



THE ANCHOR



FINANCIAL SANCTIONS EVASION TYPOLOGIES: RUSSIAN ELITES AND ENABLERS

A 'Red Alert' was recently issued by the National Economic Crime Centre (NECC), a multi-agency unit in the National Crime Agency (NCA), and HM Treasury's Office of Financial Sanctions Implementation (OFSI), working in conjunction with law enforcement and financial sector partners as part of the Joint Money Laundering Intelligence Taskforce (JMLIT).

The purpose of the alert was to provide information about common techniques that designated persons (DPs) and their enablers are suspected to be using to evade financial sanctions.

DPs are using a range of techniques to evade sanctions impacting on their personal and commercial holdings. These include transferring assets and funds directly and indirectly to jurisdictions where sanctions are not in place, such as the UAE, Turkey, China, Brazil, India and the former Soviet Union (excluding the Baltic States and Ukraine), use of secrecy jurisdictions or citing Russian legal protection from sharing information.

While this behaviour has generally occurred prior to sanctions being imposed on the DP, it is also happening shortly afterwards. Please click [here](#) for more guidance and for specific Indicators.

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FATF REVISION OF RECOMMENDATION 25 - BENEFICIAL OWNERSHIP OF LEGAL ARRANGEMENTS

The Financial Action Task Force (FATF) is currently reviewing Recommendation 25 on measures to prevent the misuse of legal arrangements for money laundering or terrorist financing, and its interpretive note. The following areas were considered:

Scope of Legal Arrangements, Risk Assessment and Foreign Trusts

The FATF is proposing a revised definition of legal arrangements based on Article 2 of the Hague Convention to reflect the scope of what constitutes a legal arrangement across different jurisdictions. FATF is further considering whether countries should apply measures to understand the risk posed by foreign trusts and similar arrangements governed under their law or which are administered in their jurisdictions or whose trustees are residing in their jurisdictions, and to take appropriate steps to manage and mitigate these risks.

Obligations of Trustees under Recommendation 25

FATF is considering how to further clarify obligations on trustees (and persons holding an equivalent position in a similar arrangement) to obtain and hold adequate, accurate and up-to-date information, related to parties to a trust. Specifically, the FATF is contemplating setting the nexus of such obligations to countries where the trustees reside and/or where the trusts are administered. The FATF is also considering whether to bring professional and non-professional trustees under the same set of requirements by extending the requirement for records to be kept for at least five years to such non-professional trustees.

Definition of Beneficial Owners

The FATF is considering whether to expand the definition of beneficial owner for trusts so that beneficial ownership (BO) information could include the identity of each: (i) settlor; (ii) trustee(s); (iii) protector (if any); (iv) beneficiary, or where applicable, class of beneficiaries or objects of a power; and (v) other natural person(s) exercising ultimate effective control over the arrangement.

Typologies

The FATF has requested further input on how legal arrangements can be misused for money laundering/terrorist financing purposes. Themes which are under consideration include complex ownership structures, flee/flight clauses etc. The FATF is interested in the features of legal arrangements that are being used to obscure ownership as well as key obstacles to transparency of trusts and other legal arrangements.

Approach to Collecting Beneficial Ownership Information

The FATF is also contemplating whether countries should be required to use mechanisms to have access to BO information besides trustees, including for example: (i) a public authority or body holding information on the beneficial ownership of trusts or similar legal arrangements, (ii) asset registries, (iii) information collected by other competent authorities, or (iv) information collected by other agents or service providers including trust and company service providers, investment advisors or managers, accountants, or lawyers.

Adequate, Accurate and Up-to-date Information

Finally, the FATF is considering how to clarify the key attributes of access to information by competent authorities, that access should be timely, and information should be adequate (to identify the natural persons who are the beneficial owner(s) and their roles in the trust), accurate (i.e. verified using reliable, independently sourced/obtained documents or other methods, on a risk-sensitive basis) and up-to-date (i.e. updated within a certain period following any change). This would leverage the approach taken in the revised Recommendation 24, adopted in March 2022.

The views and proposed revisions will be considered by the FATF and put forth for discussions at its October 2022 meetings. A further draft will be presented at the February 2023 FATF Plenary.

AML/CFT RISKS WITH DAOs

Financial service providers (“FSPs”) including Trust Company Service Providers (“TCSPs”) engaging with a decentralised autonomous organisation (“DAO”) should take note of the heightened AML/CFT risks associated with the decentralised structure and take appropriate steps to mitigate these risks.

DAOs may be used by virtual asset service providers (“VASPs”) and other businesses connected with virtual assets. The term does not currently have a legal definition, but common characteristics include that:

- It is fully autonomous and operable without a central point of control.
- It has no hierarchy.
- Decisions made by stakeholders or members instead of leaders or managers (although aspects of decision-making may be delegated to a selected team).
- It relies on smart contracts for execution.
- Financial transaction records and program rules are transparent and maintained on a blockchain.

In the Cayman Islands, the foundation company structure has attracted DAOs to the jurisdiction, who see it as a helpful legal tool for a structure with no centralised controlling interest. The types of activities undertaken by DAOs include investment, borrowing, fundraising, charity work and issuing/purchasing non-fungible tokens. DAO transactions invariably take place without intermediaries, and it is likely they will utilise blockchain technology.

FSPs may be approached by clients that are DAOs conducting relevant financial business and subject to the requirements of the Virtual Asset Service Providers Act (2022 Revision) and the Cayman Islands Anti-Money Laundering Regulations 2020. FSPs could find that effective client due diligence, risk assessment and beneficial ownership procedures are impeded by the fact that many DAOs operate pseudonymously.

DAO stakeholders or members can often exercise their token-based voting rights without revealing their real identities. This pseudonymity can enable bad actors to disguise their identities and continue participating in business transactions.

The lack of centralised control and associated accountability can help obfuscate the true source of funds and the real beneficial owners. FSPs should therefore consider additional verification methods to ensure that they truly understand the nature of business, source of funds and purpose of any transaction.

Further, a DAO may not always be as decentralised and autonomous as its name may suggest. Some DAOs use smart contracts to enact changes directly, according to governance votes, but others rely on individuals or groups of individuals to implement changes. Many DAOs leverage a mix of centralised and decentralised governance and give central management power to a small number of individuals for pragmatic reasons or because they established the DAO.

It is therefore essential that FSPs and TCSPs conduct appropriate due diligence to ensure that they have a full understanding of the structure of the DAO and incorporate this into the client risk assessment. Corporate governance and/or AML/CFT risks can then be managed accordingly. This includes but is not limited to:

- How the DAO operates.
- How decisions are made and actions implemented.
- How profit is shared and distributed.
- The level of customer due diligence undertaken for stakeholders and/or members.
- The nature of business, including all ancillary services.
- Whether transactions are transparent and on a blockchain.
- Whether transactions are monitored.
- Whether there are checks on the source of funds.
- How and if the DAO could comply with a request from law enforcement to freeze assets/ transactions.