Title: The Money Laundering and Terrorist Financing (High-Risk Countries) (Amendment) Regulations 2022	De minimis assessment
SI No:	**Date: 25 March 2022**
Other departments or agencies: **N/A** **Contact for enquiries**: **Stephanie Ukpelukpe**	**Type of regulation:** **Domestic** **Date measure comes into force:** **29/03/2022**
Cost of Preferred (or more likely) Option 73,588.50	**Equivalent Annual Net Direct Cost to Business per year** 36,794.25

1. What is the problem under consideration? Why is government intervention necessary?

The Money Laundering Regulations (MLRs) is a central component of the UK's anti-money laundering (AML) and counter-terrorist financing regime (CTF). The MLRs cover both money laundering and terrorist financing (ML/TF). Money laundering includes how criminals change money and other assets into clean money or assets that have no obvious link to their criminal origins. Money laundering can undermine the integrity and stability of our financial markets and institutions. It is a global problem, it represents a significant threat to the UK's national security and it is a key enabler of serious and organised crime, which costs the UK at least £37 billion every year.

Terrorist financing involves dealing with money or property that you know or have reasonable cause to suspect may be used for terrorism. There is an overlap between money laundering and terrorist financing, as both criminals and terrorists use similar methods to store and move funds, but the motive for generating and moving funds differs. The UK has a comprehensive AML/CTF regime, and the government is committed to ensuring that the UK effectively combats ML and TF risks.

The MLRs include a number of requirements that businesses that fall under its scope[1] must take to combat ML/TF. These requirements include the need for firms to implement measures to identify and verify the people and organisations with whom they have a business relationship or for whom they facilitate transactions. This includes measures relating to customer due diligence and enhanced due diligence.

Enhanced due diligence (EDD) is defined by regulation 33 of the MLRs as requiring measures such as obtaining additional information on the customer and customer's beneficial owner; and on the intended nature of the business relationship in order to establish with more care if money laundering or terrorist financing is likely to be an issue.

In addition, the regulations also require financial institutions and other AML regulated firms to carry out EDD in respect of business relationships and transactions involving 'high-risk third countries'. These are countries that have been identified as having strategic deficiencies in their AML/CTF regimes and that pose a significant threat to the UK's financial system.

[1] Regulation 8 sets out that the MLRs are applicable to credit institutions; financial institutions; auditors, insolvency practitioners, external accountants and tax advisers; independent legal professionals; trust or company service providers; estate agents and letting agents; high value dealers; casinos; art market participants; cryptoasset exchange providers; custodian wallet providers, auction platforms.

The definition of a 'High-Risk Third Country' in the MLRs is set out in Regulation 33A which states that a 'high-risk third country' is a country which is specified in Schedule 3ZA of the MLRs.

Schedule 3ZA is a list of countries; it mirrors the lists of countries identified by the Financial Action Task Force (FATF), the global AML/CTF standard setter, as having strategic deficiencies in their AML/CTF regimes. The FATF meets periodically (3 times a year) to discuss global AML/CTF risk profiles and amend its public lists of jurisdictions under increased monitoring and high-risk jurisdictions.

When the UK's new autonomous high-risk third countries list was introduced, the UK committed to updating the list to mirror the periodic changes made by the FATF to its lists of countries identified as having strategic deficiencies in their AML/CTF regimes. If the current high-risk third country list in legislation is not amended, it will become outdated and non-reflective of global ML/TF risk identified by the FATF, leaving the UK financial system at risk of threats from countries with strategic deficiencies in their AML/CTF regimes.

Why is this SI necessary?

Following the rationale set out above, the UK's HRTC list now needs to be updated via a statutory instrument to reflect changes made by FATF to the lists of countries identified as having strategic deficiencies in their AML/CTF regimes.[2] **The FATF has added UAE and removed Zimbabwe from the list of jurisdictions under increased monitoring and as such Schedule 3ZA of the MLRs will need to be amended accordingly**.

2. **What are the policy objectives and the intended effects?**

Effective AML/CTF regulations are a key part of making the UK a hostile environment for illicit finance, protecting the UK's reputation as a safe place to conduct business and maintaining confidence in the financial system.

This legislation will update the list of high-risk third countries that AML regulated firms need to apply EDD to. This update will ensure the UK's AML regulatory regime is reflective of global ML/TF risks as identified by the global standard setter on AML/CTF, the FATF. The FATF meets periodically (3 times a year) to discuss global ML/CT risk profiles and amend its public lists of jurisdictions with strategic deficiencies in their AML/CTF regimes. These lists form the basis of the UK's high-risk third countries list.

When a country is added to FATF's public list of jurisdictions under increased monitoring, it is assigned an action plan that sets out the strategic deficiencies in their AML/CTF regimes and the actions that should be undertaken to address them. Based on the contents of the FATF action plan it is expected that the UAE would complete all the actions and be removed from the FATF list within two years. As the UK's list mirrors FATF's list and seeks to update the HRTC rapidly after the FATF's listing and de-listing decisions, the UAE is likely to remain on the HRTC list for no longer than two years. This means that the proposed change to the MLRs, which adds the UAE to the HRTC list, is likely to be in effect for the next two years, and businesses would have to conduct EDD checks on customers and relevant transactions with a UAE nexus during that time.

[2] https://www.fatf-gafi.org/publications/high-risk-and-other-monitored-jurisdictions/documents/increased-monitoring-march-2022.html and https://www.fatf-gafi.org/publications/high-risk-and-other-monitored-jurisdictions/documents/call-for-action-march-2022.html

3. What policy options have been considered, including any alternatives to regulation? Please justify preferred option

Option 1, Do nothing. Under this option, the Government would not amend the current list of High-Risk Third Countries in the MLRs. This would result in the UK High-Risk Third Country list being at risk of becoming outdated and non-reflective of global ML/TF risk identified by the FATF, leaving the UK financial system at risk of threats from countries with strategic deficiencies in their AML/CTF regimes.

Option 2 (preferred option). Legislate to amend the MLRs to update the list of High-Risk Third Countries to mirror the countries identified by the FATF as having strategic deficiencies in their AML/CTF regimes. This will ensure that the UK's list remains up to date and reflective of global ML/TF risks as identified by the FATF.

4. Please justify why the net impacts (i.e. net costs or benefits) to business will be less than £5 million a year.

- **What will businesses have to do differently?**

Under Regulation 33 of the MLRs, AML regulated firms are required to undertake EDD and enhanced ongoing monitoring "*in any business relationship with a person established in a high-risk third country or in relation to any relevant transaction where either of the parties to the transaction is established in a high-risk third country*". The EDD measures taken must include:

- Obtaining additional information on the customer and on the customer's beneficial owner;
- Obtaining additional information on the intended nature of the business relationship;
- Obtaining information on the source of funds and source of wealth of the customer and of the customer's beneficial owner;
- Obtaining information on the reasons for the transactions;
- Obtaining the approval of senior management for establishing or continuing the business relationship;
- Conducting enhanced monitoring of the business relationship by increasing the number and timing of controls applied, and selecting patterns of transactions that need further examination.

High-Risk Third Countries:

The definition of a High-Risk Third Country in the MLRs is set out in Schedule 3ZA. Schedule 3ZA lists currently the following countries: Albania, Barbados, Burkina Faso, Cambodia, Cayman Islands, Democratic People's Republic of Korea, Haiti, Iran, Jamaica, Jordan, Mali, Malta, Morocco, Myanmar, Nicaragua, Pakistan, Panama, Philippines, Senegal, South Sudan, Syria, Turkey, Uganda, Yemen and Zimbabwe. It is with respect to these countries that mandatory EDD is required to be performed by AML regulated firms under Regulation 33.

This measure would amend the list of countries defined as a High-Risk Third Country in Schedule 3ZA in order to mirror the changes made by the FATF to its lists of countries identified as having strategic deficiencies in their AML/CTF controls following its Plenary. Specifically, the United Arab Emirates would be newly defined as a 'high-risk third country' as a result of this measure and added to the list alongside the existing countries. This measure would also result in Zimbabwe no longer falling within the definition of a 'high-risk third country' and would remove them from the Schedule 3ZA.

Therefore, the new list of countries would be as follows: Albania, Barbados, Burkina Faso, Cambodia, Cayman Islands, Democratic People's Republic of Korea, Haiti, Iran, Jamaica, Jordan, Mali, Malta, Morocco, Myanmar, Nicaragua, Pakistan, Panama, Philippines, Senegal, South Sudan, Syria, Turkey, Uganda, United Arab Emirates, and Yemen.

This measure would therefore require AML regulated firms to perform EDD and enhanced ongoing monitoring when a business relationship is established with any customer or relevant transaction from the United Arab Emirates. This measure would also require EDD to be performed by AML regulated firms in relation to any relevant transaction where either of the parties to the transaction is established in the United Arab Emirates.

How many businesses will this impact per year?

Based on data collected from AML supervisors in the latest Treasury annual returns, covering the period between 6 April 2019 and 5 April 2020, we estimate that around 97,400 entities are within scope of the MLRs and will thus be in scope of the mandatory EDD and enhanced ongoing monitoring requirements relating to high-risk third countries.

- **What is the direct cost/benefit per business per year?**

Under the MLRs, AML regulated firms are required to apply EDD and enhanced ongoing monitoring in several specific instances that are deemed to present heightened ML/TF risk. In addition, AML regulated firms must apply EDD under "any other case which by its nature can present a higher risk of money laundering or terrorist financing". Regulation 33.6 states that "when assessing whether there is a higher risk of money laundering or terrorist financing in a particular situation, and the extent of the measures which should be taken to manage and mitigate that risk" a relevant person should consider "geographical risk factors". These geographic risk factors include countries identified by the FATF in their assessments. As such it is difficult to determine the full monetised costs of this measure as there is already an analogous, but less prescriptive, obligation in the MLRs to take into account geographical risk factors when assessing the level of customer due diligence (CDD) to apply.

Estimating the cost of EDD measures is difficult as this can be highly variable and depend on a business' risk appetite, business model and software solutions which will influence the costs of carrying out checks and monitoring. This also makes evaluating the cost of the proposed changes difficult as some businesses may already carry out the checks required by the measure (as part of considering geographic risk factors under Regulation 33.6). As a result, the extent to which the changes will influence EDD cost it is unclear.

Various informal estimates regarding the cost of CDD have been given as part of the 4th Money Laundering Directive and 5th Money Laundering Directive consultations with estimates of £3-£15 as the average cost of initial CDD measures[3]. However, this estimate should be treated with caution as different institutions will likely cite different average costs for CDD depending on their size, business model, customer base and risk appetite. We assume that EDD measures are between one and a half times and twice as expensive as CDD and therefore estimate £4.5-£30 as the average cost of EDD; in our calculations below, we use a mid-point value in this range, i.e. £17.25.

In terms of calculating overall EDD costs for AML regulated firms, it is difficult to establish the number of business relationships and transactions which would require EDD annually. As such, an estimate for the potential cost to the sector from performing initial EDD on customers who are established in a 'high-risk third country' which will be defined as a result of this measure, has been calculated based on the number of individuals in the UK who were born in the countries

[3] Businesses conduct customer due diligence to identify their customer and confirm they are who they say they are. In practice, this means obtaining a customer's: name, photograph on an official document which confirms their identity, and residential address, and date of birth.

included in this measure, as well as the number of UK nationals, companies, and other entities (where available) with a 'high-risk third country' nexus as a proxy for overseas branches and subsidiaries of UK AML regulated firms required to apply similar standards.

It is important to note that national origin is not itself a basis for applying EDD under the MLRs. Ongoing costs will depend on how many high-risk customers individual businesses have and would monitor yearly, how many new business relationships are established with high-risk customers, and how many relevant transactions requiring additional EDD are carried out each year.

However, this estimate should be treated with caution. Estimating the cost of CDD and EDD measures is difficult because the nature and extent of checks will vary according to perceived risks and institutions may go beyond the minimum legal requirements depending on their risk-appetite and their application of the risk-based approach. Businesses' approach to risk and access to software solution will influence the costs of carrying out checks and monitoring. This also makes evaluating the cost of the proposed changes difficult as some businesses may already carry out the checks required by the amended regulation and others may need to review their approach to EDD.

Furthermore, as there is already an existing analogous, but less prescriptive, obligation to take into account geographical risk factors when assessing the level of customer due diligence to apply, this may also influence the estimate of new costs associated with this measure as regulated businesses may already by performing EDD checks required by this measure. As such, we expect that the impact of this additional check will be limited as it forms part of a wider EDD framework already required by the MLRs.

As part of the impact assessment carried out for the 5th Money Laundering Directive, the cost/benefits estimate for EDD checks and the HRTC list as a whole (taking into account listed countries at the time) have already been calculated. For this SI measure specifically, the cost/benefit will be calculated to account for the **change in the HRTC list and EDD requirements** i.e. the addition of UAE and the removal of Zimbabwe on the HRTC list.

Costs will arise from UAE being added to the list, and costs will be reduced by Zimbabwe being removed. Our estimates are as follows.

Addition of the UAE

To calculate the transition cost of the UAE being added to the HRTC list we use the following values:

a) Individuals in the UK whose country of birth is defined as the UAE (38,000)[4]
b) UK nationals living in the UAE (100,000)[5]
c) UK companies operating in the UAE (5,000)
d) UK commercial agencies operating in the UAE (779)
e) UK brands with UAE investments (4,762)
f) Mid-point estimated cost of EDD as discussed above (£17.25)

[4] Estimates on the number of individuals in the UK whose country of birth is United Arab Emirates have been sourced from the ONS's Population of the UK by country of birth and nationality: 2020 – taken from Table B in the July 2020-June 2021 dataset.
[5] Estimates on the number of UK businesses, commercial agencies and UK brands with UAE investments have been sourced from the DiT's Exporting Guide to the United Arab Emirates https://www.great.gov.uk/markets/united-arab-emirates/.

Using the values above (a, b, c, d, e) as a proxy for potential customers, the estimated transitional increase in EDD costs is calculated in the following way:

(38,000 + 100,000 + 5,000 + 779 + 4,762) x 17.25 = 2,562,332.25

Therefore, the estimated cost of adding UAE would be **£2,562,332.25**

Removal of Zimbabwe:

To calculate the value of Zimbabwe being removed from the HRTC list we use the following:

a) Individuals in the UK whose country of birth is defined as Zimbabwe (141,000)
b) UK nationals in Zimbabwe (3,275)[6]
c) Mid-point estimated cost of EDD as discussed above (£17.25)

Figures for UK companies, commercial agencies and UK brands investing and operating in Zimbabwe were not available.

(141,000 + 3,275) x £17.25 = 2,488,743.75

Therefore, the best estimated cost of removing Zimbabwe would be around **£2,488,743.75,**

To calculate the overall cost implications:

2,562,332.25- 2,488,743.75 = 73,588.5

Using these calculations, it is therefore estimated that this SI will lead to an increase in overall costs for businesses by **£73,588.50**

To calculate the Equivalent Annual Net Direct Cost to Business per year (EANDCB), this figure will be divided by 2 (given the estimated length of time UAE is likely to stay on the HRTC list). The EANDCB reduction is **£36,794.25**.

For further context, we have also calculated the maximum transitional cost, based on an EDD of £30, which would be an increase of £188,250 in costs compared to the current HRTC list. This has been calculated in the following way:

(38,000 + 100,000 + 5,000 + 779 + 4,762) x 30 = 4,456,230

(141,000 + 3,275) x 30 = 4,328,250

4,456,230 - 4,328,250 = 127,980

[6] Estimates on the number of UK nationals resident in Zimbabwe was taken from Zimbabwe's 2017 Inter-censal demographic survey, Table 1.12: https://www.zimstat.co.zw/wp-content/uploads/publications/Population/population/ICDS_2017.pdf

5. Please confirm whether your measure could be subject to call-in by BRE under the following criteria. If yes, please provide a justification of why a full impact assessment is not appropriate:

a) **Significant distributional impacts (such as significant transfers between different businesses or sectors)**

No. While we note potential increases in compliance costs and challenges for firms, especially financial institutions with a larger customer base with a UAE nexus, including those with branches and subsidiaries in the UAE, the additional cost to business from enhanced due diligence (EDD) will depend on the nature and extent of checks, which will vary according to perceived risks. In addition, institutions may go beyond the minimum legal requirements depending on their risk-appetite and their application of the risk-based approach. Businesses' approach to risk and access to software solutions will also influence the costs of carrying out checks and monitoring.

b) **Disproportionate burdens on small businesses**

No. This measure applies to activities that are regulated under the MLRs regardless of the size of the business, so businesses regulated by MLRs can be of varied sizes. We do not anticipate that the requirements of the Instrument will have a significant impact on small businesses as the additional EDD checks form part of a wider EDD framework already required of these businesses under the MLRs.

c) **Significant gross effects despite small net impacts**

No.

d) **Significant wider social, environmental, financial or economic impacts**

No. It is possible that persons with connections to FATF listed countries, including potentially UK customers who are nationals of those countries, will be subject to increased scrutiny when establishing a business relationship with relevant persons for example banks.

National origin or nationality is not itself a basis for a customer to be treated as "established in" a particular country. The most obvious potential impact of listing is on *residents* of a listed country who do business in the UK with a regulated business. Such customers may well also be nationals of that country. Another potential impact might be on customers living in the UK who have certain family or other ties to a listed country that are associated with their race or nationality, a protected characteristic under the Equality Act 2010. For example, these customers may carry out more transactions involving residents of that country than other UK customers, or have more interests in companies based in that country which do business in the UK. EDD requirements could therefore indirectly have a greater effect on this group than on other persons.

However, there is no expected significant negative disproportionate equalities impact as a result of this measure compared to the current status quo as relevant businesses should already be factoring in FATF assessments (which the proposed measure is based on) into their risk-based approach when considering whether to apply EDD. Furthermore, the requirements of this measure do not prohibit or limit relevant businesses from providing services to individuals established in high-risk third countries, rather it requires relevant persons to apply additional scrutiny in light of ML/TF risks.

e) **Significant novel or contentious elements**

No.

Sign-off for de minimis assessment: SCS

I have read the de minimis assessment and I am satisfied that it represents a fair and proportionate assessment of the impact of the measure.

SCS of Policy

Signed: Emily Bayley Date: 21/03/2022

SCS of Better Regulation Unit

Signed: ***Linda Timson*** Date: 21/03/2022

Sign-off for de minimis assessment: Minister

I have read the de minimis assessment and I am satisfied that it represents a fair and proportionate assessment of the impact of the measure.

Signed: ***John Glen, Economic Secretary to the Treasury*** Date: 25/03/2022

Further information sheet

Please provide additional evidence in subsequent sheets, as required.