper provides a summary of key issues identified by FATF in relation to the role of financial institutions in countering proliferation financing. Therefore, all financial institutions are urged to comprehensively read all FATF issued guidance papers.

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## II. INTRODUCTION

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**Proliferation** is the manufacture, acquisition, possession, development, export, transshipment, brokering, transport, transfer, stockpiling or use of nuclear, chemical, or biological weapons and their means of delivery and related materials (including both technologies and dual-used goods used for non-legitimate purposes), in contravention of national laws or where applicable, international obligations.

**Proliferation Financing (PF)** is the act of providing funds or financial services which are used in Proliferation. PF facilitates the movement and development of proliferation-sensitive items and can contribute to global instability and potentially catastrophic loss of life if weapons of mass destruction (WMD) are developed and deployed. If appropriate safeguards are not established, maintained, and enforced for sensitive materials, technologies, services, and expertise, they can become accessible to individuals and entities seeking to profit from the acquisition and resale, or for intended use in WMD programs.

Proliferators abuse both the informal and formal sectors of the financial system. Proliferators operate globally, disguise transactions as legitimate trades, and exploit global markets with weak export controls and free trade zones. Therefore, it is important for financial institutions to develop counter-proliferation controls and effective measures to establish domestic controls to prevent the proliferation of nuclear, chemical, or biological weapons and other means of delivery.

Targeted financial sanctions (TFS) can be a positive and effective measure in disrupting WMD proliferation networks. They act not only as a disruptive tool but as a way to provide Financial Institutions with proliferation related information on which they are implemented globally.

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### III. IMPLEMENTATION OF PROLIFERATION FINANCING CONVENTIONS

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- Recommendation 7 of the FATF standards requires countries to implement targeted financial sanctions to comply with the United Nations Security Council resolutions relating to the prevention, suppression, and disruption of proliferation of weapons of mass destruction and its financing. These resolutions require countries to freeze *without delay* the funds or other assets of, and to ensure that no funds and other assets are made available, directly or indirectly, to or for the benefit of, any person or entity designated by, or under the authority of, the United Nations Security Council under Chapter VII of the Charter of the United Nations. Recommendation 7 is **not** risk-based. Currently, Recommendation 7 is applicable to all existing and future successor resolutions and are relevant to two country-specific regimes, Democratic People's Republic of Korea (DPRK) and Iran.
- As defined by FATF, the phrase *without delay* means, ideally, within a matter of hours of a designation by the United Nations Security Council or its relevant Sanctions Committee (e.g. the 1267 Committee, the 1988 Committee, the 1718 Sanctions Committee). For the purposes of S/RES/1373 (2001), the phrase without delay means upon having reasonable grounds, or a reasonable basis, to suspect or believe that a person or entity is a terrorist, one who finances terrorism or a terrorist organization. In both cases, the phrase without delay should be interpreted in the context of the need to prevent the flight or dissipation of funds or other assets which are linked to terrorists, terrorist organizations, those who finance terrorism, and to the financing of proliferation of weapons of mass destruction, and the need for global, concerted action to interdict and disrupt their flow swiftly.
- All financial institutions are required to screen names and addresses against lists of designated persons and entities (including entities owned or controlled by them) published by the UN Security Council or its committees to ensure compliance with targeted financial sanctions. Targeted financial sanctions are applicable to persons and/or entities designated by the UN Security Council or Relevant committees based on the following designation criteria:
  - (a) Persons or entities engaging in or providing support for, including through illicit means, proliferation sensitive activities and programmes;
  - (b) Persons or entities acting on behalf of or at the direction of designated persons or entities;
  - (c) Persons or entities owned or controlled by designated persons or entities;
  - (d) Persons or entities assisting designated persons or entities in evading sanctions, or violating resolution provisions.
- Therefore, all financial institutions should implement measures to identify and detect persons, entities, and transactions relevant to proliferation financing. Such measures include

ensuring that the targeted financial sanctions are implemented effectively, robustly, and without delay, prevent any prohibited payments, and preserve the rights of the innocent third parties.

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#### IV. DPRK AND IRAN SANCTIONS REGIME

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- Implementation of UN targeted financial sanctions on the Democratic People’s Republic of Korea (DPRK) not only requires freezing measures directed at those designated or listed by the United Nations, but also those:
  - (a) Acting on behalf, at the direction of, whether directly or indirectly of, designated persons or entities;
  - (b) Owned or controlled by them; and
  - (c) Assisting them in evading sanctions or violating resolution provisions.
  
- The following examples are circumstances identified by FATF as to where customers and transactions are more vulnerable to be involved in proliferation financing activities relating to both DPRK and Iran sanctions regimes:
  - Customers and transactions associated with countries subject to sanctions;
  - Instruments that could particularly be used to finance prohibited transactions, such as certain trade financing products and services;
  - Customers involved with and/or transactions related to items, materials, equipment goods and technology prohibited by UNCSRs;
  - Value of invoiced goods against market value, inconsistency or discrepancies in trade-related documentation.
  
- FATF has established the following non-exhaustive list of scenarios in of which DPRK sanctions regime may be triggered:
  - Significant withdrawals or deposits of bulk cash that could potentially be used to evade targeted financial sanctions and activity-based financial prohibitions;
  - Opening of banking accounts by DPRK diplomatic personnel, who have been limited to one account each under the relevant UNSCRs (including number of bank accounts being held, holding of joint accounts with their family members);
  - Clearing of funds, granting of export credits or guarantees to persons or entities that are associated with trading transactions relating to the DPRK;
  - Providing insurance or re-insurance services to maritime vessels owned, controlled or operated, including through illicit means, by the DPRK or classification services to vessels which there are reasonable grounds to believe were involved in activities, or the transport of items, prohibited by UNCSRs concerning the DPRK, unless the Security Council 1718 Committee determines otherwise on a case-by-case basis;

- Direct or indirect supply, sale or transfer to the DPRK of any new or used vessels or providing insurance or re-insurance services to vessels owned, controlled, or operated, including through illicit means, by the DPRK, except as approved in advance by the Security Council 1718 Committee on a case-by-case basis;
- The leasing, chartering or provision of crew services to the DPRK without exception, unless the Security Council 1718 Committee approves on a case-by-case basis in advance;  
or
- Using real property that DPRK owns or leases in their territory for any purpose other than diplomatic or consular activities.

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## V. SCENARIOS INDICATING POSSIBLE PROLIFERATION FINANCING ACTIVITIES

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- The identification of proliferation financing may be challenging and possess difficulties due to various reasons. Such may include an increased trend in the sale and purchase of elementary components which are used for legitimate purposes, difficulty in identifying dual-used goods, the complexity of networks used for obtaining proliferation goods, and existence of proliferation financing in situations where sources of funds are legitimate and the types of goods involved are concealed.
- Trade finance is considered as a common vehicle used to financing proliferation. Enhanced due diligence measures are recommended to be implemented on trade finance transactions and relationships.
- Financial institutions are required to give special attention to certain trade activities such as loans to facilitate export transactions, factoring, providing of guarantees to or by financial institutions on behalf of exporters, and providing insurance against certain risks in trade finance.
- Financial institutions must implement measures and controls to counter the possible financial flows available to proliferators in order to impede the procurement of illicit goods and technologies used for the development of weapons of mass destruction. Primarily, financial institutions must understand the different possible situations where customers, transactions and other account activities may indicate involvement in proliferation financing. FATF developed a list of elements and scenarios that potentially indicate proliferation financing as the following:
  - Transaction involves person or entity in a foreign country of proliferation concern
  - Transaction involves shipment of goods incompatible with the technical level of the country to which it is being shipped, (e.g. semiconductor manufacturing equipment being shipped to a country that has no electronics industry).
  - Transaction involves possible shell companies (e.g. companies do not have a high level of capitalization or displays other shell company indicators).
  - Transaction demonstrates links between representatives of companies exchanging goods i.e same owners or management
  - Transaction involves persons or companies (particularly trading companies) located in countries with weak export control laws or weak enforcement of export control laws.



- Transaction involves shipment of goods inconsistent with normal geographic trade patterns (e.g. does the country involved normally export/import good involved).
- Transaction involves financial institutions with known deficiencies in AML/CFT controls.
- Transaction includes dual-used goods, proliferation sensitive or military goods.
- Wire instructions or payment from or due to parties not identified on the original letter of credit or other documentation.
- Description of goods on trade or financial documentation is non-specific innocuous or misleading.
- Information on the end-use or final destination of the trade finance transaction is unclear.
- A freight forwarding firm is listed as the product's final destination
- Order for goods is placed by firms or persons from foreign countries other than the country of stated end-user
- Discrepancy in the information provided with the trade documents and financial flow of the transaction.
- Indication of fraudulent documents and identities such as forged export/import documentation.
- Unclear and non-specific wording on customs declaration and export documents (i.e. pump, with no further explanation.)
- Evidence that documents or other representations (e.g. relating to shipping, customs, or payments) are fake or fraudulent.
- Circuitous route of shipment (if available) and/or circuitous route of financial transaction
- Trade finance transaction involves shipment route (if available) through country with weak export control laws or weak enforcement of export control laws.
- Declared value of the shipped items in the trade finance transaction is under-valued in relation to its shipping cost.
- Inconsistencies in information contained in trade documents and financial flows, such as names, companies, addresses, final destination, etc.
- Pattern of wire transfer activity that shows unusual patterns or has no apparent purpose

- Customer vague/incomplete on information it provides, resistant to providing additional information when queried.
- The customer is involved in sale, purchase, supply, or delivery of dual-used goods, particularly in higher risk jurisdictions.
- Use of personal account to purchase industrial items.
- Customer activity does not match business profile, or end-user information does not match end-user's business profile
- New customer requests letter of credit transaction awaiting approval of new account.