

**South Africa: Report on the Observance of Standards and Codes—
FATF Recommendations for Anti-Money Laundering and
Combating the Financing of Terrorism**

This Report on the Observance of Standards and Codes on the FATF Recommendations for Anti-Money Laundering and Combating the Financing of Terrorism for **South Africa** was prepared by the Financial Action Task Force on Money Laundering (FATF), using the comprehensive methodology endorsed by the Financial Action Task Force in October 2002 and by the Executive Board of the IMF in November 2002. The views expressed in this document are those of the staff team and do not necessarily reflect the views of the government of **South Africa** or the Executive Board of the IMF. ROSCs do not rate countries' observance of standards and codes or make pass-fail judgments. Consequently, no overall assessment of the effectiveness of the anti-money laundering and combating the financing of terrorism regime is provided.

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South Africa: Report on Observance of Standards and Codes FATF Recommendations for Anti-Money Laundering and Combating the Financing of Terrorism

Introduction

1. This Report on the Observance of Standards and Codes for the *FATF 40 Recommendations for Anti-Money Laundering and 8 Special Recommendations for Combating the Financing of Terrorism* was prepared by representatives of member jurisdictions of the Financial Action Task Force (FATF) and the Eastern and South African Anti-Money Laundering Group (ESAAMLG) and members of the FATF and ESAAMLG Secretariats.¹

2. The report provides a summary of the level of observance with the FATF 40+8 Recommendations and provides recommendations to strengthen observance. The views expressed in this document are those of the evaluation team and are consistent with the mutual evaluation report adopted by the FATF Plenary, but they do not necessarily reflect the views of the government of South Africa or the Boards of the IMF or World Bank.

Information and methodology used for the assessment

3. In preparing the detailed assessment, assessors reviewed the relevant anti-money laundering (AML) and combating the financing of terrorism (CFT) laws and regulations, the capacity and implementation of criminal law enforcement systems, and supervisory and regulatory systems in place in the following sectors: banks, currency exchange, securities and collective investment schemes, insurance, and money remittance to deter money laundering and financing of terrorism. The evaluation team met from 7-11 April 2003 with officials from the relevant South African agencies as well as financial institution and casino representatives and a private sector AML expert.

4. South Africa is a regional financial centre with a modern financial system and banking infrastructure. There are 50 registered banks operating in South Africa. Twenty-seven banks are locally-controlled and have 8,455 South African branches and 246 branches abroad. Seven banks are foreign-controlled and have 27 branches in South Africa. In addition, there are two mutual banks, and foreign-registered banks have 14 registered branches in South Africa. South Africa has an exchange control regime. Currency exchange business can only be conducted by Authorised Dealers in Foreign Exchange, which are appointed by the Minister of Finance and regulated by the Exchange Control Depart (EXCON) of the South Africa Reserve Bank. There are currently 38 Authorised Dealers, the majority of which are banks. Money remittance/transfer business is permitted only in accordance with the terms of an appointment as an Authorised Dealer.

5. South Africa has 73 regulated long-term insurance companies, 97 short-term non-life insurance companies, 15,000 licensed financial advisors and intermediaries that include approximately 350 investment managers. There are various collective investment schemes run by 29 local managers, and

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approximately 15,000 pension funds run by 450 approved administrators. There are 29 casinos currently operating.

Main findings

6. South Africa has developed a comprehensive legal structure to combat money laundering. Currently, the main statutes are the Prevention of Organised Crime Act 1998 (POCA) and the Financial Intelligence Centre Act 2001 (FICA). The financial intelligence unit and other supervisory and investigative bodies appear adequately staffed and genuinely committed to implementing the new system. However, many of these measures are new and have not yet been fully put into effect, and all sectors will need to continue to increase attention and training on anti-money laundering issues. Moreover, although the overall framework should be effective in the longer term, the results achieved to date are limited, and all government agencies will need to co-ordinate their efforts to ensure that the new legislative and regulatory regime that is being put into place is effectively implemented. Importantly, South Africa also needs to expeditiously develop a comprehensive framework to combat the financing of terrorism.

Criminal justice measures and international co-operation

(a) Criminalisation of ML and FT

7. Drug-related money laundering offences were first covered under the Drugs and Drugs Trafficking Act, 140 of 1992. The Proceeds of Crime Act, 76 of 1996, broadened the statutory money laundering offences to the proceeds of all criminal activity. Under the POCA 1998, predicate crimes for money laundering now apply to all underlying “unlawful activity” both within and outside of South Africa. This covers not only all criminal offences, but also other activity that contravenes South African law. The offence applies to “own funds” laundering and acts committed intentionally (actual knowledge) or negligently (“ought reasonably to have known”). This is also defined to include belief that a fact is reasonably possible. Criminal liability also extends to legal entities, and there are severe sanctions for committing an offence.

8. The financing of terrorism, terrorist acts, or terrorist organizations is not yet a criminal offence and thus not a predicate offence for money laundering in South Africa. A draft bill that will address many aspects of the fight against terrorism and terrorist financing has been presented to Parliament and is presently being considered by a Parliamentary Committee. At the time of the on-site visit, South Africa had signed the UN International Convention for the Suppression of the Financing of Terrorism and the Parliament had ratified it; however, the instruments of ratification had not yet been delivered to the UN.¹

(b) Confiscation of proceeds of crime or property used to finance terrorism

9. The legal provisions for the identification, freezing, and confiscation of the proceeds of crime are comprehensive. The POCA provides for criminal confiscation and civil forfeiture of criminal proceeds, assets of corresponding value, and instrumentalities of crime. The legal framework protects the rights of bona fide third parties, and also provides for asset sharing. South Africa has also applied increased resources to this area, and these measures have been quite successful, with a steady annual increase in the property that has been frozen and confiscated. The Asset Forfeiture Unit (AFU) of the National Prosecuting Authority (NPA) has thus far achieved over 300 seizures involving assets worth over R400 million (USD 50 million) and obtained 120 forfeiture or confiscation orders involving assets worth

¹ The UN has indicated that this process was completed on 1 May 2003.

about R80 million. Despite the otherwise comprehensive nature of these provisions, South Africa cannot currently seize property used to finance terrorism and has only limited ability to freeze funds in financial institutions and therefore cannot fully implement the relevant FATF Special Recommendations and UN Security Council Resolutions.

(c) The financial intelligence unit (FIU) and process for receiving, analysing, and disseminating financial information and other intelligence at the domestic and international levels

10. The FICA established the Financial Intelligence Centre (FIC) to receive, analyse, and disseminate suspicious transaction reports (STRs). The FIC became operational and began receiving STRs on 3 February 2003. In a short period of time, the FIC has made significant strides towards becoming an operational FIU and appears adequately structured, funded, staffed, and provided with the necessary resources and powers to fully perform its authorised functions. The legal provisions allow for co-operation with domestic authorities and foreign counterparts and appear comprehensive, but have not yet been fully put into practice. It is too early to assess the effectiveness of the FIC, but early results appear promising. FIC currently has a staff compliment of 20 officers made up of seconded personnel from other government departments, including Treasury, the South African Revenue Service (SARS), the South African Police Service (SAPS), and the NPA. The FIC plans to increase to a staff of 55 by the end of its first year (February 2004).

11. While the legal provisions are far-reaching, the results to date have been more variable. It is encouraging that the number of STRs filed with SAPS (the recipient of STRs prior to the establishment of the FIC) increased steadily from 140 (1997) to 1891 (2002), with a significant majority coming from banks. This increase continued in 2003 with the establishment of FIC, when banks and money remitters also filed more than 900 STRs between 3 February and 1 April 2003. However, prior to this, the number of STRs from securities and investment firms and from casinos was very low, and efforts will need to be made to encourage all relevant industries to actively focus on identifying suspicious transactions. It is also of concern that since 1997 a total of 4,523 STRs generated only 41 criminal investigations, which led to five convictions for offences other than money laundering. It is hoped that the creation of the FIC and the new co-ordination mechanisms being established between law enforcement agencies will result in improved use of STR data.

(d) Law enforcement and prosecution authorities, powers, and duties

12. South Africa has a number of agencies that investigate and prosecute cases involving money laundering. The NPA provides a national framework for prosecutions. Within the NPA, the Directorate of Special Operations (DSO) investigates and prosecutes a range of more serious cases. The NPA's AFU supports the police and other law enforcement structures in all aspects of forfeiture. The SAPS investigates criminal activity generally and has allocated the responsibility for investigating money laundering to specific units. The SARS, which includes the Customs Service, is responsible for revenue collection and the investigation of tax evasion and evasion of customs duties and works closely with law enforcement agencies on money laundering matters. The law enforcement agencies appear adequately staffed and resourced. However, thus far, money laundering offences have not been adequately investigated and prosecuted, and it is a matter of concern that there have been only two convictions for the money laundering offence since 1996. Although this may be partly due to the fact that some law enforcement agencies are new, it also appears that existing agencies and prosecutors have generally focused only on investigating and prosecuting the predicate offences, and South Africa should make efforts to establish an effective investigative program to increase the number of money laundering prosecutions that are brought. One approach is to consider establishing designated, specialised units and resources to deal only with money laundering cases and referrals from the FIC. The agencies have

also increased training programs, and the planned continued increase in these programs should help increase awareness in this area.

13. Investigators have adequate legal means to obtain bank records and other information and evidence regarding alleged offences. Investigators also have sufficient legal tools for a wide range of investigative techniques, including controlled delivery, undercover operations, and wiretaps.

(e) International co-operation

14. Under the International Co-Operation in Criminal Matters Act, 75 of 1996, South Africa has broad powers to provide a wide range of mutual legal assistance (MLA) related to money laundering matters, and can provide MLA even where there is no dual criminality. Thus, it can exchange information relating to terrorist financing investigations, but cannot assist in seizing assets related to terrorist financing. The Extradition Act, 67 of 1962, and various extradition agreements provide broad extradition authority, including for South African nationals. However, as dual criminality is required, South Africa cannot yet extradite individuals for terrorist financing. South Africa has acceded to the 1988 United Nations Convention Against Illicit Traffic in Narcotic Drugs and Psychotropic Substances, has ratified the 1999 UN Convention on the Suppression of Terrorist Financing, and is working to ratify the 2000 UN Convention Against Transnational Organized Crime. It has also entered into many bilateral treaties and agreements, either for MLA or at a law enforcement level. Draft legislation currently under consideration in Parliament will criminalise the financing of terrorism and enable South Africa to extradite for this offence.

Preventive measures for financial institutions

(a) Financial institutions

15. The FICA creates a range of anti-money laundering obligations for “accountable institutions,” which include banks, securities and investment firms, insurance companies, bureaux de change, money remitters, casinos, dealers in travellers’ cheques and money orders, as well as lawyers and accountants. Obligations to report suspicious transaction reports came into effect on 3 February 2003. Other obligations including customer identification, record-keeping requirements, and internal controls became effective through their implementing Regulations on 30 June 2003.

16. The FICA requires that the identity of a client, the identity of the person acting on behalf of the client, and the person on whose behalf the client is acting be established and verified. While this requirement in the Act is generally satisfactory, there is no general duty to identify the beneficial owner. In fact, the Regulations appear to limit the scope of the law in relation to legal entities by only requiring the identification of persons who own at least 25% or more of the shares of a legal entity. In addition, if shares in a company are owned by another company, there is no obligation to identify the owners of that second company. The Regulations also contain a large number of exemptions from the customer identification and record keeping requirements, some of which seem to unduly limit the effectiveness of the law. The net result is that South Africa’s ability to identify the true owner of property is undermined, and the Regulations under FICA should be amended in this respect.

17. The laws and regulations relating to record-keeping are generally satisfactory. Exchange control regulations require comprehensive originator information to be recorded for funds transfers, and this information can be made available upon inquiry. There is currently no requirement for this information to remain with the transfer form; however, a new circular to be issued by the Exchange Control Department (EXCON) of the South African Reserve Bank (SARB) will require this.

18. South Africa has had an obligation to report suspicious transactions since 1996, and under the FICA, which came into effect on 3 February 2003; the reporting obligation is now very broad. Similarly, the legal provisions concerning protection from proceedings, and no “tipping-off” are comprehensive. The FIC and other supervisory bodies still need to issue guidelines to assist in the identification of suspicious activities, and propose doing so once they have gathered further STR data. This should be done as expeditiously as possible. South Africa must also act swiftly to pass measures in relation to terrorist financing, including extending the STR obligation to this serious crime.

19. The main supervisory bodies are the SARB and the Financial Services Board (FSB). SARB supervises banks, money remittance and currency exchange business, while FSB supervises all other financial institutions. SARB, FSB and other supervisory bodies will need to play a more active role now that FICA is fully in effect.

20. In addition, although FICA creates criminal penalties for non-compliance, the supervisors may only currently inspect for compliance in accordance with their existing legislation; the ability to use enforcement powers for anti-money laundering requirements is unclear. Amendments to enabling legislation should be made to provide supervisors with clearly defined functions for combating money laundering and terrorist financing and to allow them to inspect and sanction for non-compliance with FICA’s provisions and more clearly allow co-operation with domestic authorities and foreign counterparts in sharing AML information.

21. Other anti-money laundering measures that are required include policies or guidance concerning jurisdictions that do not adequately apply the FATF Recommendations and in relation to foreign branches that operate in such jurisdictions. The laws and regulations concerning the maintenance of high standards of integrity and the necessary internal controls by financial institutions are satisfactory in most respects, and the key issue is to ensure that anti-money laundering requirements are being properly implemented by institutions.

(b) Other sectors (Casinos)

22. The Government of South Africa has indicated that casinos were one of the methods for laundering illicit proceeds in South Africa. There are 29 casinos currently operating, which contain approximately 20,000 gaming machines and 713 gaming tables. The provincial gambling boards have responsibility for licensing casinos and the enforcement of the licensing provisions.

23. Casinos are “accountable institutions” under FICA and thus subject to the general provisions concerning customer identification, record-keeping, suspicious transaction reporting, formulating and implementing internal rules, compliance officers, and training. As with the other accountable institutions, the STR provisions came into effect on 3 February 2003, whereas the remaining provisions came into effect on 30 June 2003. The FICA Regulations also set out a number of exemptions for casinos for customer identification and the corresponding record keeping, but these are generally appropriate. Casinos have been subject to suspicious transaction reporting requirements since 1997; however, only 14 STRs were filed prior to 2003. Moreover, despite the very low number of STRs, the industry believed that they are fully aware of all money laundering risks and seemed quite complacent about those risks.

24. South African officials should work to develop a tighter anti-money laundering regime in the casino sector, and to ensure that these measures are adequately enforced. Similarly, the casino industry should continue its current training initiatives to raise awareness of the money laundering risks, and should work closely with government to enhance the systems currently in place, and ensure that the sector is fully and actively complying with their obligations.

Summary assessment against the FATF Recommendations

25. South Africa is compliant with or largely compliant with most of the FATF 40 Recommendations. The most significant deficiency pertains to beneficial ownership, as there is no specific requirement for identification of the beneficial owner, and certain exemptions may diminish the law's effectiveness in this area. Although the reporting requirements are sufficiently broad, South Africa needs to issue guidelines to assist in the identification of suspicious transactions and activities. Policies to deal with differing money laundering standards for subsidiaries abroad and measures to deal with countries that do not sufficiently apply the FATF Recommendations are also needed. South Africa also needs to quickly adopt and implement comprehensive anti-terrorist financing measures.

Table 1. Recommended action plan to improve compliance with the FATF Recommendations

Reference FATF Recommendation	Recommended Action
40 Recommendations for AML	
ML offence (FATF 4)	South Africa needs to develop a more active and effective program for investigating and prosecuting the money laundering offence. One approach is to consider establishing specialised, designated investigative units and resources to deal only with money laundering cases and referrals from the FIC.
Customer identification and record-keeping rules (FATF 10-13)	There is a need to amend the Regulations to require reasonable measures to identify the true beneficiary. Should also reconsider the scope of the exemptions for the insurance and some other sectors. Supervisors also need to give careful consideration before granting "equivalent" status. Finally, South Africa will need to require that originator information be kept with funds transfers.
Increased diligence of financial institutions (FATF 14-19)	Rec. 19: There should be general provisions applicable to all financial institutions that require adequate screening procedures to ensure high standards when hiring employees, as well as requirements for a specific audit function and/or sample testing conducted by the compliance officer. Such a function only currently exists for banks.
Measures to cope with countries with insufficient AML measures (FATF 20-21)	Rec. 20: Provisions or recommendations are also needed to ensure that the higher standards of compliance are used when foreign branches of South African financial institutions are subject to a different standard than the home country. Rec. 21: Need to adopt policies or guidelines for countries that do not adequately apply the FATF recommendations.
Implementation & role of regulatory and other administrative authorities (FATF 26-29)	Rec. 26: South Africa should continue with plans to amend the sector-specific legislation granting authority to supervisors to enforce compliance with FICA's provisions. Supervisors should take a more proactive role concerning inspections and enforcement. Rec. 28: South Africa needs to develop and issue guidelines to assist in the identification of suspicious and unusual transactions or series of transactions. Rec. 29: South Africa is encouraged to adopt draft legislation amending the Banks Act, 94 of 1990, to grant the BSD an enhanced role in the application process for bank directors.

Reference FATF Recommendation	Recommended Action
8 Special Recommendations on terrorist financing	
I. Ratification and implementation of UN instruments	South Africa needs to fully implement 1999 UN Convention. Needs to criminalise the financing of terrorism, terrorist acts, and terrorist financing (to be compliant with UN SCR 1373). Need measures to be able to effectively freeze and confiscate funds and other assets of suspected terrorist financing.
II. Criminalizing the financing of terrorism and associated money laundering	Needs to criminalise the financing of terrorism, terrorist acts, and terrorist organisations.
III. Freezing and confiscating terrorist assets	South Africa needs to expand its ability to freeze, seize and confiscate funds and other assets related to the financing of terrorism, terrorist acts, and terrorist organisations.
IV. Reporting suspicious transactions related to terrorism	South Africa should amend its legislation to require reporting to the FIC of suspicious transactions that relate to funds suspected to be linked to or used in the financing of terrorism.
V. International co-operation	Although South Africa can provide mutual legal assistance in TF cases, South Africa needs to adopt measures to freeze and seize funds or property used or intended for use in TF, and to be able to extradite for TF.
VI. Alternative remittance	There are no special measures for alternative remittance; however, remittance business can only legally occur through appointed Authorised Dealers; therefore FATF recommendations apply.
VII. Wire transfers	South Africa needs to require that the originator information accompany the wire transfer. The BSD has indicated it will issue a circular that will require this.

Table 2. Other recommended actions

Reference	Recommended Action
Casinos	South Africa should work to develop a tighter anti-money laundering regime in the casino sector, and to ensure that these measures are adequately enforced.

Authorities' response

26. The Government of South Africa had no additional comments on this report.