



FEDERAL GOVERNMENT OF SOMALIA

NATIONAL RISK ASSESSMENT ON MONEY LAUNDERING AND TERRORIST FINANCING

Table Contents:

EXECUTIVE SUMMARY	1
A. NATIONAL THREAT ANALYSIS	2
B. TF THREAT ANALYSIS	3
C. NATIONAL VULNERABILITY TO ML	3
D. BANKING SECTOR VULNERABILITY	4
E. VULNERABILITY OF OTHER FINANCIAL INSTITUTIONS	5
F. DNFBPs VULNERABILITY	5
G. NON—PROFIT-MAKING ORGANIZATIONS (NPOs/NGOs)	5
H. FINANCIAL INCLUSION PRODUCTS VULNERABILITY ASSESSMENT	6
I. KEY FINDINGS	6
J. RECOMMENDED ACTIONS	8
K. CONCLUSION	9
INTRODUCTION	9
1.1 OBJECTIVES	11
1.2 METHODOLOGY	12
<i>Sub-Group One – ML Threat Analysis</i>	13
<i>Sub-Group Two – National Vulnerability</i>	14
<i>Sub-Group Three – Banking and Insurance Sectors Vulnerability</i>	14
<i>Sub-Group Four– Other Financial Institutions’ Vulnerability</i>	14
<i>Sub-Group Five – DNFBPs Vulnerability</i>	14
<i>Sub-Group Six-Terrorist Financing Risk</i>	14
<i>Sub-Group Seven – Financial Inclusion Products Vulnerability</i>	14
1.3 LIMITATIONS	15
CHAPTER 1: NATIONAL ML THREAT & VULNERABILITY ANALYSIS	17
AML/CFT COMPETENT AUTHORITY	17
<i>Robbery</i>	20
<i>Theft</i>	20
<i>Trafficking in persons and Human Migration</i>	21
<i>Human trafficking</i>	21
<i>Unlawful Smuggling of Firearms</i>	22
<i>Illegal Cross Border Movement of Cash</i>	23
<i>Bribery</i>	24
<i>Drug Trafficking</i>	24
<i>Fraud</i>	24
<i>Corruption</i>	25
<i>Smuggling of illegal goods</i>	26
<i>Tax Evasion</i>	27
<i>Piracy</i>	28
1.4 NATIONAL VULNERABILITY TO MONEY LAUNDERING	29
1.5 LEGAL FRAMEWORK AND POLICY IMPLEMENTATION	29
i. <i>Methodology</i>	30

1.6	NATIONAL COMBATING ABILITY.....	33
	Quality of AML Policy and Strategy.....	34
	Effectiveness of ML Crime definition.....	35
	Comprehensiveness of Asset Forfeiture Laws.....	36
	The quality of FRC Intelligence gathering.....	37
	Capacity and Resources for FC Investigators (incl. AF).....	37
	Independence and integrity of FC investigators (incl. AF).....	39
	Capacity and Resources of the FC prosecutors (incl. AF).....	39
	Integrity and independence of FC Prosecutors (incl. AF).....	40
	Capacity and Resources for Judicial Process (incl. AF).....	41
	Integrity and Independence of Judges (incl. AF).....	41
	Quality of Border Controls.....	42
	Comprehensiveness of the customs regime on cash and similar instruments.....	43
	Effectiveness of customs controls on cash and similar instruments.....	43
	Effective Domestic Cooperation.....	44
	The formalization level of economy.....	44
	The Level of Financial Integrity.....	45
	Effectiveness of the Tax enforcement.....	46
	Availability of Independent Audit.....	47
	Availability of reliable identification infrastructure.....	48
	Availability of independent information Sources.....	49
	Availability and Access to Beneficial Ownership information.....	50

CHAPTER 2: BANKING AND OTHER FINANCIAL INSTITUTIONS VULNERABILITY 54

	Comprehensiveness of AML Legal Framework.....	61
a)	Availability and Enforcement of Criminal Sanctions.....	62
b)	Availability and Enforcement of Administrative sanctions.....	63
c)	Availability and Effectiveness of the Entry Controls.....	63
d)	Effectiveness of supervision procedures and practices.....	65
e)	Integrity of Bank’s Staff.....	67
f)	AML knowledge Bank’s Staff.....	68
g)	Banks Effectiveness with Compliance System.....	68
h)	Effectiveness of Suspicious Activities Monitoring and Reporting.....	69
i)	Availability and access to beneficial ownership information.....	71
j)	Availability of Reliable Identification Infrastructure.....	72
	Diaspora Deposit account.....	74
	Current accounts.....	74
	Saving accounts.....	75
2.2.	AUTO FINANCE.....	76

CHAPTER 3: DNFBPS VULNERABILITY 87

A)	REAL ESTATE AGENTS VULNERABILITY.....	88
B)	NOTARY PUBLIC.....	88
C)	GOLD AND SILVER DEALERS.....	89
D)	LAWYERS.....	89
E)	ACCOUNTANTS.....	90

F)	SECOND-HAND CAR DEALERS	91
CHAPTER 4: TERRORIST FINANCING RISK AT NATIONAL LEVEL		94
CHAPTER 5: NON—PROFIT-MAKING ORGANIZATIONS (NPOS/NGOS)		103
CHAPTER 6: FINANCIAL INCLUSION PRODUCTS VULNERABILITY ASSESSMENT		106
	<i>Basic Savings Account</i>	<i>108</i>
	<i>Micro Deposit and Credits</i>	<i>108</i>
	<i>Mobile Banking</i>	<i>109</i>
	<i>Local Money Remittance</i>	<i>109</i>
ANNEXES		111

ACRONYMS

AML	-	ANTI-MONEY LAUNDERING
AML/CFT	-	ANTI- MONEY LAUNDERING/COUNTERING FINANCING TERRORISM
CBS	-	CENTRAL BANK OF SOMALIA
CDD	-	CUSTOMER DUE DILIGENCE
CoC	-	CHAMBER OF COMMERCE
CEO	-	CHIEF EXECUTIVE OFFICER
CCO	-	CHIEF COMPLIANCE OFFICER
CFT	-	COUNTERING / COMBATTING FINANCE OF TERRORISM
DNFBPs	-	DESIGNATED NON-FINANCIAL BUSINESSES AND PROFESSIONS
EDD	-	ENHANCED DUE DILIGENCE
FATF	-	FINANCIAL ACTION TASK FORCE
FIs	-	FINANCIAL INSTITUTIONS
FIU	-	FINANCIAL INTELLIGENCE UNIT
FRC	-	FINANCIAL REPORTING CENTRE
FX	-	FOREIGN EXCHANGE
IND	-	IMMIGRATION & NATURALIZATION DIRECTORATE
IMF	-	INTERNATIONAL MONETARY FUND
KYC	-	KNOW YOUR CUSTOMER
LEAs	-	LAW ENFORCEMENT AGENCIES
MENA-FATF	-	MIDDLE EAST & NORTH AFRICA
ML	-	MONEY LAUNDERING
ML/TF	-	MONEY LAUNDERING / TERRORIST FINANCING
MOF	-	MINISTRY OF FINANCE
MoJ	-	MINISTRY OF JUSTICE
MOPIC	-	MINISTRY OF PLANNING
MOCI	-	MINISTRY OF COMMERCE AND INDUSTRY
HMND	-	MINISTRY OF HUMANITARIAN/NATURAL DISASTER
MOIS	-	MINISTRY OF INTERNAL SECURITY
MNO	-	MOBILE NETWORK OPERATORS
MTBs	-	MONEY TRANSFER BUSINESSES
NISA	-	NATIONAL INTELLIGENCE SERVICES AGENCY
NGOs	-	NON-GOVERNMENTAL ORGANISATIONS
NPOs	-	NON-PROFIT ORGANISATIONS
NRA	-	NATIONAL RISK ASSESSMENT
NSA	-	NATIONAL SECURITY ADVISORY
NCA	-	NATIONAL TELECOMMUNICATION AGENCY
OFls	-	OTHER FINANCIAL INSTITUTIONS
OAG	-	OFFICE OF AUDITOR GENERAL
PEPs	-	POLITICALLY EXPOSED PERSONS
RBA	-	RISK BASED APPROACH
SSA	-	SUB-SAHARAN AFRICA

SDD	-	SIMPLIFIED DUE DILIGENCE
SBA	-	SOMALI BANKERS' ASSOCIATION
SR	-	SOMALI REMITTANCE ASSOCIATION
SPF	-	SOMALIA POLICE FORCE
STR	-	SUSPICIOUS TRANSACTION REPORT
AGO	-	THE ATTORNEY GENERAL'S OFFICE
TCSP	-	TRUST AND COMPANY SERVICE PROVIDERS
TF	-	TERRORIST FINANCING
WB	-	WORLD BANK
WG	-	WORK GROUP

Disclaimer

"National ML/TF Risk Assessment of Somalia has been conducted as a self-assessment by Somalia Authorities, using the NRA ML/TF Risk Assessment Tool that has been developed and provided by the World Bank. World Bank team's role was limited to delivery of the tool; providing guidance on technical aspects of it and review/feedback to assist with the accurate use of it. The data, statistics, and information populated into National Money Laundering and Terrorist Financing Risk Assessment Tool templates, and any other finding, interpretation, and judgment under the scope of National Money Laundering Risk Assessment process completely belong to the Somalia authorities and do not reflect the views or opinions of World Bank".

EXECUTIVE SUMMARY

The Federal Government of Somalia (FGS) assumed the task of conducting its first National Risk Assessment (NRA) on money laundering (ML) and terrorist financing (TF) in compliance with FATF Recommendations¹. Somalia has undertaken the NRA exercise to identify, assess, and understand the ML/TF risks, and should take action, including designating an authority or mechanism to coordinate actions to assess risks, and apply resources, aimed at ensuring the risks are mitigated effectively.

Based on that assessment, Somalia should apply a risk-based approach (RBA) to ensure developing measures to prevent or mitigate ML/TF are commensurate with the risks identified². Another key feature of the NRA is identifying specific threats and vulnerabilities and their impact on the country, to include the economy.

Somalia's AML/CFT regime has gained momentum with the enactment of the AML/CFT Act 2016. This milestone was followed by the creation of the NAMLC³ and the FRC (the country's Financial Intelligence Unit "FIU") exercising its powers to enforce the AML/CFT regime, aimed to introduce the AML/CTF regulations to relevant institutions.

The AML/CFT law and relevant regulations are supportive in identifying the AML/CFT strengths and weaknesses of the country's legal, judicial, and financial systems. Somali authorities requested the World Bank to provide technical assistance to conduct the NRA. This exercise will enable government and AML/CFT stakeholders to better prioritize the country's AML/CFT combating strategy and to facilitate the implementation of the RBA.

The objective is to identify, assess and mitigate ML/TF risks, through adjustments and when necessary, re-assessing the country's legal and regulatory framework. These measures may also require direct policy changes. One of the key desired outcomes of the NRA process is to develop a National Strategic AML/CFT Action Plan that will assist in the allocation of AML/CFT resources, as well as assist in revising or developing guidance for "Accountable Institutions" that will ensure compliance with the AML/CFT regime.

The World Bank provided the conceptual framework in the form of an NRA tool (including excel templates). The World Bank experts have provided the technical assistance and guided the working groups in the effective use of the NRA tools. However, the findings, interpretations, and judgments of the exercise are solely the work of the working groups in Somalia, and they do not reflect the views of the World Bank. This report was produced entirely by the working groups.

¹ Assessing risks and applying a risk-based approach FATF in accordance with R.1.

² Ibid

³ Table appended

The NRA process for Somalia involved three phases, undertaken between June 2019 and December 2020, phase one: workshop conducted in June 2019 attended by 25 key AML/CFT stakeholder institutions; ii) phase two: data collection by the working groups and drafting the NRA report; iii) phase three: workshop aimed at discussing the draft report and finalizing the NRA report.

The NRA concludes with a set of recommended actions to be used as the basis to develop a National Action Plan (NAP) aimed to address the main ML/TF risks identified.

The exercise involved assessing the national ML/TF threats and vulnerabilities. The assessment of the vulnerabilities focussed on several areas to include: i) the national combating ability; ii) the sectorial vulnerabilities on the country's financial institutions and the Designated Non-Financial Businesses and Professionals (DNFBPs) and iii) the ML/TF risk of financial inclusion products.

The assessment revealed that the country faces several vulnerabilities. At the highest level, the following three cross cutting vulnerabilities affect the AML/CFT regime: the country's lack of proper identification, the lack independent sources of information, and the lack federal and provisional sources of information. Consequently, these impact the ability to establish a Know Your Customer (KYC) programs, as well as appropriate implementation of an RBA by financial institutions and other reporting entities.

Additionally, the country's LEA lack the capacity to investigate and prosecute ML criminal offenses. The country's judicial system has also similar challenges manifested by lack of ML prosecutions and investigation cases. Moreover, there have not been convictions in ML cases which is inconsistent with the country's overall level of ML risks.

The country's overall ML risk is **High**. This is affected by the national ML threat which is rated **Medium/High**, and the national vulnerability also rated as **Medium/High**. For terrorism financing, the TF level is **High** as there is terrorism activity in Somalia and increased threats of TF cases are reported. Somalia faces a significant TF threat. TF cases are identified via several mechanisms by the financial intelligence unit. However, a lack of coordination was a major challenge limiting access to official numbers at the time this report was in progress, inclusive of cases prosecuted or convicted. Additionally, the number of STRs received from the reporting entities were very low. Due to the lack of proper channels of cooperation on TF investigations, the FIU has not been able to disseminate cases to law enforcement agencies (LEAs) relating to STRs.

a. National threat analysis

In this component, authorities lacked concrete figures on values of proceeds linked with offences, specifically offenses related to ML, as LEAs hardly retain records of these types of offences. However, minor figures regarding the frequency of other financial offences committed were obtained.

The assessment is based on the measures implemented related to ML criminalization laws and regulations being effectively enforced, offenses rightly classified, LEAs ML records properly captured and maintained. ML risks and threats sources are based on tax evasion, corruption, fraud, human trafficking, smuggling in person, drug trafficking, illegal possession of firearms, theft, organized crimes, kidnapping, illegal entry, piracy, robbery and bribery.

b. TF Threat Analysis

FGS has remained a committed partner of the United States in the ongoing fight against al-Shabaab (AS) and ISIS-Somalia, taking significant steps to strengthen security sector and implement other institutional reforms designed to improve its counterterrorism capabilities.

However, AS retained de facto control over significant portions of the country, particularly in south-central Somalia, continuing to move freely, collect “taxes,” and exerting governing authority in the areas under its control. AS conducted multiple, significant, and high-profile terrorist attacks in Somalia and appeared to increasingly use targeted assassinations against key government figures and community leaders to undermine the credibility and effectiveness of FGS’s institutions⁴. Al-Shabaab also has launched external operational attacks including neighboring Kenya. Moreover, in East Africa, AS maintains a safe haven, has access to recruit Somali youth, and has the capability to increase their financial resources.

c. National vulnerability to ML

The assessment revealed that the national vulnerability to ML is **Medium/High** with a score of 0.74. This is a combination of high overall sectoral vulnerability and low national combating ability. The sectors that are most vulnerable are financial institutions and other financial services sectors followed by DNFBPs. These vulnerability levels are due to a number of factors including lack of collaboration between stakeholders, lack of regulatory enforcement, ineffective LEA enforcement, inadequate knowledge and minimal effectiveness related to the capacity of the country’s judicial system.

The national combating ability is low mainly because of law enforcement incapacity in respect to ML criminal investigation, criminal prosecution, criminal conviction, and uncertain and ineffective use of the existing asset forfeiture law. Those critical four factors have adversely impacted other 22 variables:

1. Low quality of AML Policy and Strategy
2. Ineffective of ML Crime Definition
3. Incomprehensive of Asset Forfeiture Laws
4. Low quality of FIU intelligence gathering and processing
5. Low capacity and resources for Financial Crime Investigations (incl. AF)
6. Low Integrity and lack of Independence of Financial crime investigators (incl. AF)
7. Low capacity and resources for financial crime prosecutions (incl. AF)
8. Low Integrity and lack of Independence of financial crime prosecutors (incl. AF)

⁴ Country Reports on Terrorism, CT Bureau

9. Lack capacity and resources for Judicial Processes (incl. AF)
10. Low Integrity and Independence of Judges (incl. AF)
11. Low quality of Border Controls
12. Incomprehensive of customs regime on Cash and similar instruments
13. Ineffective of customs controls on Cash and similar instruments
14. Ineffective of Domestic Cooperation
15. Ineffective of International Cooperation
16. Low level of formalization of Economy
17. Level of Financial Integrity
18. Ineffective of tax enforcement
19. Unavailability and lack of standard and practices of independent Audit
20. Lack of reliable Identification Infrastructure
21. Lack of independent information sources
22. Unavailable and lack of access to Beneficial Ownership Information

d. Banking Sector Vulnerability

The overall ML vulnerability for this sector is Medium/High. There are 11 banking products and services offered by the commercial banks that were evaluated. At least half of those products and services are entry level accounts and have low level of activities. Consequently, their individual weighted average has impacted the overall risk rating of the banking sector. Out of 11 investment vehicles listed in the banks' consolidated financial statement in 2018-2019, trade finance and real estate loans make up over 52% of banks loan portfolios. This is followed by 12% construction and personal household loans. Manufacturing and Agriculture loans both contribute only 1% in the loan portfolio⁵. Therefore, the resulting Medium/High rating in the overall ML vulnerability in the banking sector is not necessarily reflective of the true extent of the risk to exposure for banking products and services.

Despite the banks being risk averse, the real estate and trade finance are vulnerable to ML specially the current environment the banks are operating. For example, banks are not able to conduct robust background verification of the beneficial ownership a legal person. The following sections detail the vulnerability and product risk rating information.

Private banking attracts high net worth customers most of whom are public officials or Politically Exposed Person (PEPs), require proper KYC and Enhanced Customer Due Diligence (ECDD). However, supervision exercises have found KYC on these customers to be inadequate, for example, the banks disregard the risk because of the individual's status. Another category of concern is import merchants who use inconsistent invoices for international funds transfers with the aim of externalizing foreign currency and evading taxes and the lack of scrutiny of these transactions by banks.

⁵ Central Bank of Somalia

e. Vulnerability of other financial institutions

This component of the assessment comprised of both formal and informal sectors. Formal sectors are those that are regulated while informal sectors are those that are not regulated. MTBs are regulated by both the CBS and the FRC, their AML vulnerabilities are like those of the commercial Banks. The informal sector, including foreign exchange, poses High ML vulnerability as it is not regulated and there is no KYC or record keeping maintained. The informal sector had varying ML vulnerability because there is no securities sector platform in Somalia. There were foreign exchange trading activities that took place in the past; however, there is lack of substantive information as to how the LEAs have dealt with those types of incidents. The insurance sector is rated as medium risk based on their current activities. However, insurance companies are operating without oversight, they are high risk category and are exposed to ML abuses. for E-money providers operating in Microfinance which are also operating without AML/CFT oversight might be subject to ML abuses.

f. DNFBPs Vulnerability

Under this component, the assessment established that the public notary sector, especially those specialized in dealings with the real estate and agents' sector, have a high ML vulnerability; both rated 0.85 as high risk. The sectors may be targeted by PEPs and the diaspora, followed by the lawyers' society which is rated 0.76 (medium/high).

The DNFBPs sectors do not apply KYC measures, currently not using lawyers for their transactions and business activities. They do not maintain proper customer records, and do not allocate resources towards AML/CFT programs. The DNFBPs with lower vulnerability include accountants and dealers of precious stones and gold/silver dealers are rated as 0.63 and 0.60 (medium high) respectively. The reliability of these ratings may need improvement overtime considering there was very minimal data collected on this sector. However, the working group has concluded that the sectors are non-compliant in the application of AML/CFT regulations.

g. Non—Profit-Making Organizations (NPOs/NGOs)

Non-Profit organizations “NPOs” and Non-Governmental Organizations “NGOs” are types of charity organizations operating in Somalia. According to the Ministry of Planning’s NPOs/NGOs registrations office, there are 106 NPOs and 144 active NGOs registered as local non-profit organizations. The Ministries responsible to regulate the NPOs/NGOs are Ministry of Interior “MoIFAR”, Ministry of Planning “MoPIED” and Ministry of Finance “MoF”. The NPOs represent Non-Profit organizations that are locally registered, and their activities are mainly limited in the national level. Although, some NGOs are also locally established charities, NGOs are normally arranged and registered from other locations outside Somalia.

Somalia received US\$ 1.887 billion in 2019, and US\$ 2.102 billion in 2020 in official development assistance (ODA), comprised of roughly equal volumes of humanitarian and development aid. The

Somalia Development and Reconstruction Facility (SDRF) serves as both a coordination framework and a financing architecture for implementing the National Development Plan (NDP). The vulnerability in the SDRF, disbursement is cash intense as there is no overseas banking and correspondent services. Therefore, transparency in aid management diminishes when fund is channeled outside government system⁶.

There is little or no information available about their budget, financial records, and the government authorities accountable have not shared relevant financial data with the NRA Report working group. The NPOs/NGOs are majorly using for their disbursement and fund remittance through Somali Money Remittance Companies. There is no information available as to who and why they pay and which parties they are on their behalf funds being disbursed. Additionally, to being non-compliant with standards and best practices for charity organizations, NGOs/NPOs receive and remit funds through Somali remittances services companies. These are one of the main drivers that might be placing the remittances sector in Somalia and charity organizations at high risk.

h. Financial inclusion products Vulnerability Assessment

Financial inclusion products include basic bank savings accounts, basic bank credit accounts, ordinary market retail activities, mobile payments, mobile banking, locally received and payments through remittance companies, and savings and credit through unregulated micro-credit companies. Currently, commercial banks offer financial products and services focused for certain groups in the community or customers such as female or student accounts and accounts for residents in IDP camps and rural areas. These types of products have accidently emerged as financial inclusion products and are accommodating the marginalized and low-income groups.

Financial inclusion products are supposed to pose low ML/TF vulnerability. However, for financial inclusions products to qualify for a simplified method for ascertaining customer identification process, there are factors that need to be corrected by both the regulators and the service providers to make the financial inclusion products in the country pose low ML/TF vulnerability,

i. Key findings

2. Somalia completed its first ML/TF NRA in 2020 and assigns a national risk-rating as **Medium-High** for ML and **High** TF. However, the NRA's findings suffer from a lack of quantitative and qualitative data as well as limited collaboration and engagement among key stakeholders.

⁶ **On Budget:** Aid is integrated into the budgeting process and is reflected in the appropriation act. Only aid delivered on treasury in Somalia can also be reflected fully on budget, whereas aid channeled outside the treasury is considered off budget. **On Treasury:** Aid is disbursed into the Treasury Single Account (TSA), recorded on the Somalia Financial Management Information System (SFMIS), and managed through government systems.

Overall, the competent authorities have a limited understanding of the country's ML/TF risks, and the private sector has a mixed understanding of risks relating to ML and TF.

3. While Somalia has established a multi-agency approach to implement its AML/CFT regime, the country is not implementing a comprehensive and coordinated risk-based approach to combating ML and TF.
4. Somalia is using the FRC to combat ML/TF, but the agency suffers from a lack of collaboration and challenges in identifying predicate offenses and identifying and tracing proceeds that could be subject to seizure, resulting in negligible ML/TF related asset freezing or confiscation. Currently, FRC's effectiveness in disseminating information is hindered because of lack of coordinated efforts among stakeholders. To a minimal extent, FRC is accessing STRs and other reporting information from FIs and non-bank financial services entities, while none of the entities in the DNFBPs sector are currently reporting.
5. Somalia LEAs have yet to undertake ML investigations and the records for prosecution of financial crimes or related offenses, which is not proportionate to the country's the criminal activity. LEAs have not yet presented charges relating to ML activities for other predicate offenses or for autonomous ML.
6. There are limited cases convicted by the court for natural persons related to corruption. Proportionality and imposition of dissuasive sanctions against natural persons could not be assessed due to a lack of information.
7. Somalia's law enforcement efforts to combat ML are not consistent with the country's predicate offenses and risk levels.
8. In this NRA assessment, the country's ML/TF combating ability is rated low across all sectors, which increases the country's risk exposure.
9. In utilizing the penal code of Republic of Somalia and AML/CFT Law, the LEAs have measures to freeze, seize, which gives them the legal powers to deal with property subject to confiscation. LEAs are seizing some assets in predicate offences cases, but the records about the values confiscated are not available and overall, the values of confiscated assets are not proportionate with the country's ML/TF risk profile.
10. The cross-border cash declaration system is not effectively utilized to seize cash including other instruments required to be declared upon arrival/departure in Somalia borders.
11. Somalia faces a significant TF threat. TF cases are identified by number of other sources but because of a lack collaboration among stakeholders, the official sources from the Somalia's financial intelligence, registered TF cases prosecuted, or number of convictions are not officially available.
12. There are publications and reports about TF incidents available in the public domain; however, the information generated by Somali government authorities was inaccessible during the NRA process. Accordingly, TF activities pose a threat to Somalia's security and economic vulnerabilities are high. Therefore, Somalia should take steps to improve TF coordination, collaboration among regulatory agencies, LEA and the judicial section including the Office of the Attorney General to effectively combat TF.

13. There are cases of individuals prosecuted through military court under the Anti-Terrorism Act and pursuant to UNSCR 1373⁷ but there is a lack of official data from the authority.
14. Commercial Banks and Money Transfer Businesses have a good understanding of their AML/CFT obligations and have conducted internal ML/TF risk assessments, which underpin a reasonable understanding of their customers ML/TF risks. These entities apply record-keeping requirements and have risk-based CDD policies/procedures - significant deficiencies are attributed to the lack of a proper personal identification infrastructure, questionable third-party identification verification, the lack of uniformity in land registration in real estate dealings, and inadequate independent customer background checks for beneficial ownership. Consequently, their application to effectively conduct EDD measures and AML/CFT internal controls are limited. Banks and MTBs are not reporting STRs and LCTs in proportionate with ML/TF risks in these sectors which is mainly a cash-based industry.
15. Additionally, other financial services companies have a limited understanding of their ML/TF risks; they are in a nascent stage of implementing risk based CDD and internal controls.
16. Financial services entities lack proper systems to identify PEPs.
17. DNFBPs are not currently screening their customers or in compliance with the regulations which is in violation of Somalia's ML/TF Law.
18. Financial inclusion products are available and offered by MNOs, FI and non-banking financial services. Varying products are informally offered by those organizations, without conducting CDD/EDD.

j. Key Recommended Actions

- The NAMLC take a more prominent role in promoting domestic coordination amongst key stakeholders.
- Building capacity of financial crimes investigators, prosecutors, and judicial officers.
- Prioritizing training on AML/CFT for officers within the CID and the police, prosecutors from the AG's Office, and judges presiding over the financial crime cases and implementing measures that fosters domestic coordination among these key stakeholders.
- Improve the current tax enforcement system and relevant pieces of legislations are reviewed with a view of making it more effective and efficient.
- The FRC should increase its human resource capacity to ensure that it is commensurate to the size and scope of the reporting entities, which would allow for more effective regulatory oversight of the activities of all participants.
- FRC should publish periodic reports to provide stakeholders with an insight into its supervisory functions/activities and encourage for more transparency and impartiality, which may also positively influence the behavior patterns of industry partakers.

⁷ May 23, 2017 — United Nations *Security Council resolution 1373* (2001) · 2(a) Refrain from providing any form of support, active or passive, to entities or persons.

- FRC should review the current data and information available relating to the DNFBPs sector and with the collaboration of the industry gather necessary information to enhance the risk assessment of the sector.
- Increasing knowledge and understanding of predicate offences to encourage the filing of STRs by all reporting entities.
- CBS to finalize its AML/CFT examination manual and ensure that it is in line with best practice and consistent with FRC's examination manual.
- Reviewing the AML Act to evaluate whether all the international standards are met.
- Building capacity within regulators and LEAs to successfully build a case against AML non-compliance.
- All reporting entities to adopt a risk-based approach for AML risk management.
- All supervisors and regulators commit to implement AML/CTF measures in a collaborative, effective and efficient manner through the enactment of MOUs or other mechanisms.
- All public sector key stakeholders responsible for combating ML/TF are properly resourced and trained.

k. Conclusion

The NRA has been an important exercise for the country. The NRA report will assist stakeholders to understand where they are placed, and what roles and responsibilities they play in the fight against ML/TF. Results from this assessment should be a wakeup call for stakeholders to start paying attention to sectors that have the highest vulnerability. Further, it is imperative that the regulatory authorities and financial institutions will, out of this process, conduct vulnerability assessment on their products, services, customers, channels of delivery and geographical locations where they offer their services. All these efforts will ultimately lead to reduced threat and vulnerability of ML/TF in the country and enhance multi-sectoral cooperation and enables better performances.

INTRODUCTION

The threat of ML/TF has put global financial systems at risk. Money launderers continue to conceal their illicit proceeds by investing in businesses through schemes at Financial Institution (FIs), Non-Bank FIs, and Designated Non-Financial Businesses and Professions (DNFBPs). The United Nations has estimated that the criminal proceeds laundered annually amount to between 2 and 5 percent of global GDP or \$1.6 to \$4 trillion a year⁸.

⁸ FINANCE & DEVELOPMENT, DECEMBER 2018, VOL. 55, NO., *Cleaning Up, Countries are advancing efforts to stop criminals from laundering their trillions*, Rhoda Weeks-Brown

The Financial Action Task Force's (FATF) 40 Recommendations set out the international standards that jurisdictions should implement to effectively combat ML/TF and the financing of proliferation of weapons of mass destruction. FATF Recommendation 1 and its interpretative note (IN) outline general principles that may serve as a useful framework in assessing ML/TF risks in Somalia at a national level.

Consequently, Somalia's international partners, including the IMF and WBG and donor organizations have recommended that Somali authorities undertake and complete their respective NRAs. This resulting NRA is intended to provide guidance on the conduct of identifying and assessing threats and vulnerabilities of a country at the national level as required by the FATF.

This report details findings from Somalia's initial national ML/TF risk assessment and has been conducted as a self-assessment by authorities, using the NRA Tool developed and provided by the World Bank.

The country's public and private sectors containing the following list was proposed as working groups and has contributed and have developed this report:

1. The Attorney General's Office (AG),
2. Somalia Police Force (SPF),
3. the Ministry of Finance (MoF),
4. the Ministry of Justice (MoJ),
5. the Ministry of Planning (MoPIC),
6. the Ministry of Commerce and Industry (MoCI),
7. the Ministry of Humanitarian and Natural Disaster (HMND),
8. the Office of the Auditor General (OAG),
9. National Intelligence Services (NISA),
10. Academia (SIPAM and Hiraal),
11. Immigration and Naturalization Directorate (IND),
12. the National Security Advisor's Office
13. (NSA, the office of the president),
14. Ministry of Internal Security (MoIS),
15. Financial Reporting Centre (FRC) "FIU",
16. Central Bank of Somalia (CBS),
17. Somali Bankers Association (SBA),
18. Somalia Remittances Association,
19. Financial Institutions including non-Bank financial services organization, Money Transfer Businesses (MTBs),
20. Takaful/Insurance companies,
21. Mobile Network Operators (MNO),
22. Designated Non-financial Businesses and Professional Services (DNFBPs),
23. National Telecommunication Agency (NCA),

24. the Non-profit Organization and Non-governmental Organizations NPO/NGO respectively,
25. Chamber of Commerce (CoC).

The role of the World Bank team is limited to the delivery of the tool, providing overall guidance and on technical aspects on its implementation, and offered feedback to assist with the correct use of the tool. The data was populated onto templates of the NRA Tool by working groups listed above.

All findings, interpretations, and judgments under the scope of the ML/TF NRA process belong to the Somali authorities and do not reflect the views of The World Bank, its Board of Executive Directors, or the governments they represent. Nothing herein shall constitute or be a limitation upon or waiver of the privileges and immunities of The World Bank, all of which are specifically reserved.

NAMLC chart for competent authority

AML/ATF Competent Authority

FGS has designated the following Federal Government of Somalia executive members and agencies to lead Somalia AML/CTF:

Authority	Primary role within the AML/CFT
National Anti- Money Laundering Committee (NAMLC)	<ul style="list-style-type: none"> ▪ AML/ATF policy development of the national policies, framework, and program. ▪ NAMLC Task force: ML/TF policy implementations
Attorney General	<ul style="list-style-type: none"> ▪ Central authority – ML/TF Legal matters
CBS	<ul style="list-style-type: none"> ▪ Supervisory and licensing authority for financial sector
Ministry of Internal Security	<ul style="list-style-type: none"> ▪ LEAs, Criminal investigations ▪ Immigration and customs control at all ports of entry ▪ Criminal prosecutions ▪ Confiscation/forfeiture (conviction based)
Financial reporting Centre (Somalia FIU)	<ul style="list-style-type: none"> ▪ Receipt of Suspicious Transaction Reports (STR) and analysis and dissemination of STRs and other financial intelligence ▪ Supervisor for dealers in precious metals and stones and other high-value dealers ▪ FRC acts as secretariat for NAMLC and plays a key role oversight in reporting entities; receive reports, analyze, and disseminate ▪ the delegated authority for targeted financial sanctions ▪ AML Supervisory Authority for DNFBPs
The Ministry of Finance (MoF)	<ul style="list-style-type: none"> ▪ Authority tax information ▪ Domestic tax authority ▪ The Minister; MoF is appointed for NAMLC Chair
Ministry of Commerce and Industry	<ul style="list-style-type: none"> ▪ The licensing of companies and registration of legal entities (company registry)
National Intelligence Services Agency	<ul style="list-style-type: none"> ▪ Combating Terrorist and Terrorist financing,

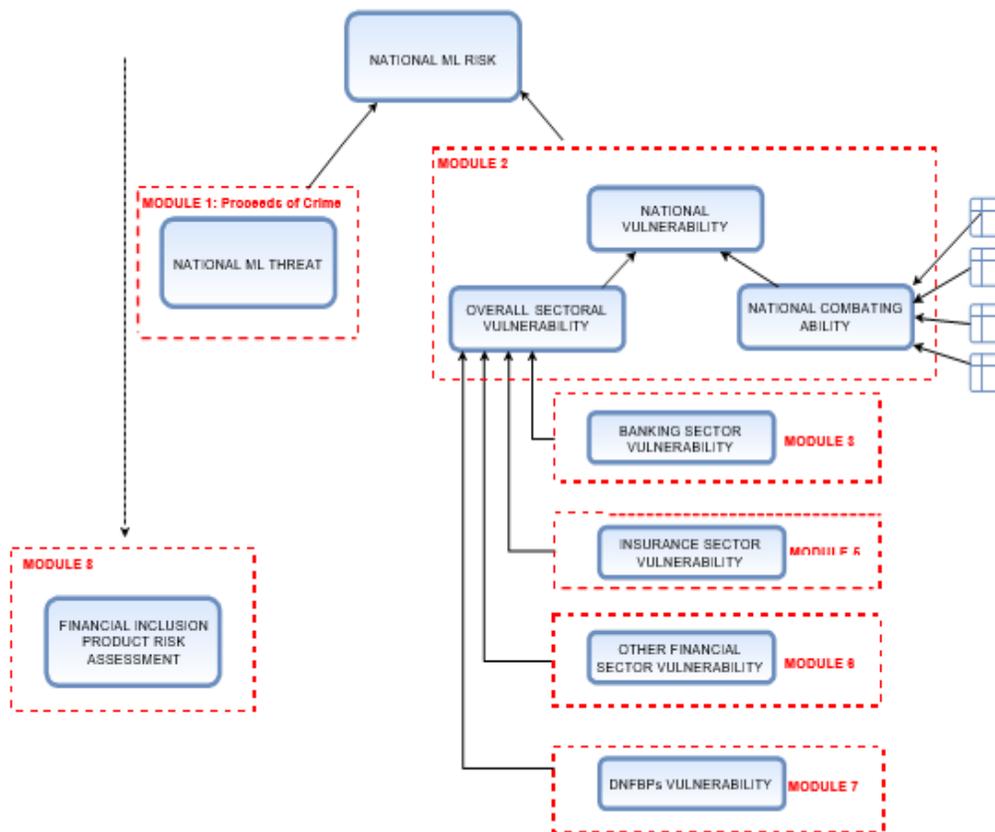
1.1 Objectives

The objectives of the NRA are:

- a) Understand the level of proceeds of crime generated in or coming into and the threat posed by ML/TF;
- b) Determine how vulnerable the economic and financial sectors are to ML and TF;
- c) Determine and understand the weakness in the legal framework, by considering the criminal and administrative justice system, and existing preventative measures; and
- d) Appreciating the best manner to allocate resources for the prevention, investigation and prosecution of ML/TF.

1.2 Methodology

Figure 1



The diagram above demonstrates the architecture of the World Bank excel template. The FRC is key coordinator for planning and bringing together the WGs for the NRA program. This led to the creation of seven (7) WGs consisting approximately 65 members.

The seven WGs were each tasked to work on one of the following modules.

1. National Threats Assessment
2. National Vulnerability Assessment
3. Banking Vulnerability Assessment
4. Insurance Assessment
5. Other Financial Institutions Vulnerability Assessment

6. Designated Non- Financial Businesses and Professions Vulnerability Assessment
7. TF Risk Assessment
8. Financial inclusion Risk Assessment

The stakeholders named above formed an NRA Working Group (NRAWG) which was further divided into seven sub-groups with each group focusing on a specific module of the World Bank risk assessment tool. The overall risk assessment was formed by the ratings of the first two groups namely: ML threat analysis and National Vulnerability. The other five groups assessed the ML vulnerability of various sectors and the results from these WG were fed into the National Vulnerability module.

It was agreed that the WG would include members of the private sector as full members, as they would add value to the process considering their hands-on experience with the institutions that would form the subject matter of the assessment.

The NRA process involved: Three stages, the first stage being a 3-day workshop, which provided a summary on the NRA concepts, and introduced the NRA tools, followed by an explanation of the assessment methodologies, and use of the NRA tool. The WGs used the information collected beforehand to populate the NRA tool, and to identify information gaps.

The second stage required the WG members to collect data, re-evaluate the inputs made during the initial workshop and populate missing data as identified during the initial workshop, and drafting an initial group report. Program continuation at the second stage was interrupted by number factors which are explained in the following pages.

The final stage of the NRA process involved a joint five-day final workshop. This workshop provided a venue for a final review of the NRA report, as well as having a discussion on the recommendations from the NRA, and a possible way forward to design an action plan.

The joint session was **NRA high-level meeting** and has attracted various dignitaries from international and national level heads of agencies and ministries, foreign country representatives and ambassadors. The participants and keynote speakers have expressed the importance for Somalia to have a National AML Strategic Plan to combat ML and TF.

The sub-groups of the NRAWGs are briefly explained below:

Sub-Group One – ML Threat Analysis

This group analyzed the ML threat, by identifying and compiling data on the criminal offences that generate proceeds of crime which can be laundered. The group also considered the level of ML external threat from neighboring countries and beyond.

Sub-Group Two – National Vulnerability

This group analyzed the national vulnerability to ML by considering how well competent authorities are equipped to tackle this problem. This included assessing the levels of training, integrity, and resources in these institutions as well as how these institutions cooperate with one another, including the extent of international cooperation.

Sub-Group Three – Banking and Insurance Sectors Vulnerability

The group assessed the vulnerability arising from the Financial Institution sectors, including the banking and insurances by looking at the AML general controls and the product specific variables which included volume, average transaction size, client profile, other vulnerable features, and the controls specific to the products offered.

Sub-Group Four– Other Financial Institutions’ Vulnerability

The groups assessed the vulnerability that arises from other financial institutions that are not part of mainly the MTBs, foreign exchange, and microfinance, MNOs and other small-time electronic payment systems offered by some money remitters. This included an analysis of the control measures that are in place in each of these sectors.

Sub-Group Five – DNFBPs Vulnerability

This group analyzed the vulnerability of DNFBPs, including the following sectors: public notary, real estate agents; second-hand car dealers, precious stones, gold/silver dealers, lawyers and accountants.

Sub-Group Six-Terrorist Financing Risk

This group analyzed the country’s TF threats and vulnerabilities levels. The group is focused as to how the current insurgents active in Somalia (Al-Shabaab). Mechanism AS uses to raise funds, what channels of delivery used, and the size of funds and other assets are stored. AS main sources of funding, and sectors that are vulnerable including NPOs, and the country’s preventive measures are analyzed.

Sub-Group Seven – Financial Inclusion Products Vulnerability

The aim here was to assess the ML/TF vulnerability arising from financial inclusion products in the country offered by several Banks and Microfinance organizations.

Data collected through the private, public sectors and other venues:

- The data collected came from databases of the FIU, MoIFAR, MoPIEC, MC, MoF, MoCI, commercial banks, MTBs, MoJ, AGO, Micro-finance Network, MTBs, Insurance

- (Takaful), entities. Public and private information were also used and are part of the NRA report.
- Questionnaires were administered to the concerned financial institutions such as banks, non-bank financial institutions, and DNFBPs.
 - Review of publications by relevant regulators, such as the CBS, FRC, Somali Institute of Certified Public Accountants, “SICPA”, legal association/Lawyers, and the Academia sector; the Somali Institute for Public Administration “SIPAM”, Hiraal Review, the Insurance Sector.
 - Telephone and face-to-face interviews were used to obtain information, following and contacts were made to clarify responses provided during WG sessions.
 - Public information sources were used including AML/CFT reports by number of publications country report on terrorism, Ministry of finance tax laws and regulations, the ML/TF Typologies Report 2019, World Bank Report on Shadow Economies, and other media publications.
 - Legislations referred to include: Somalia’s AML/CFT Law, Proceeds of Serious Crime and TF Act; Anti-Corruption Strategy, Federal Government of Somalia Penal Code 5 dealing with the country’s criminal laws.

1.3 Limitations

The NRA faced number of limitations as outlined below however, the limitations have been addressed in the recommended actions in each section of the report. Moreover, the stated limitations do not in any way undermine the results of this NRA.

- Mainly, data was not available from the targeted sources. This was common among the informal financial sector and DNFBPs. The data provided was in some instances inadequate to come up with a proper ML vulnerability rating for certain areas. This resulted in the use of common knowledge of the sectors.
- Access to data was limited. Some respondents did not have information or a statistical unit and, therefore did not see the need to find and make the information readily available.
- Reluctance of some institutions to provide information was prevalent among public and private sector institutions. There was **a lack of proper understanding of ML**.
- The non-cooperative attitude displayed by some key stakeholder institutions and not recognizing the impact of the country’s lack of corresponding banking relationships available to Somalia commercial banks and more so to the FGS were challenges, despite the benefits to be derived by all stakeholders
- Time allocated to complete phase-one of the NRA program was extended due to several reasons; COVID-19 interrupted the process to conduct working group meetings. Alternatively, VC meetings were only possible to complete working group meetings, and through to the end of the program. Going forward, the only realistic way of completing Somalia’s NRA program is to conduct the entire program through virtual meetings.

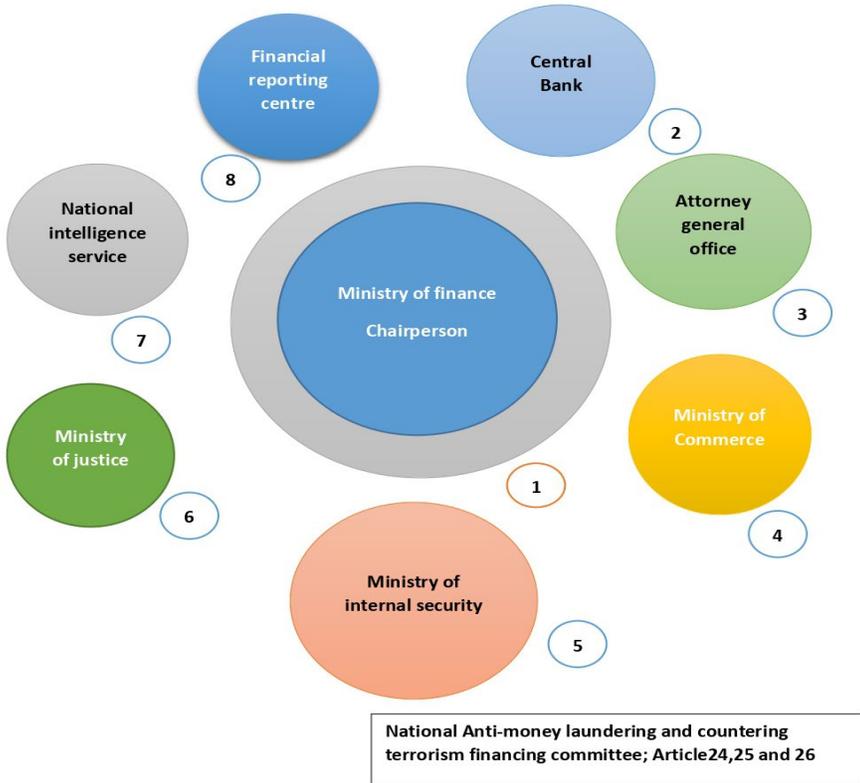
- Team members representing different institutions were mainly junior staff whose experience in the subject matters were not quite equivalent to the level of the NRA requirements.
- In other instances, the data was available, but some institutions were not forthcoming with the information. This was applicable to some private sector institutions and most of the public sector institutions.
- At the time of preparing this draft report some institutions or stakeholders had not yet submitted the requested data, despite repeated requests having been made.
- ML and TF issues are relatively new to the DNFBPs sector. Many governmental agencies, including LEAs, do not yet implement the law on money laundering, despite AML training being given in the past. The country's judicial system has no clear prosecutorial guidelines, wherein the terrorist financing is currently adjudicated through the military court, in which themselves have no experience in prosecuting TF cases.
- Proceeds generated from criminal activities are not captured in most predicate offenses, the reports by LEAs do not demand data on proceeds generated. Consequently, it was difficult to obtain reports of proceeds from crimes amid the number of investigations, prosecution and convicted cases. Parallel financial investigations are not part of standard operating procedures, and no information is available that indicates that LEAs identify and trace the proceeds or instrumentalities of crime special ML proceeds of crime.
- It was observed that data on cases handled by LEAs are not handled properly. There is little collaboration among LEAs in terms of data collection. There is no centralized database from which information could easily be accessed by LEAs. Moreover, most LEAs data is handled manually, which makes data collection a harder task for the NRA.
- NRA working groups were individuals from various institutions with limited authority, which reduced their access to the information needed to complete the NRA process. This created problems with data collection and finalization of the draft report.
- Access to data was limited, some respondents did not have information or a statistical unit and therefore, did not see the need to find and make the information readily available.
- Reluctance of some institutions to provide information was prevalent among public and private sector institutions.
- Non-cooperative attitude by some key stakeholder institutions was a challenge, despite the benefits to be derived by all stakeholders. Not recognizing the impact of the country's lack of corresponding banking relationships available to Somalia commercial banks and more so to the Federal Government of Somalia was also a challenge.

Chapter 1: National ML Threat & Vulnerability Analysis

AML/CFT Competent Authority

The Somalia has designated the following FGS executive members and government agencies as

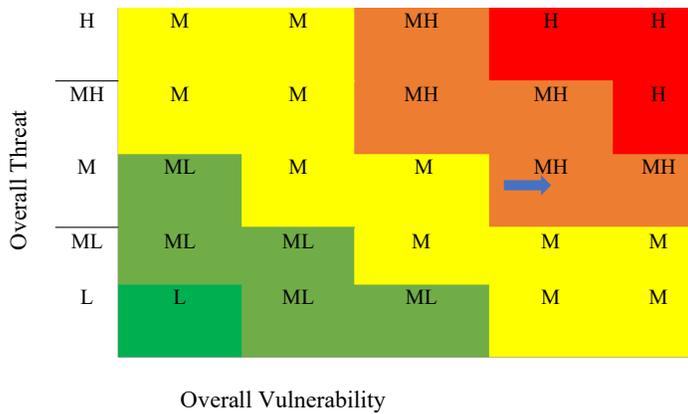
Chart 1



OVERALL NATIONAL ML RISK ASSESSMENT

- 1. Overall ML Threat (L, ML, M, MH, H).
- 2. Overall ML Vulnerability (L, ML, M, MH, H)

Figure 2: Risk level functionality Threat compared to Vulnerability.



1.

1.1. OVERALL NATIONAL ML RISK ASSESSMENT

Rating

The overall ML risk is **Medium-High**, encompassing the overall threat which is rated Medium-High and the overall vulnerability which is rated Medium-High. The findings underlying this assessment will follow. The country’s overall ML risk is rated as Medium-High takes into consideration other inputs that have low risk factors as well.

1.2. ML Threat Analysis

A clear determination and understanding of the ML threat is important in the process of assessing the ML risk. The ML threat analysis considered the level and trend of predicate offences reported. The most prevalent predicate offences the working groups have discussed are organized crimes, drug trafficking, corruption, kidnapping, tax evasion, illegal entry, tax fraud, piracy, robbery, bribery,

smuggling, illegal possession of firearms, and theft. The data surrounding the criminal offenses listed, which are the most prevailing crimes committed in the country and lead the offenders to commit crimes relating to ML cases, proceeds of crimes relating to ML charges, prosecution or convictions are unavailable.

There is a significant information gap between the number of ML crimes committed and data available resulting in the country's low ML combating ability. Somalia's penal code enables LEAs and the country's judicial system the powers to prosecute cases involving predicate offenses relating to illicit finance.

Moreover, the data shared from several institutions and government agencies are immaterial. There is little information about whether the cases handled are related to ML. Data for assets confiscated, asset forfeiture procedures, numbers of cases investigated, prosecuted, or convicted, method of investigations, number and names of LEAs involved in the investigation are unavailable. There is little information about how and who and where the assets confiscated or seized are managed. Based on the discussions of the working groups combined with expert opinions, the overall ML threat is High.

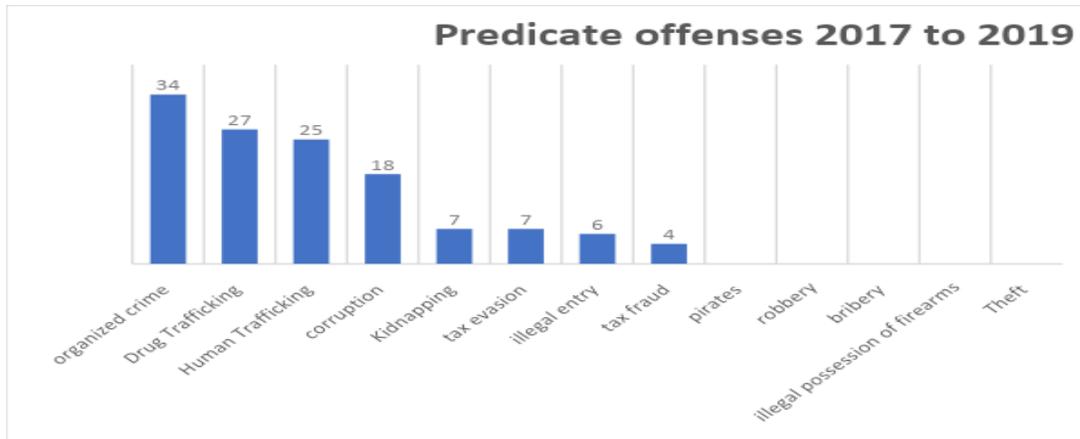
Somalia is combating corruption, strengthening its ability to cooperate with international partners, and became a member of MENAFATF, the most appropriate FSRB. As an urgent matter, Somalia criminalized both ML and TF into law in 2016. The government is working toward equipping its LEAs and judicial authorities with the resources and capacity – staffing, budget, and training – to investigate and prosecute financial crimes.

Notwithstanding, the government has increased the amount of revenue it collects, but it lacks the resources necessary to effectively improve government capacity and may continue to rely heavily on donors. Somalia is currently identified by the US Secretary of State as a Safe Haven for International Terrorism⁹.

1.3. ML predicate offenses.

Figure 3: Number of Predicate Offences From 2017 To 2019

⁹ US State Dept Terrorism Report 2016



There was limited information on values of proceeds linked with offences because LEAs have not recorded financial crimes related to ML offenses. Therefore, the assessment under this section needs to be read with this fact in mind.

Robbery

Robbery is defined as the theft done by persons who are armed with dangerous or offensive weapons or instruments. Robbery is covered under the penal code law number 5 on December 16, 1964. The number of robberies committed, or cases investigated from 2017 to 2019 are unavailable. Whether trends of occurrence in robbery cases are increasing or decreasing may not be evident based on information available. However, the working groups are of the opinion robberies with violence and incidents taking place in Somalia are prevalent. The fact that the system has no combating ability, robbery is an exposure to high risk and increases ML threat levels. Therefore, the jurisdiction's robbery incident is rated as **High**.

Theft

Theft for the purpose of deriving wrongful gain for himself or for another, takes any movable property of another personal and public property misappropriation are covered in P.C articles 480¹⁰ and crimes against the public are covered under the penal code; (*part II crimes against the public administration chapter I: crimes by public officers against the public administration*).

Number of cases investigated, prosecuted, or convicted private property. Theft or public assets misappropriation from 2017 to June 2019 are not available. Therefore, no records on the amount of proceeds identified and confiscated on theft related crimes.

Theft is a predicate offense causing proceeds of crime and ML threat level is rated as high.

1.4. Illegal Cross Border Cash, Trafficking in persons and Human Migration, and Smuggling Unlawful of Firearms.

¹⁰ Whoever, for the purpose of deriving wrongful gain for himself or for another, takes any movable property of another [24 Const.], by depriving him of the possession thereof, shall be punished with imprisonment [96 P.C.] up to three years and with fine [97 P.C.]

Trafficking in persons and Human Migration.

In 2009, IOM initiated the first counter trafficking programme in the three regions of Somaliland, Puntland, and South and Central Somalia, which generated much interest and support from regional authorities and civil society. Through its counter trafficking projects, IOM was able to further establish evidence that victims are being trafficked within and out of Somalia. In fact, findings from rapid assessments commissioned by IOM in Puntland and Somaliland confirmed that the phenomenon is indeed widespread¹¹. The exact scale of trafficking in Somalia is difficult to determine and document, due to the very nature of this crime¹².

While many community members are not aware of their vulnerability to trafficking, the level of threat is **high**. Somaliland lacked basic formal response mechanisms for emergency victim assistance and referral. This lack of awareness and subsequent lack of effective response mechanisms increased the vulnerability of people to fall prey to traffickers and posed a capacity building challenge.

As a result of conflict in Somalia people in South and Central Somalia were displaced and continue to immigrate. The displaced populations in South and Central Somalia, as well as refugees, who have fled out of Somalia to other countries such as Kenya, are highly vulnerable to human trafficking¹³.

Puntland has been identified as a source, transit, and destination region for trafficked persons. Victims are trafficked from and to Puntland as well as internationally across the Gulf of Aden to Yemen and beyond or to Ethiopia and Tanzania. Most victims are trafficked for sexual exploitation and domestic servitude. Children are more prone to international trafficking for various forms of exploitation, including organ removal.

Human trafficking

Human trafficking is the recruitment, transportation, transfer, harboring or receipt of persons, by means of the threat or use of force or other forms of coercion, of abduction, or fraud, of deception, of the abuse of power or of a position of vulnerability or of the giving or receiving of payments or benefits to achieve the consent of a person having control over another person, for the purpose of exploitation. The total number of cases investigated from 2017 to 2019 were 25.

Looking at the information on the number of occurrences, there is no trend in occurrence of human trafficking cases. The working groups indicated that there is an economic motive to human trafficking cases. There are no records on proceeds identified and confiscated. Additionally, the WG discussed that there are several human traffickers connected to North African human traffickers, known as

¹¹ <https://www.iom.int/sites/default/files/jahia/webdav/shared/shared/mainsite/activities/countries/docs/somalia/Counter-Trafficking-Somalia.pdf>

¹² Ibid.

¹³ Ibid.

“Magafe”. They are all over the country. They entice young boys and girls that there is an opportunity to go to Europe via Libya.

It is noted that there is lack of capacity to effectively enforce the existing laws against human trafficking. Additionally, the legal framework to address human trafficking is not comprehensive¹⁴. The pre-1991 penal code—applicable at the federal and regional levels—criminalized labor trafficking and some forms of sex trafficking. Article 455 criminalized slavery, prescribing penalties of five to 20 years’ imprisonment. Article 464 criminalized forced labor, prescribing penalties of six months to five years’ imprisonment. Article 457 criminalizes the transferring, disposing, taking possession, or holding of a person, and prescribed penalties of three to 12 years’ imprisonment. All these penalties were sufficiently stringent. Article 408(1) criminalize compelled prostitution of a person through violence or threats, prescribing penalties of two to six years’ imprisonment, which were sufficiently stringent but not commensurate with those prescribed for other serious crimes, such as rape. The provisional constitution prohibited slavery, servitude, trafficking, and forced labor under Article 14. Article 29(6) under the provisional constitution prohibited the use of children in armed conflict.

In November 2017, Puntland ratified a human trafficking legislative framework after three years of consultations with an international organization. The legal framework was composed of new penal and criminal procedure codes and a law that specifically prohibited trafficking. Despite the minimal reporting from the FGS, neither the federal nor the regional levels gathered or shared comprehensive statistics on investigations, prosecutions, or convictions of or related to trafficking¹⁵.

The lack of statistical data makes it difficult for the working groups to make an informed determination supported by evidence. However, the overall understanding and experience of the practitioners of the working groups do conclude that it is likely that the ML threat posed by human trafficking is **High**. **Human Trafficking ML threat is high than records reveal.**

Unlawful Smuggling of Firearms

Unlawful possession of Arms and Arm Smuggling are covered under the Somalia Penal Codes 21 and 54 (Public safety order and Smuggling/contraband, National security Law respectively). Unlawful possession of firearms and arms smuggling are most prevalent incidents subject to proceeds of crime in Somalia. The public has concealed weapons and powerful firearms in their hands in most main cities in Somalia.

Arms smuggling is critical issue facing the jurisdiction for a long time. However, cases handled and trends in occurrence unlawful smuggling of Arm cases in 2017 to 2019 are officially unavailable. No

¹⁴The current laws human trafficking laws are not aligned with conventional laws or international laws.

¹⁵ US department of State (office to monitor and combat trafficking in person), 2020 Trafficking in Persons Report: Somalia

incidents recorded and shared by the LEAs and confiscated or identified ML for proceeds of crime in relations to firearms smuggling is also not available.

The working groups have particularly discussed that the unlawful possession of firearms are the main causes of violence and robberies, concealed weapons used for assassination to government officials, clan leaders, and parliamentarian comes from unlawful possession of Firearms. Personal and family protection are also other reasons that people carry weapons. Moreover, there is an economic motive to smuggle firearms into Somalia.

On 23 January 1992, in response to the civil war and humanitarian crisis in Somalia, the UN Security Council issued an arms embargo on the country in Resolution 733. In July 2002, Resolution 1425 banned the financing of arms acquisitions and the indirect sale and supply of technical advice and military training.

In December 2006, Resolution 1725 partially lifted the arms embargo. In 2007, UN Resolution 1744 partially lifted the arms embargo, to allow the supply of weapons, military equipment, and technical training and assistance intended solely for the support or use of the African Union Mission to Somalia (AMISOM). AMISOM's purpose is to stabilize the country, prepare for its post-conflict restoration, and create the necessary security for humanitarian assistance. The embargo was further amended in November 2008 by UNSCR 1844. UNSC Committee pursuant to resolution 751 (1992) concerning Somalia.

UN Member States are required to implement the arms embargo on all deliveries of the weapons and military equipment to Somalia, including the prohibition of the financing of all acquisitions and deliveries of the weapons and military equipment, and the direct or indirect supply to Somalia of the technical advice, financial and other assistance, and training related to military activities, until the Council decides otherwise, which is set out in the paragraphs 9 and 19 of the resolution 2498 (2019)¹⁶. **Considering the arms embargo, weapons available and considering the criminal proceeds the ML Threat is high.**

Illegal Cross Border Movement of Cash

Due to customs and border security officials' lack of capacity to control points of entry, country's long borders and coastlines, the smuggling of currency into and out of Somalia remains common. However, the record available shows in 2017 to 2019 only 3 cases were handled which suggest a substandard of record keeping. Moreover, records on occurrences indicate that on illegal cross border movement of cash are unavailable. The working groups have raised that high rank public officials are able to transport cash without their luggage controlled. The most common instances are cash coming into

¹⁶ UN Security Council Resolutions

Somalia or to other East African States and/or the Middle East. **The ML level relating to the illegal cross border movement of cash into and out from Somalia is high.**

Bribery

Bribery is covered under the penal code law, Art. 241. (Peculation: A public officer [240a) P.C.]¹⁷. In Somalia, bribery is commonplace in all sectors, and procurement contracts frequently involve corruption. Businesses face corruption in the customs sector, its communal when clearing goods through the ports of Somalia. The diversion of revenue from ports is very common; for instance, in Mogadishu, revenue collected from the ports is much smaller than when compared to funds received at the Central Bank of Somalia¹⁸.

Bribery occurs at all levels in both the public and private sectors and is a visible and expected form of behavior. It affects every aspect of the Somali society: from public officials' misuse of public goods for private gain and the solicitation of bribes in exchange for basic services to the clan-based patronage networks used to obtain employment and political appointments. Businesses have likewise adjusted to the climate of lawlessness, for instance, by avoiding taxes and selling expired food and drugs¹⁹. **The ML threat due to bribery is high.**

Drug Trafficking

Drug traffickers can have great access in entering Somalia and they are capable of exporting drugs out of Somalia with ease. However, the working groups were unable to come up with concrete data in the targeted years or beyond. Therefore, there are no records indicating the ML risks identified or proceeds of crime confiscated. There is little information referring to Hashish or unrefined *Cannabis leaves*. There is a recent publication regarding cannabis farming reported in the Hiraan and Hirshabelle regions of Somalia. The police confiscated a farm and arrested 11 people connected to the case. No further information was available concerning the value of confiscated assets, and whether those suspected perpetrators arrested were charged, or whether any convictions took place.

The ML threat due to drug trafficking is high.

Fraud

Fraud is covered under sections 332 to 336 of the Somalia Penal Code. The most common type of fraud in Somalia is public funds swindling, defrauding NPOs, and defrauding procurements. No concrete data available regarding, number of cases handled in 2017 to 2019 and the amount of proceeds identified also not available. However, through the experience and expert judgment, the working groups observed that fraud cases are increasing. **The ML threat for fraud is high.**

¹⁷ Art. 241. (Peculation: A public officer [240 a) P.C.] or a person entrusted with a public service [240 b) P.C.] who, being by reason of his office or service in possession of money or other movable property belonging to the Public Administration [D.L. 20---12---1961 n. 2], appropriates it or converts it to his own use or the use of another, shall be punished with imprisonment [96 P.C.] for a term from three to ten years and fine [97 P.C.] of not less than Sh. So. 1.000.

¹⁸ Hiiiraan online January 13, 2015

¹⁹ Marqaati 2017a; Legacy Centre for Peace and Transparency 2016.

Corruption²⁰

Corruption is covered under the Somalia Penal Code 245 and 240 section (a), National **Anti-Corruption Strategy (NACS 2020-2023)** was passed at the time of writing this NRA report. Additionally, Somalia is yet to ratify the UN, the African Union²¹, and Arab conventions against Corruption. The document titled “Governance and Corruption” is approved by the Somalia Cabinet Ministries and is distributed to go through first parliamentary reading during January 2020²². (The work is in the tube).

The UN Convention against Corruption is the legally binding universal anti-corruption instrument. The Convention covers five main areas: preventive measures, criminalization and law enforcement, international cooperation, asset recovery, and technical assistance and information exchange.

The Convention covers many different forms of corruption, such as bribery, trading in influence, abuse of functions, and various acts of corruption in the private sector. A highlight of the Convention is the inclusion of a specific chapter on asset recovery, aimed at returning assets to their rightful owners, including countries from which they had been taken illicitly. Most of the UN Member States are parties to the Convention²³.

Despite Somalia having all the legal powers to fight against corruption and progress made particularly in the public financial management, the FGS’s combating ability is ineffective. Only 18 corruption cases have been recorded between 2017 to 2019²⁴, which indicates a significant exposure to corruption. Somalia has remained at “low” in the Transparency International’s Corruption Perception Index in 2019.²⁵

Corrupt government officials tolerate illegal activities in return for payments. Business is based on patronage networks, and tight monopolies dominate the market. Somalia’s Provisional Constitution criminalizes several forms of corruption (including abuse of office, embezzlement, and bribery); however, there is lack of implementation of the laws. The governing elite are continuously involved in allegations of embezzlement of public funds from the already meagre Somali coffers, providing opportunities for rampant ML.²⁶

²⁰ The Somalia penal code 5 part II “crimes against the public administration”. chapter I: crimes by public officers against the public administration, gave Somali authorities the powers to fight against corruption.

²¹ <https://au.int/en/treaties/african-union-convention-preventing-and-combating-corruption>

²² Extended Credit Facility (ECF BM item).

²³ Adopted by the UN General Assembly: 31 October 2003, by resolution 58/4. Entry into force: 14 December 2005, in accordance with article 68(1).

²⁴ Office of the Attorney General

²⁵ <https://www.transparency.org/en/cpi/2019>

²⁶ Information provided by GAN Integrity. Financial development

COVID-19 opened new avenues for corruption. The first case of COVID-19 in Somalia was confirmed on 16 March 2020. Since then, the government has received budget support from donors, but internal challenges are impeding the response. Control over humanitarian aid has remained a source of fierce competition since the collapse of the state and subsequent famine in the early 1990s, and insecurity continues to inhibit effective monitoring mechanisms.

Despite recent improvements in public financial management in Somalia, corruption remains widespread. Keeping track of the rapid influx of material donations intended to prop up a healthcare sector dominated by unregulated private actors will remain a formidable challenge.²⁷

During 2015, the government made public commitments to prevent corruption, but government took limited steps to improve transparency in its public financial management to reduce endemic corruption. The government increased cooperation with the Financial Governance Committee, a body mandated to review concession and public procurement contracts at or above a value of \$5 million.²⁸ The Ministry of Finance has increased its cooperation with the international donor community to implement public financial management reforms. Based on the number cases charged, prosecuted the country's combating level for corruption is not commensurate to the level of prevailing corruption activities, therefore **The ML threat for corruption is rated as high.**

Smuggling of illegal goods

The aim of the smugglers whether it is imports and exports loading or unloading from conveyance, or the diversion for consumption of any goods subject to customs control, is to either to defraud the Government of any duty payable thereon or to evade any of the provision of the Customs laws section. The most common type of illegal goods smuggled into are small arms, weapons, or IED components.²⁹

Only 200 miles from the border of Somalia is the city of Harar, Ethiopia. An ancient center of commerce linking Africa to the Arab world. Smugglers daily carry everything from cell phones to satellite dishes into Ethiopia, unhindered by taxes and law, dominating local markets.³⁰ Although the smugglers are beating the system, their merchandise value is not high. There are no records available for confiscated goods on either side of the borders. However, the trend in the number of occurrences of smuggling cases is increasing.

FATF defines trade-based ML (TBML) as “the process of disguising the proceeds of crime and moving value through the use of trade transactions in an attempt to legitimize their illegal origin or finance their activities”³¹. The primary aim of any TBML scheme is the deliberate movement of illicit

²⁷ civil society observatory of illicit economies, in eastern and southern Africa. Issue 9, June-July 2020

²⁸ civil society observatory of illicit economies, in eastern and southern Africa. Issue 9, June-July 2020

²⁹ By Joe DeCapua, February 12, 2013, Weapons Flowing to Somali Militants

³⁰ Smuggled Goods Dominate Ancient Ethiopian Trade Route, By Heather Murdock, June 20, 2010. VoA, Africa.

³¹ FATF-Trade-Based ML Trends and Developments. December 2020.

proceeds through the exploitation of trade transactions. In doing so, criminals may engage in a range of other potentially unlawful activities, such as preparing false invoices, mischaracterizing goods to circumvent controls, and other customs and tax violations. The aim of TBM is not the movement of goods, but the movement of money, which the trade transactions facilitate.³²

Somalia's khat ban has led to the emergence of contraband activities. In the wake of the COVID-19 pandemic, the SFG temporarily banned imports of the narcotic leaf, khat, on public-health grounds. Regional administrations quickly followed suit. After the ban, the price of the drug in Somalia's capital Mogadishu jumped as much as fifteen-fold, and new land and sea smuggling routes quickly emerged. The primary result of Somalia's ban has been a shift away from khat of Kenyan origin towards Ethiopian imports. While it is unclear if the public-health objective has been achieved, the loss of revenue to Somali authorities was significantly high.³³ As smuggling goods create proceeds of crime which is susceptible to ML, it is considered that the **ML threat of smuggling is High**.

Tax Evasion

Tax evasion is covered under the Somali suppression and Tax Violation code 12³⁴. Tax evasion is the result of deliberate suppression of facts or the deliberate distortion of facts for the purpose of evading the payment of taxes due to the local and federal governments within Somalia. Different sections under the Revenue Administration Act and the Customs Act operates in relation to these offences.

The amount of tax evasion committed in Somalia compared to the cases recorded, which is 7 cases in between 2017 to 2019, such a figure is not revealing the reality on the ground. Moreover, tax enforcement agencies and other LEAs have not shared relevant data regarding tax evasion cases.

In view of the country's current economic situation, the working groups are of the opinion that tax evasion as a predicate offence is widespread in Somalia. Data received from the Ministry of Finance with regard to reporting, investigating, prosecuting, and convicting cases related to tax evasion are relatively low. Notwithstanding, tax evasion is considered a real issue for Somalia by the working groups based on their expertise and observations. From information received and discussion within the working groups and interviews carried out, it appears that there are challenges for relevant authorities in assuming their responsibilities including conducting and collecting what is recorded as a tax evasion cases as per Somalia's penal code 12 (*rules on the assessment and repression of the violations of the financials law*). The perception is supported by the data provided by the MoF revenue department³⁵.

³² Ibid.

³³ civil society observatory of illicit economies, in eastern and southern Africa. Issue 9, June-July 2020

³⁴ LEGISLATIVE DECREE No.5 of 1 August 1966. the Penal Code

³⁵ MoF revenue department.

Moreover, in accordance with the Office of the Auditor General, the basis for adverse opinion³⁶ is as follows: “I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my opinion. Revenues collected of US \$1,350,400 and used at source without reporting. Based on my audit sample of reporting entities, there were some government ministries, departments and agencies that collected revenues amounting to a total US \$ 1,350,400 and used them at source contrary to the provisions of the Financial and Accounting Procedure (FAPS) of the State of 1961 (as amended in 1972)”.

The variable is rated that risk of tax evasion is High.

Recommended Actions

- Register existing SMEs with MoF revenue department, for FGS/local government assess taxes dues for local or federal government.
- To control of understatements of income, and overstatement of expenditures, financial statements with vouchers with expenses vouchers receipts of payments extra should be used.
- Customs involvement element of forgery, submission of incorrect records.
- Gain control of other custom related offences.
- Taxable Asset transfers on fixed assets should be introduced.

Piracy

Country’s Piracy law is covered under the decree no 14m of the 9th February 1989 as an instrument of ratification of the president of the SDR. Additionally, the Security council authorizes states to use land-based operations in Somalia, as part of fight against piracy off coast, unanimously adopting 1851 (2008), Somalia³⁷. There is other proposed piracy legislation in the pipeline, which shall address the current situation in the jurisdiction according to risk levels. However, the law awaits to pass through Somalia’s legislatures.

Despite the lack of national records availability, the UN Security Council reported that piracy has declined significantly, with no large commercial vessels hijacked or held for ransom by Somali pirates over the past few years, resulting in a decrease of ransom payments³⁸. ML threat level remains **high**, and jurisdiction is exposed to high risk so long Somalia not able to control its borders.

Recommended actions.

- Drafting of National/Regional Plans of Action to combat human trafficking, including resources and capacity building for effective investigation, prosecution and conviction of illegal cross

³⁶ Adverse opinion, section 2. Para. A, of the auditor general, 2018.

³⁷ UN Department of Public Information • News and Media Division • New York, 16 December 2008

³⁸ U.S State country report 2019

border cash, trafficking in persons and human migration, and the unlawful smuggling of firearms, and related offenses such as ML in the judiciary and LEAs.

- Community awareness campaigns and involving the media about the threats of human trafficking in persons will boost the awareness.
- Target awareness raising focus on the youth programs, schools, and college campuses street billboards and among the health care providers will serve the multitude of benefits.
- Expansion and enhancement to develop victim assistance centres and mechanisms to establish referral systems including employing post victim individuals, so they can also serve as real expert witnesses.
- Integrate, as a part of the action plan, having training and mechanisms for LEAs to identify and trace the proceeds generated by human traffickers, including protocols to conduct parallel financial investigations.
- Register existing SMEs with MoF revenue department, for FGS/local government assess taxes dues for local or federal government.
- Understatements of income, and overstatement of expenditures.
- Customs involvement element of forgery, submission of incorrect records.
- Other custom related offences.
- Taxable asset transfers on fixed assets not existent or ineffective.

Conclusion

The overall ML threat is rated as **high** due to lack of awareness of the predicate offenses, financial crimes committed which contribute to ML offenses. Moreover, the lack of collaboration among LEAs and the absence of serious consideration intensifies the domestic ML threats. The LEAs lack of capacity and ability to initiate ML investigations in financial crime and other predicate offenses. FGS's efforts to enforce tax evasion, corruption and human trafficking laws need a reform. There are a number of unaccounted theft incidents taking place within government assets, which generate proceeds of crime and are laundered through the country's economic system and transported out the country as undetected cash proceeds.

1.4 National Vulnerability to Money Laundering

1.5 Legal framework and policy implementation

In 2019, the FGS took renewed interest in police reform, appointing new leadership to key posts, including the SPF commissioner. Additionally, on September 8, 2019, the Office of the Prime Minister, the Ministry of Justice, Military Courts, the Attorney General's Office, the Ministry of Internal Security, SPF, and the Somali Bar Association approved a U.S.-supported roadmap for transferring serious cases from military to civilian courts.

Somalia has also enacted several new regulations and laws in respect of ML. This was accomplished in response to country's lack of correspondent banking relationships and the accounts closure and de-risking imposed by foreign banking institutions on Somali remittances companies in Europe and the USA.

Despite the legislations in place, ML convictions and cases relating to asset forfeitures are not recorded. Number of STRs filed are negligible, poor in quality, and did not culminate in successful ML prosecutions and convictions.³⁹

i. Methodology

National vulnerability assesses lapses in the available defenses and reactions mechanism for combating ML. Information was gathered by the NRA Vulnerability WG. The information available was largely qualitative, including interviews conducted with certain key stakeholder institutions, and the administration of questionnaires. Somalia suffers greatly from a lack of relevant quantitative data due to crosscutting issues.

Limited data was collected from relevant institutions such as the office of the Attorney General, the judicial system, and number of other stakeholders. Secondary sources also included interviews, the country's academia group, and the country ML (know your country) annual report in 2016. Information used for analyzing in this NRA report covers the period between 2017 to 2019. The objective of this module was to assess the national ML vulnerability. The overall national vulnerability is rated **Medium-High** with a score of 0.73. Overall sector vulnerability score is 0.77 (chart below) which is also rated as **Medium-High**. The National Combating Ability is rated low because of poor compliance performance levels across the board, which have directly or indirectly impacted the outcome.

The NRA is driven by over 22 input variables, given the lack of implementation of the law of the asset forfeiture, the lack ML criminal proceeds investigation practices, prosecution, and lack of ML criminal conviction. Moreover, the FIs including banks and MTBs suffer lack of conducting proper KYC, consequently, unable perform quality CDD. There are two insurance services companies operating without licenses. Additionally, the DNFBPs are unregulated and unfamiliar with AML/CFT law and regulations. Some of the other financial institutions are not properly regulated and are operating without licenses. Similarly, e-money service providers are not complying with the AML/CFT regulations.

The charts below summarize the ML national vulnerability (Chart 1) which is affected by the ML national combating ability (Chart 2) and the overall ML sector vulnerability (Chart 3). The vulnerability map in chart 4 shows the interrelationships between the factors affecting national vulnerability.

³⁹ U.S State country report 2019

CHART 1:



Figure 4: Vulnerability to Money Laundering: National Level
NOTE: Lower is better

CHART 2:



Figure 5: National Money Laundering Combating Ability
NOTE: Higher is better

CHART 3:

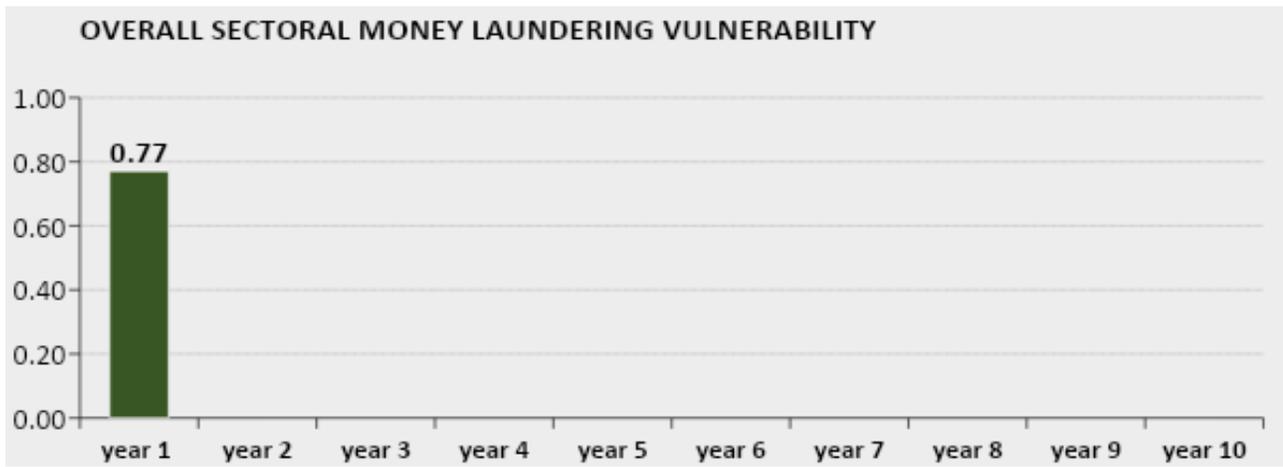
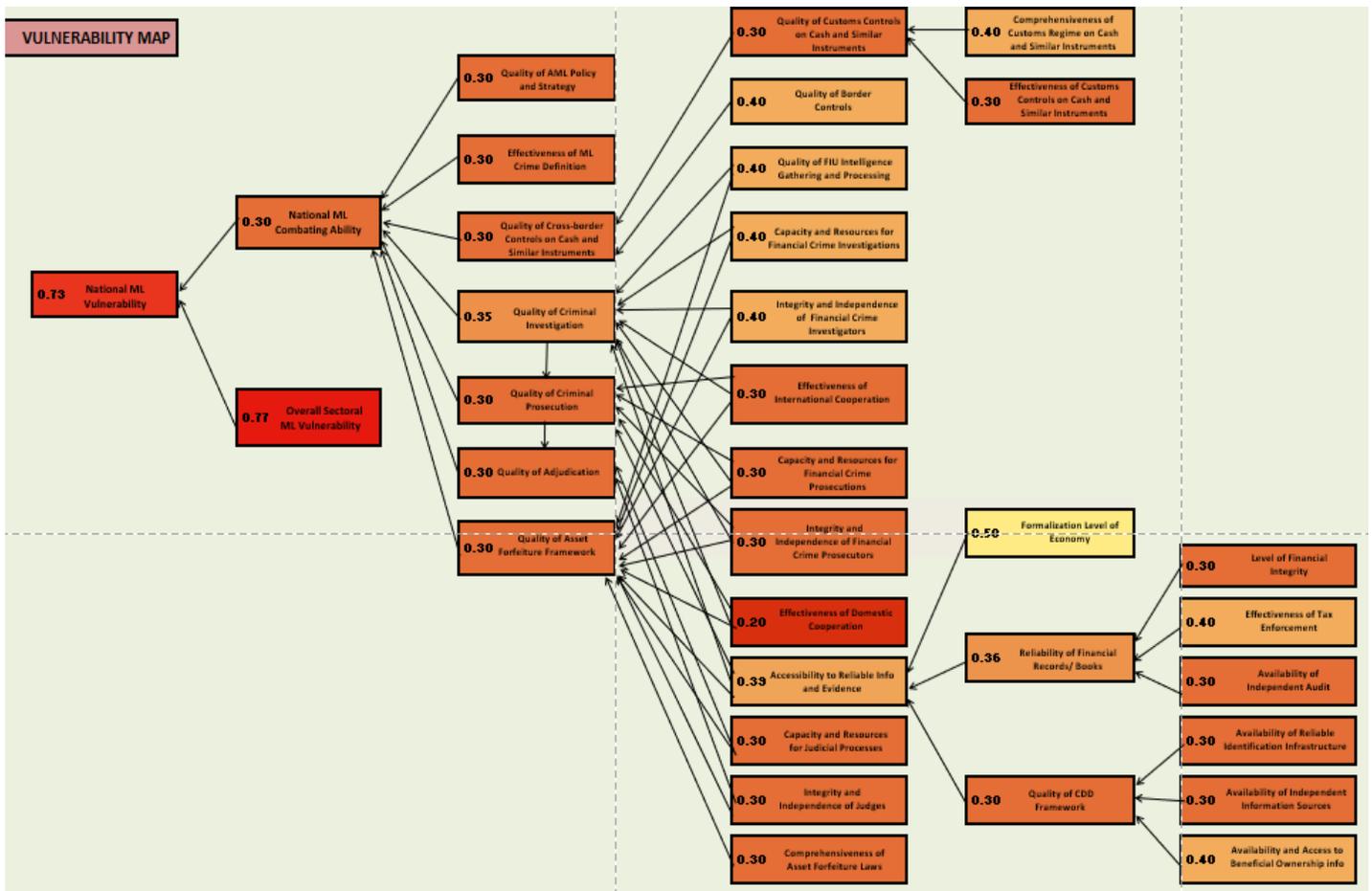


Figure 6: Overall Sectoral Money Laundering Vulnerability
NOTE: Lower is better

CHART 4: Figure 7: **ML vulnerability map**



1.6 National Combating Ability

There are a total of 22 input variables that influence the country's ability to combat ML. Information gathered from various sectors assisted in assessing the ML vulnerability of each variable.

The ML national combating ability is low with a score of 0.30, resulting the jurisdiction is not doing well concerning the ability to combat ML. The table below summarizes the most vulnerable areas under this component of the national vulnerability assessment:

Table 1: Variables of National ML Combating Ability

INPUT VARIABLES/NATIONAL ML COMBATING ABILITY FACTORS		Assessment rating	
1	Quality of AML Policy and Strategy	Low	0.30
2	Effectiveness of ML Crime Definition	low	0.30
3	Comprehensiveness of Asset Forfeiture Laws	low	0.30

4	Quality of FIU Intelligence Gathering and Processing	low	0.40
5	Capacity and Resources for Financial Crime Investigations (incl. AF)	Low	0.40
6	Integrity and Independence of Financial Crime Investigators (incl. AF)	Low	0.40
7	Capacity and Resources for Financial Crime Prosecutions (incl. AF)	Low	0.40
8	Integrity and Independence of Financial Crime Prosecutors (incl. AF)	Low	0.30
9	Capacity and Resources for Judicial Processes (incl. AF)	Low	0.30
10	Integrity and Independence of Judges (incl. AF)	Low	0.30
11	Quality of Border Controls	Low	0.30
12	Comprehensiveness of Customs Regime on Cash and Similar Instruments	Low	0.30
13	Effectiveness of Customs and Controls on Cash and Similar Instruments	Low	0.40
14	Effectiveness of Domestic Cooperation	Low	0.30
15	Effectiveness of International Cooperation	Low	0.20
16	Formalization Level of Economy	Low	0.30
17	Level of Financial Integrity	Low	0.40
18	Effectiveness of Tax Enforcement	Low	0.40
19	Availability of Independent Audit	Low	0.40
20	Availability of Reliable Identification Infrastructure	Low	0.40
21	Availability of Independent Information Sources	Low	0.40
22	Availability and Access to Beneficial Ownership Information	Low	0.40

NOTE: Higher is better performance.

The above 22 variables are explained below:

Quality of AML Policy and Strategy

The assessment established that Somalia has moderately formulated policies and structures in place. For instance, there is a NAMLC comprising of various agencies namely:

- The Ministry of Finance,
- Financial Reporting Centre (country's FIU),
- The Central Bank of Somalia,
- The National Intelligence Agency,
- The Ministry of Internal Security,
- The Attorney General,
- The Ministry of Justice and Constitutional Affairs,
- The Ministry of Commerce and Industry

The committee is proposed to meet regularly to discuss issues affecting proper implementation of AML requirements. The passing of the ML Act in 2016 and consequent AML/CFT regulations were positive signal for Somalia. However, there are challenges in implementing the laws and relevant

regulations. Majorly, there is limited political will to ensure that AML requirements are implemented at all levels.

Recommended actions

- AML competent authority shall formulate an AML policy and strategy, based on a risk assessment conducted with all relevant governmental authorities and private sector participants and updated on a regular basis.
- Implement the AML policy and strategy with RBA.
- Allocate resources and setting priorities as to the implementation of preventive and mitigating measures.
- FIs and DNFBPs also undertake their own ML risk assessments and implement measures to prevent or mitigate identified risks.
- Develop initiative in the public sector with private sector partnership to share relevant information and data.

Effectiveness of ML Crime definition

ML is criminalized under Art. 1 of the AML/CFT Act. The Act defines ML in terms of which offences constitute ML. “The AML/CFT law 2016 defines the criminalization of the ML crime as follows “Predicate offence” means any criminal offence, defined as a crime in the Criminal Code or other relevant laws, that generates illegal proceeds of crime. “Proceeds of crime” means any funds, property, or any advantage or benefit derived from or obtained directly or indirectly through the commission of an offence⁴⁰”.

While this is a positive step, ML prosecution having predicate offences has not yet taken place, as the capacity of prosecutors and financial crimes investigators which is low as indicated in the discussion below. There is a need for identification of ML cases in predicate offences investigation.

The criminalization of ML is not comprehensive. There are a wide range of predicate offenses including, tax crimes. Additionally, the penalties for ML offenses are not proportionate and dissuasive considering the seriousness of the ML offenses.

Recommended action

- ML crime should be comprehensively defined in law and enforced effectively to rightly prosecute ML crimes based in the law.

⁴⁰ <https://frc.gov.so/aml-cft-law/>

Comprehensiveness of Asset Forfeiture Laws.

Asset forfeiture is covered under the Somalia Civil Law Art. 635, which gives the LEAs the powers to enforce and to freeze, confiscate, and forfeit assets on behalf of the presiding court/judge. Additionally, Art. 21 sec 3 the AML/CFT Act gives the FRC powers to direct a FI to freeze accounts and seize assets suspected of belonging to a terrorist or terrorist organization.

Additionally, the AML/CFT Act provides for restraining orders on realizable property, confiscation orders and pecuniary penalty orders in respect of benefits derived from the commission of an offence. Under Section (2.1, 2.2 and 2.3) of the recently passed National Anti-Corruption Strategy, the NACS enables the office of the auditor general to carry out independent audits, while also having powers to apply for a court order to seize or freeze any document, or other records or evidence or asset, account, money or other pecuniary resource or wealth, property, or business or other interest. NACS will enhance and strengthen the powers of the FRC. NACS will also establish collaboration and exchange of information.

The WG discussions concluded that there are sufficient legal provisions to govern for asset forfeiture. However, because of interagency lack of collaboration and the ineffective legal framework to govern and implement the asset forfeiture provisions, Somalia has a limited investigative and enforcement capacity to deal with predicate offenses and the subsequent assets derived from criminal offenses. The key obstacles in implementing Somalia's new AML/CFT Act include: the FGS's limited capacity including pressing security threats to the government, the lack of capacity at all levels of government, and insufficient enforcement, policing, and lack of ML investigative skills.

Since the collapse of the state in 1991, Somalis have relied primarily on customary and sharia legal systems to adjudicate disputes. At moment, the legal system in both civilian and military courts nominally operate under the federal government, but existing laws are difficult to enforce, given the weak capacity of judicial and LEAs linked with general instability.

The police reportedly are responsible for investigating financial crimes. The police lack the capacity, including financial, technical, and human resources, to investigate suspected ML/TF. Deficiencies related to implementation of the asset forfeiture law are more prevalent.

Recommended actions.

- Asset forfeiture law should be reviewed for comprehensiveness to ensure that LEAs have adequate powers to effectively trace, detect, seize assets, and apply for the forfeiture of proceeds and instrumentalities of crime.
- Strengthen capacity of LEAs by boosting their skills and allocating adequate resources,

The quality of FRC Intelligence gathering

The FRC is the financial intelligence unit of Somalia. The FRC is an independent agency, operating at arm's length from LEAs including the National Intelligence Services Agency "NISA", with a mandate to collect, analyze, assess and, where appropriate, disclose information to assist in the detection, prevention and deterrence of ML and TF activities. In 2019, FRC established country's AML regulatory strategic guidelines.⁴¹

Notwithstanding FRC's independence and autonomy to perform its activities, the FRC has challenges to effectively execute its mandate. Communication and collaboration between FRC and LEAs are ineffective. Consequently, this limits the agency's ability to investigate and prosecute criminal predicate offenses and ML cases.

The FRC receives minimal number of STRs from the banking sector and MTBs. In addition, FRC is not currently receiving STRs and other reports from number of other financial institutions including insurance companies and microfinance companies because they are either not licensed or not efficiently regulated by both CBS and FRC. Moreover, the DNFBPs sectors have not yet started reporting.

Although FRC's operational capacity has improved in recent years, its oversight potential is hindered by its infancy as well as the immense challenges of regulating Somalia's reporting entities including the financial sector. Therefore, the quality FRC intelligence gathering is ineffective due to below standard policy development and coordination⁴².

Recommended actions.

- FRC and LEAs should develop AML/CFT policy and protocols to improve coordination and information exchange.
- To effectively and efficient function, FRC should be adequately structured, resourced provided appropriate training and improving the skills of the personnel, specialized in financial crimes including ML.
- FRC be given sufficient financial, technical and human resources to perform its functions.

Capacity and Resources for FC Investigators (incl. AF)

Investigating financial crimes within the context of the FATF Recommendations and pursuing ML investigations is a relatively new phenomenon for Somalia. Considering the AML law was not enacted until 2016 and the political and security challenges faced by Somalia over the past thirty years, the focus on financial crimes, resources dedicated to combating financial crimes, and the

⁴¹ Country Reports on Terrorism 2019, BUREAU OF COUNTERTERRORISM

⁴² FATF R.1

capacity to combat financial crimes were meagre. Nevertheless, Somalia recognizes the importance of financial crimes and is keen to fulfill its obligations in meeting the FATF Recommendations.

There are 53 skilled serious crime investigators recruited in Somalia; however, according to information received from the investigators, only 8 of those qualified investigators are active in the police departments and engaged in the Criminal investigation department. The other 45 investigators are now disbursed in other police departments. Some are involved in other duties, while others are inactive in the police force. 25 more people were recruited as serious crime investigators; however, they have little or no experience for investigating ML related financial crimes.

In the Attorney General's Office, approximately 17 investigators are also present to assist the Somali Police Force in the investigation of financial crimes, where amongst them, there are only 2 prosecutors trained for ML criminal investigations.

While keen to conduct financial investigations, financial investigators within all the competent authorities are severely under resourced. There are serious deficiencies in human resources and IT equipment, lack of secure servers, desktop and laptop computers, case management software systems, sufficient office space, and designated vehicles for investigations.

The Financial Crime Investigative Unit is part of the Somali Police Force, which is inadequately structured, lacks adequate funding and staffed with unskilled personnel. The Unit is not properly trained to deal with financial crimes and more importantly ML/TF investigations and asset recovery. Additionally, there is a lack of understanding by investigators of financial products and services offered by financial institutions. Moreover, the capacity to conduct financial investigations, especially complex investigations, is very low because of limited experience, limited access to information, poor record keeping, insufficient regulatory compliance, inadequate training programs, and lack of a strategic focus on financial investigations and asset recovery.

The investigating process suffers from: i) a lack of effective cooperation with domestic and international investigatory agencies; ii) limited powers for the seizure of the records held by FI, DNFBPs, and other natural or legal persons; iii) absent or poor case management systems; iv) investigator complicity, interdiction, and other issues relating to officers mishandling or not sufficiently reporting cases; and v) data unavailable about officers punished for their misconduct.

Recommended action

- The investigative agencies should be adequately structured, funded and develop skilled human resources.

- The investigative agencies should have experience and understanding dealing with financial products and financial processes.
- Develop mechanisms for LEAs to adequately utilize case management systems, including resources for an electronic platform for registering cases.
- Develop AML/CFT policy and protocols for LEAs and other agencies to improve cooperation and coordination with domestic and international authorities.

Independence and integrity of FC investigators (incl. AF)

The Investigative Financial Crime Unit of the Somali Police Force is assigned to investigate and prosecute financial crimes; however, the unit has ineffective transparency and accountability. Safeguards are not in place to preserve the integrity of the investigators or the investigations. Investigated FC or ML cases are not available in their records. Therefore, whether investigators of ML offenses and associated predicate offenses and asset forfeiture investigators can conduct investigations without fear or favor are unclear. Recently passed National Anti-Corruption Strategy sections 2.4, 2.4.1 and 2.5 are proposed to improve the professionalism of the Somali Police Force, building capacity, and strengthening effective criminal investigations, free from corruption and interventions.

Recommended Actions.

- Develop standard operation procedures for cases pursual and prioritization to ensure that the heads of the police department don't have discretion to approve or disapprove cases arbitrarily.
- Develop additional protocols to ensure that investigators should account for all cases referred to them as a part of their performances; and those records must be tangible and be free from mismanagement.
- Develop code of conduct to improve case integrity and investigator integrity must be improved.

Capacity and Resources of the FC prosecutors (incl. AF)

ML/TF cases were not reported to the Attorney General's Office in the period between 2017 to 2019. Although some prosecutors have received ML/TF Training programs and are certainly aware of the issues relating to AML/CFT, actual cases in prosecuting ML cases are unavailable.

Financial crime prosecutors lack the capacity and resources to effectively prosecute ML offenses and associated predicate offenses and proceeds of crimes relating to ML offenses. Resources including adequate financial, technical, and human resources to enable staff to carry out their duties are unavailable.

Recommended actions.

- Provide additional financial resource to invest in specialized, trained for prosecutors regarding financial crimes and related to ML and predicate offenses.
- Develop specialised training for prosecutors on the use of financial products and financial service processes.
- Enhance the technical capacity and the resources to perform the prosecutor’s functions.
- Provide access to all necessary documents, information, and witnesses and/or other relevant individuals for use in prosecutions.
- Increase knowledge and skills in understanding the flow of proceeds of crime and lack the capacity to present such cases to the court.

Integrity and independence of FC Prosecutors (incl. AF)

The prosecutors have number of challenges to overcome. Mainly, deepening the rule of law in Somalia is taking too long to fix. The formal justice system in Somalia remains very fragile, and many Somalis continue to rely on traditional dispute resolution mechanisms” (rule of law in Somalia, IDLO ASJ, Victoria Harrison Neves).

Country’s National Anti-Corruption Strategy “NACS” section 2.6 is proposed to strengthen and improve prosecutorial independence and efficiency. In the judicial chain, the office of the attorney general plays an important role in prosecuting ML cases. However, the prosecution unit is inadequately structured, poorly funded, and are not appropriately staffed with skilled and trained prosecutors, particularly, staff specialized in financial crimes, financial products, and financial processes.

The working group brought up the need that prosecutors enabled to obtain access to all necessary documents, and individual witnesses and other information for use in prosecutions.

Therefore, the kind of environment financial crime prosecutors are operating in, linked with lack of coordination and interagency collaboration, the prosecutors are unable to function independently and rightly honour with their jobs.

Recommended Actions.

- Develop standard operation procedures and protocols to ensure that prosecutions of ML and other related predicate offenses are instituted without interference, political or social pressure, corruption, intimidation, or abuse of office and properly monitored for those purposes.
- High-profile criminal cases must be dealt legally, independently with integrity and concluded in an objective and professional manner.

Capacity and Resources for Judicial Process (incl. AF)

The Somali courts and judicial system are structured. Judges are trained in law and have the skills to preside over financial crime cases. Some judges have also been trained on the AML/CFT laws and regulations and financial crimes. However, the country's judicial system lacks adequate capacity and resources to effectively undertake judicial processes for cases relating to ML offenses and associated predicate offenses, including proceeds of foreign predicate offenses, and asset recovery.

After the passage of the AML/CFT law in 2016, Somalia courts have yet to adjudicated proceeds of crime relating ML cases. Judges do not have experience and required skills to preside over prosecutions for ML offenses. The entire judicial system is understaffed and underfunded. Prevalent financial crimes are not classified as ML cases or ML charges are not included in the prosecutor's list of charges.

Recommended actions.

- There should be specialized judges in financial crimes specific to ML/TF.
- There should be a program to develop skilled and trained judges and staff, including the use financial products/services, financial investment and markets' processes and transactions.
- Sufficient technical and resources should be provided to the country's judicial system.

Integrity and Independence of Judges (incl. AF)

In the current environment in Somalia, proceedings or trials of any cases or related to financial crime offenses may not be free from interference, political or social pressure, corruption, intimidation, or abuse of office. Moreover, judges are not free from undue influence, or do not enjoy sufficient judicial independence and autonomy. Overall, the independence of the presiding judges is likely weakened by external influences. The causes of the existing challenges are often attributed to positions in the judicial system that largely include political nominees and clan referrals, among others. Normally, the main government positions are shared through the infamous 4.5 clans-based formula⁴³. Moreover, important government positions may be nominated based on clan, rather than the qualifications of the people, or judges in this case. The country's security is another factor, meaning that judges presiding over prosecutions do not function without fear or favor. Above all, safeguards are not in place to preserve the integrity of the judges.

Recommended action

- Judges to preside cases of financial crime or predicate offenses are dependent on court's capacity and resources.

⁴³In nutshell, the 4.5 formula was what the delegates of Somali Nairobi peace conference, after a much squabbles, have agreed upon. The 4.5 formula gives equal quota to the four "major" clans, and a half-point to a cluster of "minority" clans. (Wikipedia talk: Somali clan

- Judge’s independence and integrity is also dependent on ensuring that they are hired on merit, skills, and training, which will pave the way for judges to preside financial crime cases freely, and without fear or fear.

Quality of Border Controls

The Somali Police Force (SPF) is main civil law and criminal cases enforcement agency of Somalia. SPF’s duties include crime fighting, maintaining public safety, and counterterrorism. It is under the jurisdiction of the Minister of Interior Security. In emergency situations, the police can be reached by dialing 888 from any telephone in Somalia. Although SPF suffers from a lack of capacity concerning the country’s quality of Border Control, according to the Art. 6 of the penal code⁴⁴ (*Offenses committed in the Territory of the State*), the Federal Government of Somalia has continued efforts to improve civilian security within the borders.

In 2016, the United States made considerable contributions toward the development and capacity building of the LEAs. Somali LEAs’ capacities have improved markedly with U.S. mentoring and training initiatives launched in prior years. The U.S. funded SPF Joint Investigative Team (JIT) responded to more than 100 terrorist incidents, during which they collected evidence, maintained the integrity of the evidence by following chain of custody protocols, and ensuring a safe hand-over of the evidentiary materials to the Criminal Investigative Division (CID) for further processing. The National Intelligence Services Agency (NISA), Somalia’s lead counterterrorism unit, has began coordinating with the JIT during responses to critical incidents⁴⁵. Nevertheless, additional training is necessary to increase the SPF quality of border controls. It is also necessary to improve police investigation skills and interagency coordination.

Despite the efforts made, the working group assessing this module, in general, agreed that Somalia's border controls are weak. The border controls are too loose and illegal border passes are relatively convenient due to the absence of barriers and adequate LEA presence. Some of the country’s borders may be used as routes for smuggling trading goods, human smuggling, drug trafficking, and arms smuggling into and out of Somalia undetected. There are incidents where border security officials seize contraband or smuggled assets, where higher authorities intervene sometimes and order the goods to be released. Therefore, the geographical circumstances and poor border controls render the country to have insecure borders, and remain vulnerable to the smuggling of bulk cash, precious stones, counterfeit currency, and illegal goods into or out of the country. Other criminal activities are possible, specifically criminal incidents related to proceeds of crime.

Recommended actions

⁴⁴ The legislative decree NO. 5 of 16 December 1962

⁴⁵ Counterterrorism Assistance to the Somali Police Force Joint Investigative Teams (JIT)
<https://www.state.gov/counterterrorism-assistance-to-the-somali-police-force-joint-investigative-teams/>

- To protect and prevent the illegal border passes, the quality border controls capacity should be strengthened and sufficient resources allocated.
- Capacity and resources include, surveillance cameras, monitoring, transparency for criminal cases, recordkeeping and sharing information with relevant interagency and improved coordination.
- Criminal and civil cases records should be polished and available in nationwide websites.

Comprehensiveness of the customs regime on cash and similar instruments

The FRC and Customs have an MOU to detect the physical cross-border transportation of currency of a certain threshold amount \$10,000 or more, and any amounts that are suspected in relation to ML/TF. Financial service organizations are advised to get clearance from the FRC for all their cross border large cash movements.

However, the country lacks a comprehensive customs regime that allows the authorities to effectively detect and deter any unauthorized physical cross-border transportation of cash, and goods that can possibly produce the proceeds of crime. Additionally, the inexistence of appropriate sanctions for travelers making false declarations or disclosures, the law that enables customs authority take legal actions, to properly confiscate currency and other values subject to ML suspicion, renders the customs authority's actions to be ineffective.

Moreover, the laws and regulations pertinent to other financial instruments including: bearer negotiable instruments, precious stones, gold, and other minerals restraining/disclosures travelers to bear those items are unavailable.

Recommended actions.

- Develop country's comprehensive customs regime that allows for detection and investigation of illegal cross-border transportation of cash and assets.

Effectiveness of customs controls on cash and similar instruments

The customs controls on cash and similar instruments are poorly formulated. The country's lack of a well-designed legal and regulatory framework that effectively informs all travelers entering and leaving the country about their AML/CFT related declaration or disclosure obligations.

The consequences of any wrongdoing are not defined which have deterred criminal activities and have allowed authorities to effectively detect any unauthorized physical cross-border transportation of cash or other concealable assets.

Recommended actions

- Develop a comprehensive and well-designed legal and regulatory framework that effectively informs all travelers entering and leaving the country about their AML/CFT related declaration or disclosure obligations and the consequences of any wrongdoing.
- Establish preventive measures allowing the border authorities to effectively detect and deter any unauthorized physical cross-border transportation of cash, and other valuable and concealable assets.

Effective Domestic Cooperation

Somalia's FRC has several domestic cooperation agreements, has signed MOUs with the Office of the Attorney General, the SPF, and with the Immigration and Naturalization directorate. The purpose of the MOUs is improved coordination including information sharing among the parties.

Although there are cordial working relationships, the interagency relationships suffer from ineffective implementation of the country's AML/CFT law and relevant regulations. Moreover, there is little functional interagency cooperation among the high-level committee, or the country's competent authority proposed to effectively develop AML/CFT policy and coordination.

Recommended actions.

- Improve capacity and resources to FRC and other relevant agencies to boost effective domestic cooperation.
- Develop effective AML/CFT policy for coordination and cooperation.
- Promote joint investigations by relevant investigative units including, country intelligence services, investigators of financial crime, asset forfeiture investigators, customs, and tax authorities and the prosecutors of financial crime.
- Create a mechanism for stakeholders regularly meetings to share information and discuss joint initiatives, as well as to exchange intelligence and information, typologies and trends concerning the jurisdiction's AML/CFT threats.

The formalization level of economy

This variable assesses the degree to which the economy is formalized, and whether there is significant level of informal economic activity in the country. As a result of various conditions in a country, including low regulatory and law enforcement capacity, limited economic regulation, high levels of social exclusion, and/or tax considerations, many the economic activities remain unregistered and informal, whilst such activities may or may not be illegal in themselves.

Generally, records are not kept of informal economic activities, making it difficult for LEAs to access transaction and client information. Informal and/or unregistered economic activities pose challenges for LEAs when they investigate and to prosecute ML offenses and trace proceeds of crime, as well as the larger the informal economy and the lower the level of formalization of the economy. Quantitative data is unavailable to determine the level of formalization of the economy. However, the working group has discussed several scenarios including information and interviews taken from the Ministry of Commerce and Industry; FGS “MoCI” pointing that the current economic activity in the country is majorly informal; as high as over 60%. Somalia’s informality is higher than the informal economy in SSA countries averaged to 36-40 percent of official GDP in 2010-16.⁴⁶

It is important to note that the working group has identified the following weaknesses: i) DNFBPs sector are majorly informal due to ineffective regulatory guidelines; ii) LEAs lack capacity; iii) lack of economic inclusiveness, and iv) ineffective nationwide tax enforcement.

Recommendation actions.

- Somalia’s informal/unregistered economic activities are estimated as high as 60% therefore, the FGS and federal member states should coordinate to have businesses a inclusive SME to make it mandatory to register with their relevant local, federal governments, ministries, and municipalities.

The Level of Financial Integrity.

This variable assesses the level of financial integrity, focusing on the quality of business and professional ethics and tax transparency in the country. Financial integrity assesses whether the country’s tax framework provides: (1) transparency of financial matters of citizens and residents and; (2) the sharing of information by the tax authorities and law enforcement agencies, where appropriate.

In general, the level of financial integrity in Somalia is low. The current tax law covered under the number 12, enacted August 1, 1966: “Rules on the assessment and repression of violations of the financial law.” There are no clear disclosures or enforcement for transparency for businesses in Somalia. For example, a small number of business establishments, mainly hotels and restaurants, charge VAT on food and accommodations. Similarly, not all corporations are regularly charged corporate taxes. Imports often involve under-declared invoices with the aim of paying lower import duty. This is exacerbated by the inability of the tax authorities to detect, prevent, and effectively enforce tax laws. Consequently, the financial sector is exposed to supporting illegal tax evasion or tax fraud proceeds which are laundered through various financial institutions.

⁴⁶ BOX 2.6.1 Informality in Sub-Saharan Africa “world Bank 2019 report.

Sub-Saharan Africa has high levels of informality, especially in West and East Africa, low-income countries, fragile states, and commodity exporters. Policies to increase human capital and foster productivity, improve access to resources, reduce regulatory burdens, and strengthen governance have been associated with a decline in informality, which in turn has been associated with better macroeconomic and social outcomes. However, for these policies to be effective, they need to be tailored to the specific nature of informality and types of informal firms.

Somalia's financial system is mostly informal, operating outside of government oversight. The country's lack of a personal identification infrastructure and lack of independent sources of information such as credit agencies, puts financial institutions at a weak position to conduct CDD/EDD, which severely impacts CBS as regulatory body to perform its supervisory directives.

Remittance companies are the most active financial services sector providing domestic and international services. An estimated \$1.3 billion in remittances is sent to Somalia every year, primarily by the Somali diaspora residing in several countries in the world. Remittances account for roughly one quarter of Somalia's GDP, eclipsing all international aid to the country. Most remittances are routed through financial centers in the Gulf. The World Bank estimates 40 percent of all Somalis depend on remittances for their basic needs⁴⁷.

Recommended actions.

- To better the level of the country's financial integrity, the Ministry of Finance and the Ministry of Commerce and Industry should combine their efforts institute business and professionals commit to good corporate governance and standardized business activities. These activities will allow companies to comply with country's regulatory guidelines, including local and federal tax laws and country's AML/CFT law and regulations.
- Currently, the registered and unregistered alike are operating under poor business standards and practices. These factors may be corrected by setting appropriate codes of conduct, data preserving, and gathering more detailed information from existing entities. So, financial crime cases, including fraud, theft, tax evasion, ML, corruption, tax fraud can be accessed. The natural and legal persons comprehensive information can be retrieved, including enabled authorities to make decision by assessing corporate income and assets. LEAs should have access to information held by the tax authorities when they investigate ML offenses by a taxpayer, where appropriate.

Effectiveness of the Tax enforcement

This variable assesses the effectiveness and efficiency of tax enforcement in the country. It assesses whether the tax laws are enforced fully, fairly, and consistently, through regulatory actions such as tax inspection and criminal and civil litigation, to promote voluntary compliance with the tax laws and to maintain public confidence in the integrity of the tax system.

Audit inspections by tax authorities are a major tool for tackling non-compliance with the tax laws. The tax administration is weak in Somalia and most businesses operate in the informal sector and thus go untaxed. The government lacks the capacity both to collect taxes and to control the country's territory, parts of which are under the rule of Al-Shabaab. This has allowed rebel leaders and warlords

⁴⁷ Somalia economic update, August 2018

to establish their unique tax collection system from traders and businessmen operating in areas under their control⁴⁸.

Tax authorities are majorly ineffective to perform their duties. Part of the problems are inadequate capacity and lack of resources. Additionally, financial matters of citizens are not transparent. Tax declaration requirements are not properly enforced such that it is up to the individual to declare his/her tax status and in practice, there is little or no awareness regarding tax laws among citizens. As a result, both local and federal bodies charge taxes to a small number of businesses.

Recommended actions

- To improve the effectiveness of the Tax enforcement, a sustainable resources and capacity development should be allocated for tax authorities to enjoy sufficient operational independence and autonomy to undertake tax enforcement effectively and efficiently.

Availability of Independent Audit

Sound independent auditing practices increase financial transparency and ensure that proper and reliable accounting records and financial statements are available, thereby ensuring entities are less vulnerable to abuse by criminals.

The Somalia Institution of Certified Public Accountants (SICPA) is primarily established and proposed to self-regulate the professional accountants' sector in Somalia. According to interviews conducted with two of the directors on the board of the organization. SICPA was established in 2012 and has a board structure, registered with the IFAC, and extended its registration and membership to the Pan-African Federation of Accountants, the accountants body recognized throughout Africa. In 2014, the WBG declared that SICPA would draft the Accounting Act for Somalia. The draft document is ready for the Somali parliament to pass the Accounting Act. SICPA board and executives had several meetings with FGS bodies including MoF, OAG, and the Office of the Accountant General to press the body's professional body standards for operation.

It is quite difficult to measure the integrity of accountants and auditors, as the self-regulating body and the Accounting Act are not established. Government bodies are subject to auditor general's auditing standards. Government agencies and institutions have employees in accountant positions wherein most of them are not certified to qualify the accounting standards in their institutions. This is probably due to the poor remuneration package for such positions in the civil service. The challenge is the country has no self-regulating body for accountants because of the inaction of the parliament passing the Accounting Act.

⁴⁸ Risk and compliance, July 2020.

It was noted that the ministerial office neither has an internal audit unit nor a functioning financial accounting department with exception the works of the Accountant General whose main activities dealing with Single Treasury Account activities. There were no periodic internal audits conducted within the government bodies. There is no law for formal establishment of internal audits for units in the FGS except the annual audit conducted by the OAG. There are proposals and operational guidelines in the SFMIS, but except for the CBS and the MoF, the SFMIS system is ineffective and not implemented.

Without regular internal audits conducted in government bodies, there is a risk for non-compliance with laws, regulations, procedures, and policy irregularities may take long to be detected and remedial action taken in a timely manner. With the absence of periodic internal audits conducted in ministries, there is no assurance that internal controls for financial management and accountability are strong and effective to ensure that financial losses are minimized, or the risk of accounting irregularities are mitigated. Therefore, financial losses arising from errors, omissions, and commissions in ministries may take long to be detected for prompt remedial action.

Recommended actions.

- The Somali Institution of Certified Public Accountants (SICPA) and similar audit companies to be established as self-regulated entities in the professional accountants’ sector in Somalia, the existing draft law should be presented to the SFG parliament.
- The Office the Auditor General should take the enactment of the law as an eminent issue to improve the financial infrastructure of the public and private sectors.

Availability of reliable identification infrastructure

Financial transparency, customer identification and verification processes are enhanced when AML regulated institutions can verify the identity of customers using reliable, independent source documents, data, or information. A good identification infrastructure will also prevent the use of fake documents and false identities. Fake documents and false identities hamper the ability to detect and investigate ML and trace the proceeds of crime.

Currently, there is no personal national identification document in Somalia. Commercial entities, including FI sectors, recognize passports and the driver’s license as identification documents. While it’s hard to get the exact number of residents who hold those types of documents, its estimated that the percentage of the population holding those types of documents is very low. Consequently, KYC procedures are inadequate in most banks because few people possess the acceptable identification documents. Banks and commercial houses use a combination of identification methods: letters from the elders and community chiefs and employer identifications and similar pieces of ID are informally

used as identification documents. Therefore, the WGs have raised that those identifications are not sufficient and are subject to abuse and criminals may have access and use this flaw to defraud banks. As a result, the financial institutions and MTBs are not enabled to conduct proper CDD/EDD.

Customers of banks are required to indicate telephone contacts. However, currently, some consumers can buy SIM cards of telecommunication companies without being required to provide identification details. For this reason, it is not possible for banks to verify whether the telephone number belongs to the bank customer or not. Sometimes consumers can establish different numbers with different MNOs. If customers misplace them, they can easily be replaced by buying another without any verification by the telecommunication companies.

To respond to this shortfall, the FGS MoIFAR was engaged to introduce a National Digital Identification system beginning in 2019 and with support of the WBG. Other ID projects are also in process, such as ensuring citizens are registered at birth, consequently creating vital statistics as permanent personal records, but this exercise is still in progress and long overdue.

Recommended actions.

- A secure national identification system with government issued identity documents, whether issued by the national or a local authority are all acceptable so long the identification meets AML/CFT standards and practices⁴⁹. FGS should promote full-fledged standards of customer identification, required personal ID, public and private verification centers used as independent sources of information.

Availability of independent information Sources

Independent and reliable sources of information is one of the main pillars for reporting entities to perform a better-quality customer due diligence process. Reporting entities can identify, verify and designate customer risk level, and develop preventive measure for high-risk customers. Additionally, the banks can prevent and deter ML and TF activities. For banks to meet their AML compliance obligations, the availability of independent information sources allows them to report suspicious transactions.

FIs can benefit from such valuable sources of information and verify clients' transactional patterns and customer commercial history. Additionally, other users of independent information sources such as LEAs can investigate financial crimes.

Independent information may be sourced from a data held by credit bureaus, detailing previous banking and other business relationships, and the availability of utility bills, such as electricity, water, and telecom/internet bills.

⁴⁹ FATF R.1

A credit bureau is not available in Somalia. While utilities bills are obtainable, the reporting entities are not using utility bills as a form of identification. The primary reason is the utility service providers are not following a formal process of registration or the information collected is not up to the standards acceptable for regulated entities.

In the absence of those immense benefits, at the moment, independent information facilities or sources are not available in Somalia. In exchanging information or ease of access, both the public and private entities are facing similar hurdles.

Businesses and financial institutions are unwilling to exchange information, and sometimes have internal policies restricting others to access their records. Additionally, there is lack of existing public systems and protocols that may have encouraged the private sectors the benefits of exchanging information between industries.

A limited number of government department or agencies have developed interrelationships by way of MOUs to access with each other's records. Otherwise, exchanging information and willingness to openly communicate are similarly hard in the public sector.

An often-stated defence is the country has no data protection laws. However, in view of the current situation, where government institutions are operating under capacity levels, defensive data protection will only prevent progress. Instead, data and consumers' information should be merged and shared, so all users benefit from the access of centralized independent information sources.

Recommended actions

- FGS should take action to establish comprehensive and reliable public information systems that assist in the verification of clients' details, together with private and independent sources of information centers such as credit bureaus, existing utilities companies may also be improved, by collecting standardized data useful for third party users for verifications and for patrons to conduct business with reporting entities.
- Develop comprehensive and reliable historical sources of information through private companies, FIs and DNFBP associations, will create and improve data centres and improve the overall public sector data centres in the country, accessible to all stakeholder and including consumers.

Availability and Access to Beneficial Ownership information

The regulation of the company law enacted in 2019 is in its early stages and is currently ineffective in addressing AML risks with the types of companies registered. However, according to the office of the registrar of companies, articles 8, 9, 13 of the regulation for company registrations identifies and describes the types of corporations and the process of creating legal persons.

Technically, the guidelines for beneficial ownership information on legal persons, including the number of shareholders and their information, number of shares issued, and their addresses information are stated in the regulations, despite that, current company regulations are not precisely aligned with the FATF Standards.

As per requirement, when financial institutions engaged with legal persons, they should evaluate the risk associated with their customers in accordance with the guidance. Therefore, the financial institutions are subject to adhere the country's AML/CFT law 2016⁵⁰.

However, the FIs have a number of limitations to perform quality customer due diligence, because of the lack of transparency relating to beneficial interests in corporations or similar entities, amplified by not have the access of detailed company information, through publicly available independent information sources, to verify company structure, controls, shareholders, and beneficiary ownership information. Moreover, in the absence of beneficiary ownership data sources, the first NRA report produced in 2020 was not able to capture the number of legal persons that exist in the jurisdiction.

Moreover, In the new commercial law or company law, the information retained for the benefit of achieving beneficiary ownership is not compatible for the AML/CFT law and regulations. The information gathered by the MoCI is not available for access by the public and reporting entities and including country's competent authority in a timely manner.

Ina additions, the capacity of prosecutors, financial crimes investigators and that of presiding officers has been identified as a problem area. The authorities such as CID, AG, and MoJ need to consider training of officers in the SPF. These institutions were trained back in 2015 and 2016 by the US State Department and World Bank. This was in the early stages of the AML/CFT regime. Since then, the group received training to respond to the country's predicate offenses; however, ML cases have proven immaterial. There must be deliberate efforts by the authorities to enhance AML capacity of the officers involved in the proceeds of crime.

Recommended actions

- Tax laws and tax administrations should be strengthened, and a task force should be established to promote enforcement.
- Tax, fraud, and evasive tax activities should be criminalized without exceptions.
- The allocation of sufficient resources towards AML/CFT activities for FC crime investigators, prosecutors, and judges. These institutions fail to function due to a lack of resources and support to conduct ML investigations and prosecutions.

⁵⁰ AML/CFT law, 2016 art. 5 (customer due diligence)

- The Revenue section of the MoF should focus on tax declarations and make them mandatory, and implement measures promoting compliance with tax obligations and sanction those non-compliant to include pursuing and/or supporting ML investigations.
- MoF should also work with stakeholders to make it mandatory for businesses to produce a tax registration number before opening a bank account or renewing their business licenses. This will ensure that all businesses are registered for tax purposes and therefore it will be easy for the revenue department to follow up with businesses.

1. OVERALL SECTORAL VULNERABILITY

The other component fed into the assessment of national vulnerability is the overall sectoral vulnerability. This component combines the WBG findings from the other modules on various sectors. The sectors considered are the banking sector, insurance sector, other financial institutions, MTBs, microfinance, and DNFBPs. Assessment of these components are explained in detail in the subsequent sections of this report.

The overall vulnerability of the sector is **Medium-High** with a score of 0.77 on the assessment tool. The results from these sectors are summarized in the table below.

Table 3: Overall Sector Vulnerability

SECTORS	FINAL VULNERABILITY SCORE	WEIGHTS
Banks	0.68	0.6
MTBs	0.66	0.5
Insurances	0.72	0.3
MNO	0.87	0.7
TMT	0.62	0.3
Microfinance	0.71	0.3
Real Estate & Agents	0.85	0.2
Lawyers	0.75	0.4
Notary Public	0.87	0.4
inflow/outflow NGO	0.84	0.4
NPO/NGO	0.84	0.4
Accountants	0.63	0.3
financial inclusion	0.84	0.4
E-Money personal	0.86	0.4
E-Money Business	0.88	0.4

The banking vulnerability is **Medium**. The banking sector is regulated, and it follows AML/CFT regulations. Despite banking sector efforts, their performance is directly or indirectly impacted by other factors beyond their control, and which have increased their level of vulnerability such as the cross-cutting themes.

The insurance sector, despite its importance in the financial sector, is essentially inactive and unregulated. There are one or two companies whose activities are relatively minimum. Currently, they are not in compliance with AML/CFT regulations. The companies are registered with the CBS and are regularly participating in regulatory events, including multinational capacity building, and training programs. Insurance/Takaful companies are vulnerable with a rating of **medium-high** risk.

Other financial institutions have mixed status, where some of them are regulated, and registered with the country's FIU. But there are number of other financial institutions operating without oversight. The MNOs currently offering e-money and microfinance companies are not in compliance with the AML/CFT law and regulations. The most vulnerable financial institutions are the unregulated organizations: microfinance, foreign exchange, MNO, and TMT have higher risk levels. MTBs are regulated by the CBS and by far are the most active businesses, their vulnerability rating is **Medium**. The MTBs are also vulnerable, in similar ways as the banking sector. Foreign exchange markets are unregulated and their vulnerabilities to AML/CFT are rated **High** and are subject to fraud and abuse.

The main priority areas (in order of highest ranked in terms of vulnerability) for the authorities and the stakeholders to improve are as listed below:

Table 4: Priority Areas

Sectors	Laws enacted/regulation	Regulated	AML/CFT complia	Risk level	Requirements
E-Money Business	Partially regulated	FRC/CBS/NCA/MoF/MPTT	not compliant	high	Register with FRC, comply with AML/CFT regulations, meet reporting requirements
Notary Public	Partially regulated	MoJ/FRC	not compliant	High	Register with FRC
MNOs	Partially regulated	FRC/CBS/NCA/MoF/MPTT	Not compliant	high	Register with FRC
E-Money personal	Partially regulated	FRC/CBS/NCA/MoF/MPTT	Not compliant	high	Register with FRC
Inflow/outflow NGO	Partially regulated	FRC/CBS/NCA/MoF/MPTT	Not compliant	high	Register with FRC
NPO/NGO	Partially regulated	MoIFAR/FRC	Not compliant	High	Register with FRC

Real Estate and Agents	Partially regulated	MoF/FRC	Not compliant	High	Register with FRC
Financial inclusion	Partially regulated	CBS/FRC	Not compliant	High	Register with FRC
Lawyers	Partially regulated	MoJ/FRC	Not compliant	high	Register with FRC
Microfinance	Unregulated	CBS/FRC	Not compliant	high	Register with FRC
Insurance	Unregulated	CBS/FRC	Not compliant	high	Register with FRC
TMT	Unregulated	FRC/CBS/NCA/MoF/MPTT	Not compliant	high	Report to FRC, register with regulators
Accountants	Unregulated	FRC/OAG	Not compliant	high	Register with FRC.
Banks	Regulated	FRC/CBS	compliant	Medium	Strengthen AML/CFT compliance policy and procedures, supervisory oversight with RBA.
MTBs	Regulated	FRC/CBS	compliant	Medium	Strengthen AML/CFT compliance policy and procedures, supervisory oversight with RBA.

Chapter 2: Banking and other financial institutions vulnerability

- 1.
- 2.
- 2.

3.1. BANKING SECTOR VULNERABILITY

Context Background

Somalia descent into a civil war in 1991 hence, all major economic activities were disrupted by the conflict, which led to the collapse of agriculture, manufacturing, and the country's banking system. Prior to the civil war, there were no private banks in Somalia. The commercial banking activities including correspondent banking, savings and loans, international trade activities and all other financial services were handled by government banks.

Therefore, the private banking system was emerged after the civil war. During the conflict, major businesses were operating in a less restrictive business environment. As early as 1992, private Telecom companies were offering telephone services, and since 2002, Hormuud Telecom, the largest telecom company started offering telephone banking without AML/CFT regulatory oversight.

In 2012, the Country’s Financial Institution Law and Central Bank Act were reinstated. In 2009, the Central Bank of Somalia licensed the first private bank and in 2010, more Commercial Banks were licensed. Currently, there are 13 Commercial Banks licensed, wherein 11 Banks are operational at moment. The size of the commercial banks in Somalia is growing as well as total assets value, equivalent to 556.2 million USD, and in 2019, the banks’ GDP contributions stood at 8%. The figures are relatively low compared to the commercial banks in the region (Horn of Africa), but they are expected to continue gaining momentum and maintain a positive upward trend. The expected growth potential is over 30% in 2020⁵¹.

In view of the current environment, the interoperability between commercial banks and other financial services are limited or non-existent therefore, all personal and business transactions are based on cash. Regarding supervision and regulatory oversight, the Central Bank of Somalia “CBS” has the legal mandate to regulate the Commercial Banks⁵². The CBS executes this responsibility through the Licensing and Supervision Department “LCD”. in addition to on-site supervision, the department conducts off-site supervisions based on the regular submission of reports.

All commercial banks are also registered with Financial Reporting Centre (FIU, Somalia). The FRC has the legal powers (AML/CFT Law 2016) to regulate the reporting entities to ensure they comply with the AML/CFT law and regulations, including reporting entities meeting their reporting obligations. Financial Institutions are required to develop policy and procedures pertinent to risk-based approaches⁵³. The compliance policies and procedures should address: risk assessment for their customers, products/services, geographic locations, and delivery channels as well as retaining records for high-risk transactions.

AML/CFT policies should be revised as it becomes appropriate. Internal and external audits should be conducted to test the effectiveness of the AML/CFT compliance program. Financial institutions should set up mechanisms to monitor designated risk customers and transactions⁵⁴, identify unusual business activities, and report suspicious transactions to the FRC⁵⁵. All relevant information regarding the transaction should be shared with the FRC as well⁵⁶.

⁵¹ CBS consolidated financials

⁵² fil law 2012 & the CBS Act 2012 confer the CBS to having supervisory and regulatory oversight.

⁵³ AML/CFT reg. Article 2: AML/CTF Compliance Policies and Procedures, FAFT R.1

⁵⁴ AML/CFT law 2016 art. 11

⁵⁵ AML/CFT law 2016 art. 14. FATF R.20

⁵⁶ AML/CFT law 2016 art. 13

The CBS has implemented regulatory and supervisory reforms which have assisted them in becoming in line with international standards.

Despite continue CBS reforms, many regulatory and supervisory challenges remain:

- Risk and macroprudential analyses are weak, which is reflected in the lack of financial sector data, as well as the fragmented regulatory and supervisory framework and/or weak coordination among national regulators.
- Supervision departments do not have sufficient resources to carry out their tasks properly.
- Enforcement of prudential norms needs to be improved.
- Legislative and regulatory developments are lagging behind compared to market developments, banking advancement including;
 - National payments system and its legislation.
 - Microfinance regulation, insurances law, and, mobile banking regulation regarding AML/CFT.
 - Credit reference bureau law and regulation.
 - Insurance law and regulations.
 - Most of the above establishments also need to set up their respective self-regulating bodies.

The banking sector was assessed by the WGs involved in the AML/CFT regulatory environment. Therefore, participants were relatively more prepared and understood the subject matter compared to other NRA WGs.

The data and material evidence evaluated were contributed by five (5) Commercial Banks. The five banks were selected because, they were the only banks capable of providing reasonable data and materials to form a factual representation of the commercial banking sector. Questionnaires were sent to all banks to collect data and qualitative information and all banks have participated. During the AML vulnerability analysis, the working group discussed the banking products, transactions, client profile and degree of controls existing for each product were assessed containing 11 banking sector AML vulnerability variables. The outcomes were fed into the excel-based banking sector vulnerability assessment modules provide by WBG. The deficiencies identified and together with the required actions plans were noted.

3.2. Overall Findings

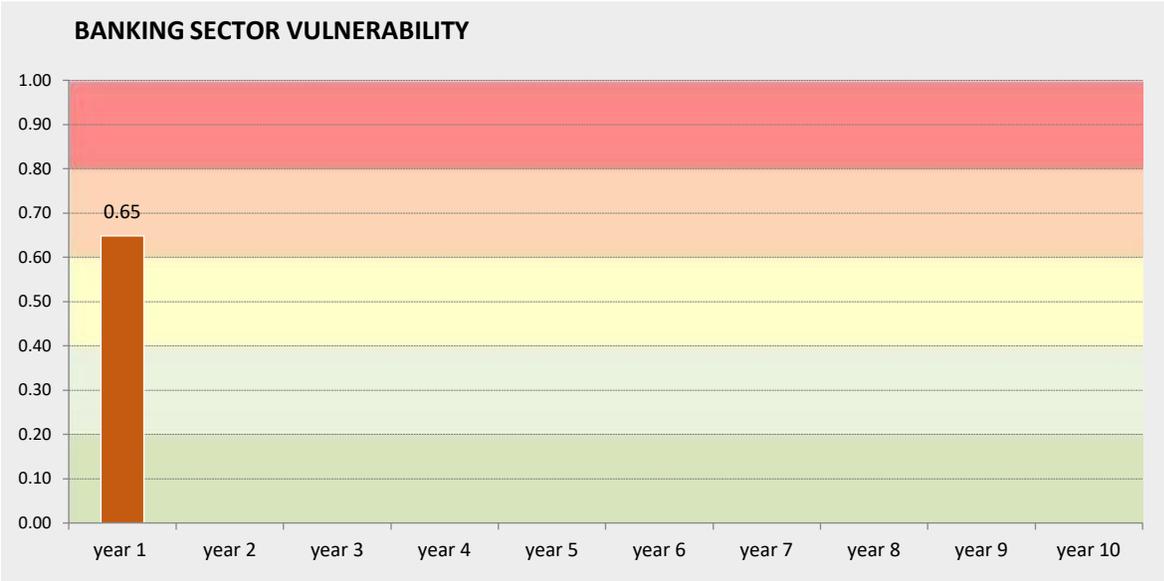
The vulnerability of the banking sector is dependent on the strength of AML general controls and product specific variables. The overall banking sector vulnerability to ML risk is rated medium with a score of 0.65. This is due to the quality of CDD framework, which is low with a rating of 0.30. Other factors are rated low, medium, or medium-high performance. Some products/services that seem like high performers as result of low transactional levels are otherwise vulnerable.

The most vulnerable banking products/services is Trade Finance with a vulnerability rating of 0.87, which is high, followed by Construction Finance with a rating of 0.86. Real East Finance is rated with a high level of vulnerability (0.85) followed by the Wire Transfers and Diaspora Saving Accounts scores at 0.82 and 0.81, respectively (both corresponding to high vulnerability). Personal/household loans represent 15% of consumers' leisure goods.

The productive sectors of the economy such as the agriculture, manufacturing, travel, tourism, and hospitality sectors in general contribute only 3% of the banks' loan portfolios. Other mixed least vulnerable banking products categories include the products seemingly dedicated low-income female accounts such as Marwo and Maandeeq accounts assigned for entry level female accounts and student accounts, considered as Financial Inclusion products will be discussed in the financial inclusion section below.

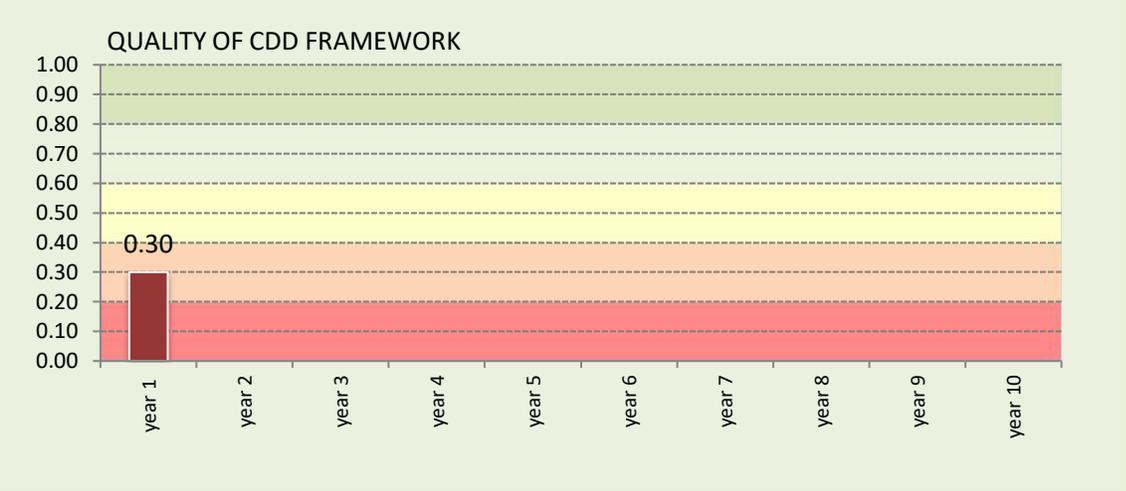
Charts 1 – 3 below summarize the overall sector vulnerability adversely impacting the quality of general controls and the products risk levels.

Figure 7: Banking Sector Vulnerability



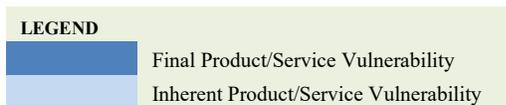
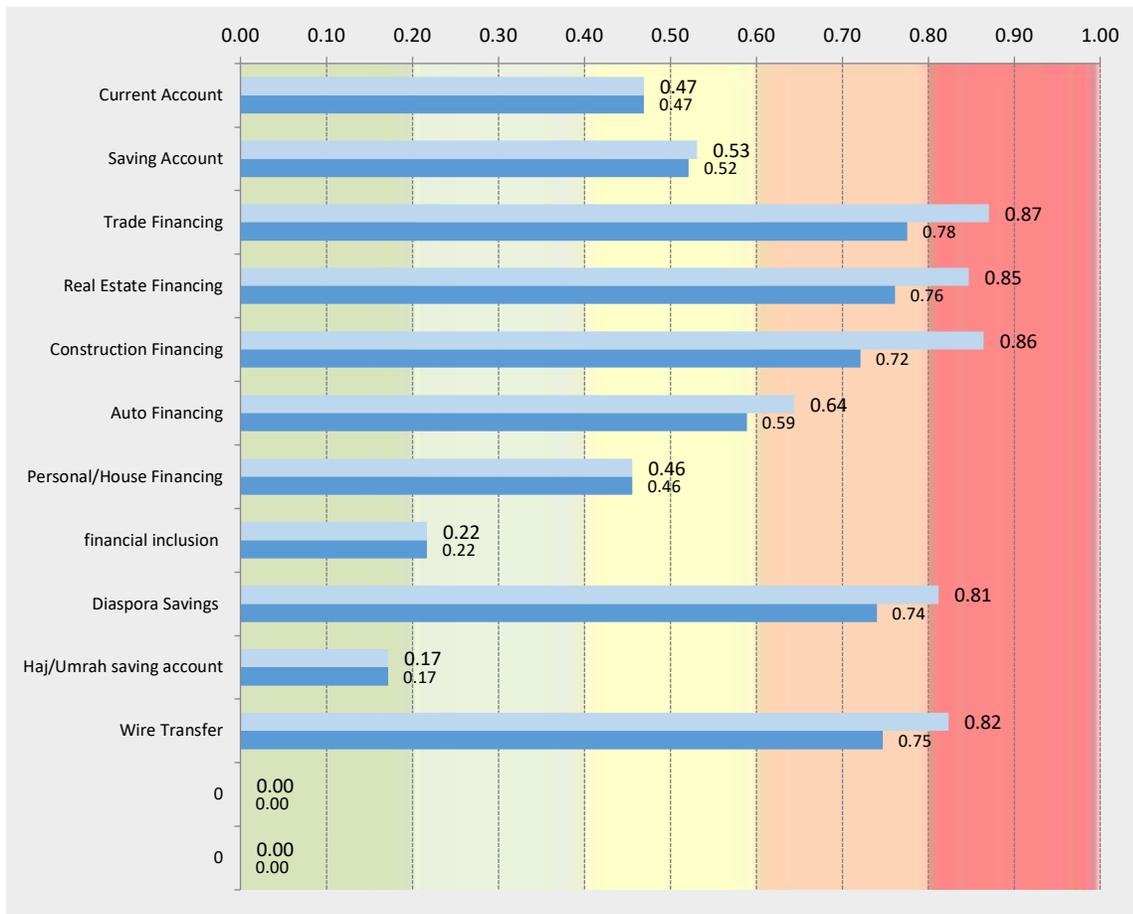
Note: Lower is better

Figure 8: Quality of CDD Framework



Note: High % value is low vulnerability

Figure 9: Vulnerability to ML on Products/Services



Note: High % value is more vulnerable to ML

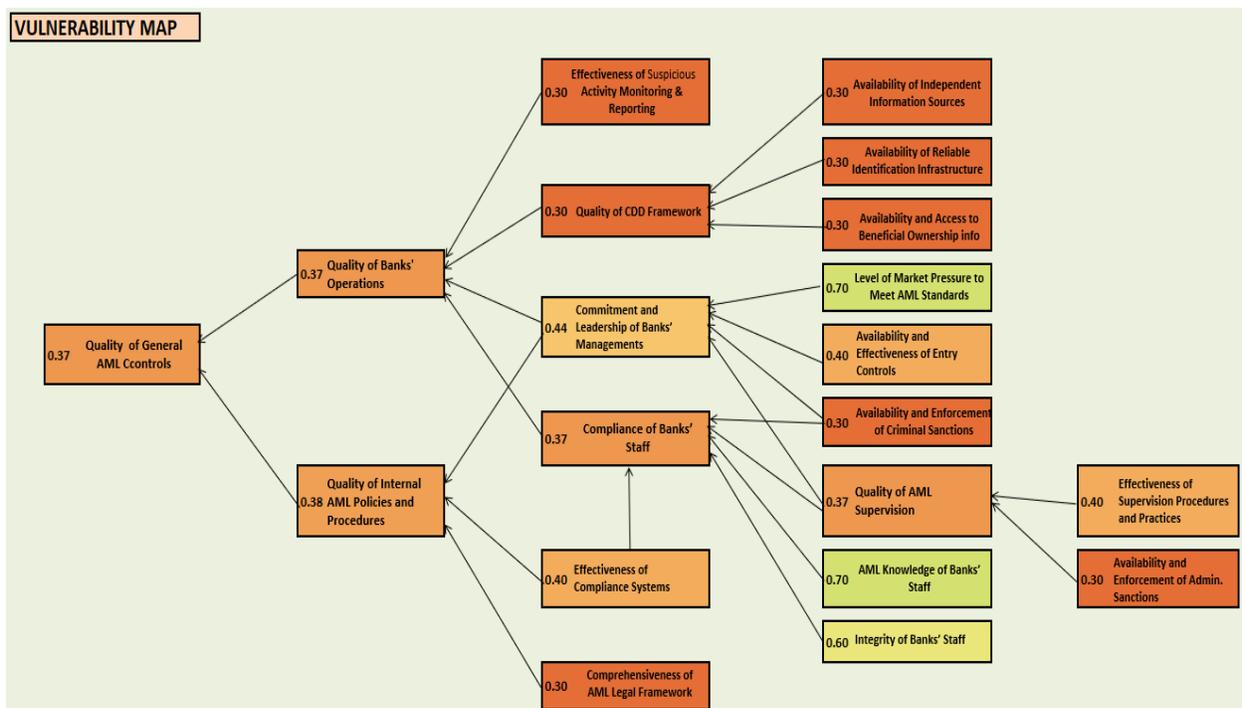
Table 5: Quality of AML General Controls

A. GENERAL INPUT VARIABLES	Rating
1. Comprehensiveness of AML Legal Framework	0.3
2. Availability and Enforcement of Criminal Sanctions	0.3
3. Availability and Enforcement of Administrative Sanctions	0.3
4. Availability and Effectiveness of Entry Controls	0.4
5. Effectiveness of Supervision Procedures and Practices	0.4

6. Integrity of Banks' Staff	0.6
7. AML Knowledge of Banks' Staff	0.7
8. Banks Effectiveness of Compliance Systems	0.4
9. Effectiveness of Suspicious Activity Monitoring and Reporting	0.3
10. Availability and Access to Beneficial Ownership Information	0.3
11. Availability of Reliable Identification Infrastructure	0.3

	Excellent	Close to Excellent	Very High	High	Medium High	Medium	Medium Low	Low	Very Low	Close to Nothing
	1.0	0.9	0.8	0.7	0.6	0.5	0.4	0.3	0.2	0.1

Chart 4: Figure 4: Banking sector Vulnerability Map



The justification for the above ratings is as follows:

Comprehensiveness of AML Legal Framework

Since the AML/CFT Act was signed into law in 2016, Somalia has strengthened the AML capacity of the financial services sector. To facilitate the country's AML/CFT policy and coordination, NAMLC has been formed as the competent authority to regulate and enforce the country's AML/CFT law and regulations, to align with the FAFT R.1, for Somalia to prevent country's financial institutions from illicit finance.

The FRC is the AML/CFT regulator and has the powers to enforce the law and relevant regulations. There has been lots of progress made with regard to developing AML/CFT policies. However, due to cross-cutting issues, mainly in the financial institutions, public and private sources of information are not available for banks to perform customer due diligences thoroughly, therefore, challenges remain in the area of customer due diligence. The banks' ability to conduct risk-based approaches, such as the verification of beneficiary ownership, collecting detailed information from persons, legal entities, and quality of legal arrangements are poorly formulated for banks to perform risk-based approach⁵⁷. Banks also have limitation to retaining a quality customer profiles, including ascertaining the identity and verification for PEPs. Customer background and credit checks are not available for banks when dealing with international trade accounts.

Additionally, the reliance of third-party checks and verification are not available. Moreover, systems in place for banks to comply with their reporting obligations and submit suspicious transactions are not effectively maintained. The concept of tipping-off information to customers is not clearly understood among banks' staff members. For them to follow AML/CFT Law 2016 art. 18. in some situations, the tipping-off policy obligation is not clarified in the banks' policies and procedures.

Recommended Actions.

- AML/CFT Law 2016 and other relevant regulations should be revised to bring them in line with FATF Recommendations and other International Standards and Convention.
- Country's identification infrastructure is key, which without it, the AML/CFT law and relevant regulations may not be implemented effectively.
- As prescribed in the AML/CFT Law art. 3, commercial banks and other reporting entities should comply with their CDD/EDD regulatory obligations, verify PEPs' business activities as prescribed by AML/CFT law.
- Political will is a key element to resolve for banks and other reporting entities to ascertain the identity of the PEPs.

⁵⁷ AML/CFT law art. 5

a) Availability and Enforcement of Criminal Sanctions⁵⁸

In general, Somalia's sanctions law is not enacted and is currently truncated in the Somali parliament. Alternatively, the enforcement of criminal sanctions is covered under AML/CFT Law 2016 Art. 21. The AML/CFT legislative measures against terrorists, terrorist groups, and other listed and sanctioned individuals are contained in this law.

The legislation imposes prohibitions, disclosures, and other compliance obligations. The legislation is applicable to Somali citizens, including those residing outside the country and the regulated financial institutions. Additionally, the Sanctions law addresses measures, designated persons, and prohibited activity with respect to assets of designated persons, that require the disclosure of information concerning the assets of law enforcement authorities. While there are no records or indications that a bank or person, legal or natural, in the banking sector has been prosecuted for violating AML obligations, the AML/CFT law requires that financial institutions adhere and implement AML internal control measures⁵⁹.

In the absence of the country's sanctions law, the current AML/CFT law 2016; Art. 22 can be used as a functional financial crime sanctions law. Even though, the Penalties for AML/CFT Non-Compliance Art. 22 falls short to the standard requirements. AML/CFT Law articles 27, 28, 29 in the law⁶⁰ stipulate in the literature as having range of effectiveness, the penalties imposed for civil and criminal charges are not up to the standard requirements such as proportionalities for imprisonment, and dissuasiveness of the criminal sanctions applicable to cases of non-compliance with AML laws and regulations, including sanctions for serious breaches that can be linked to ML offenses. Currently, the sanctions law is ineffective or overall incompatible with the international standards and practices⁶¹. The country needs a regulatory framework with a sufficient range of sanctions having enforceable powers.

Recommended actions.

- Enforcement and Criminal Sanctions law, currently pending in the Somali parliament should be a priority to be enacted and effectively implemented.
- Legal framework of the sanctions law in cases of noncompliance for banks should be enforced with actions taken against banks, individual members of the bank management or staff members, enforcement meaning administrative/civil or criminal actions should be initiated in case of non-compliance with AML requirements. A record of administrative, civil or criminal enforcement actions taken in the past by law enforcement authorities regarding non-compliance with AML requirements within the sector would be an indication to the effectiveness of the sanctions law.
- Based on the legislations, the criminal sanctions should be effective, proportionate, and dissuasive, in the way the banks management comply with sanctions laws and obligations.

⁵⁸ FATF R.6, Somalia, AML/CFT 2016, art. 21

⁵⁹ AML/CFT law 2016. Art. 9.

⁶⁰ sanctions and penalties, concerning the natural persons and Penalties applicable to legal entities and the management thereof, respectively

⁶¹ FATF R.35

b) Availability and Enforcement of Administrative sanctions.

Under natural person Art. 28 sec. 2 and the AML/CFT law 2016, the law gives the authority for regulators to enact powers for civil and/or administrative penalties appropriate to and in proportion to the seriousness of the violation⁶². Art. 29 is subject to legal natural persons and legal entities sec. 1; “Legal entities that violate any provisions of this law are subject to any penalties stipulated in Art. 28 sec.2. whereas; the legal entities, the monetary penalties shall be not less than \$25,000 USD or the equivalent in any currency and not be more than ten (10) times the amount of the money laundered⁶³”. Whilst the regulatory guidelines are available yet, enforcement and action taken in relation to those such violations are either weak or overlooked. For instance, regarding penalties against a person, the number of administrative actions that have been taken against banks, bank executives or staff members for non-compliance with AML obligations recorded or are unavailable.

Evidence of sanctions imposed in those cases such as written warnings, orders to comply with specific instructions, regular reports on the measures the institutions taken are not available. Additionally, barring individuals from employment within the banking sector, replacing or restricting the powers of managers, directors, and controlling owners, or suspension are not presented. There are no records showing restrictions or the withdrawal of banking operating licenses or criminal penalties imposed to offenders.

Recommended actions.

- Actions taken against violators must be proportionate, and dissuasive to ensure banking staff members and executive management will comply with the regulations.
- To make sanctions law more effective, the regulator must retain incident reports, including resolutions, enforcement and actions taken against bank, directors and other senior management.

c) Availability and Effectiveness of the Entry Controls.

The Central Bank of Somalia “CBS” is the authority that has the oversight and powers to regulate the banking sector. Currently, the Somali Commercial Banks are operating as licensed financial institutions where their business activities are regularly supervised.

Financial Institution Law 2012⁶⁴ defines the meaning of a commercial bank operating in Somalia and describes their consequent business activity parameters.

Regulation and supervision of financial institutions. “Countries should ensure that financial institutions are subject to adequate regulation and supervision and are effectively implementing the FATF Recommendations. Competent authorities or financial supervisors should take the necessary legal or regulatory measures to prevent criminals or their associates from holding or being the beneficial owner of a significant or controlling interest, or holding a management

⁶² AML/CFT Law, and regulations

⁶³ ibid

⁶⁴ fil 2012, Ch. I, Article 2

function in, a financial institution. Countries should not approve the establishment, or continued operation, of shell banks⁶⁵.

A person who intends to engage in banking businesses in Somalia must first obtain a license issued by the Central Bank⁶⁶.

Financial Institution Law 2012 prescribes the procedures and guidelines banking licenses is applied⁶⁷. The CBS also ascertains to collect more information from the shareholders, significant shareholders, directors, officers and/or third parties that the bank deems necessary to complete its assessment of a bank license application. However, the bank's ability to verify business ownership information is limited due to the country's lack of public and private independent sources of information; as prescribed by AML/CFT law art. 1 a, c, and d Bank Resolution on 31st December 2017 require the minimum capital licensed commercial banks to maintain, wherein a part of the same capital is deposited into the Central Bank of Somalia⁶⁸.

Commercial banks should always maintain a Capital Adequacy Ratio, which equals or exceeds twelve percent (12%) and a Core Capital Ratio which equals or exceeds eight percent (8%). A liquidity ratio which equals or exceeds twenty (20%) is also required. Commercial banks operating in Somalia should abide that that no person or group of related person's shareholders of licensed commercial banks direct or indirect owns or controls more 25%⁶⁹.

More information about CBS licensing and regulatory framework.

Despite the legislative and regulatory requirement available, the CBS has limitations to maintain effective entry controls in the financial service sectors. There are little or no legal restrictions for effective entry control laws that prevent financial services organizations to entering the financial markets. additionally, other government bodies, both local and federal levels are authorized to issue permits for businesses to operate, permits are not related to financial services companies. Issuing government bodies incentive is to generate revenues and some of them are unaware that financial service organizations require special license to operate⁷⁰.

Currently, the CBS is undergoing major reform and development, whilst in some situations the bank is not equipped to license institutions other than the Commercial Banks and Money Transfers Businesses. Whereas the other financial service companies have the option to register with CBS to commence operating temporarily. Consequently, operating without financial service authorization from the right regulator is common with other financial institutions.

Recommended Actions.

- The Ministry of Commerce and Industry and other permit issuing or regulating entities must ensure that financial services bodies must go through the right channels to obtain financial institution licenses prior to applying local or federal permits. Additionally, they should amend

65 FATF R.26

66 Fil 2012, Ch. II, Article 1

67 Fil 2012, Ch. III, Article 4

68 Fil 2012, Ch. III, Section 14 Article 1, 2

69 Fil 2012, Ch. 9 Section 67 Article 1,

70 Licensing procedures for FI are lately available on CBS website.

the relevant laws so that financial services applicants are prohibited from operating without a permission letter from industry regulators, mainly from the CBS and FRC.

- Publications and awareness relating to the process for licensing and procedures within the financial services sector should be available through the regulator websites.
- Applicants should satisfy conditionalities to operate as financial service organization before obtaining other local or national level permits.
- Strengthening the fit and proper regulations to shareholders, CEO, Board of Directors, staff members; “Know Your Employees”, proper vetting should be conducting for all key positions.
- To safeguard the integrity of the financial services industry, the regulators and government and agencies should find a common ground including arranging to sign MOUs, to creating preventive measures in averting unlicensed or unregistered entities with their respective regulator, and by operating unlawfully as financial service establishments.

d) Effectiveness of supervision procedures and practices

In view of the CBS ongoing reform program, the Financial Institution Law 2012, CHAPTER V, Article 34 the on-site examination of banks is proposed to align with the internationally accepted standards for bank supervision set out by the Basel Committee for Banking Supervision.

The Licensing and Supervision Department performs: 1) on-site examinations and off-site monitoring of banks; 2) develops and implements approved policies and strategies aimed at fostering a sound financial system; 3) reviews financial institutions licensing and re-licensing applications; 4) and liaises with financial industry associations. The Department’s responsibilities are expressed under the provision of Central Bank Act 2011 and Financial Institution Law 2012⁷¹. The Department has four Divisions, which are listed as follows: 1) Banking Supervision Division, 2) Non-Banking Supervision Division, 3) Licensing, Regulations & Compliance Division, and 4) Payment System & Payment Instruments Oversight Division⁷², additionally with its prudential supervisory oversight role.

The Bank’s Licensing and Supervision Department “LSD” carries out the AML/CFT on-site examinations with the financial institutions at least once a year⁷³. The off-site examinations are conducted on more regular intervals ensuring that the commercial banks observe their ML/TF regulatory obligations. Any related AML/CFT non-compliance weaknesses noted during the review process and deficiencies are reported to the Central Bank’s Board of Directors. Given the findings, the CBS Board takes corrective measures and, where necessary, penalties are imposed on banks. To make the bank’s supervisory activities more effective and comprehensive, there is no evidence to show that proportionate criminal or administrative penalties are imposed on the commercial banks.

71 FIL 2012

72 <https://centralbank.gov.so/supervision-and-licensing/>

73 FIL 2012, CH. V, Article 33

CBS staff members receive an ongoing capacity building programs from different international agencies, such as the World Bank and Financial Services Volunteering Corp⁷⁴ (FSVC). The training programs have focused on AML/CFT law and regulations. The Bank's staff members have gained experience in AML/CFT regulatory requirements, skills, and experiences.

Despite the experience and capacity development of the bank's staff, CBS is not legally responsible to regulate and enforce AML/CFT law and regulations; however, the CBS may apply the anchor regulation issued by the AML/CFT regulator⁷⁵; entitled "***AML/CFT Governance-Compliance regulation, revised in 2019***". Instead, the CBS has also developed AML/CFT regulations in 2019. The two AML/CFT competing regulations were both signed in 2019⁷⁶. In effect, the two regulations were published calling the reporting entities to comply with the AML/CFT regulations.

Nevertheless, by status and in accordance with the country's AML/CFT Law 2016 mandates the FRC, the country's FIU, as the authority designated to issue AML/CFT regulations for the reporting entities including the Financial Institutions⁷⁷.

The two regulations are the basis of misperception among the reporting entities, specifically in the financial services industry representatives have concerns about whose roles and responsibilities are to regulate them in complying with their AML/CFT regulatory obligation.

Moreover, FIs are raising questions regarding whether the FRC or The Central Bank of Somalia has the power to conduct AML/CFT on-site and off-site examinations and enforcing reporting entities' AML/CFT regulatory obligations.

Assessing risks and applying a risk-based approach; in accordance with standards and best practices, countries should require financial institutions to identify, assess and take effective action to mitigate their money laundering and terrorist financing risks⁷⁸.

AML/CFT policies and procedures developed by the commercial banks, their risk-based approach is inadequate in being effective in performing customer transactions monitoring, good recordkeeping, submitting quality STRs, resulting in insufficient testing outcomes. Additionally, the country's lack of proper identification with a comprehensive identification structure undermines the progress made by financial regulatory bodies.

In general, CBS and regulated commercial banks are both facing an incomprehensive legal and regulatory framework that are supportive to well-resourced and appropriate powers.

Recommended Actions.

74 (FSVC) Non-profit org. helps strengthen financial sectors in developing countries.

75 Financial Reporting Centre, AML/CFT law 2016 art. 21 sec. 9

76 CBS AML/CFT reg. 2019, and FRC AML/CFT regulatory framework.

77 AML/CFT law 2016. Art. 21: FRC Responsibilities, authority, and functions.

78 FATF R.1

- The NAMLC is the competent authority and the right policymakers. Therefore, they should make a policy decision to clarify the roles and responsibilities of the authorities through by-laws and ensuring who has the right to regulate and conduct off-site onsite examinations and for the reporting entities to comply with their AML/CFT law and regulatory obligations.
- A regulator should employ a risk-based approach for their on-site/off-site monitoring and inspection. Somalia’s Competent authority, namely NAMLC, should seek ways to strengthen and diversify their efforts to establish a comprehensive legal and regulatory framework supportive to a well-resourced appropriate power⁷⁹.
- Regulators should at minimum:
 - implement risk based onsite and offsite supervisory manuals
 - Undertake a risk assessment of all the entities under their supervision and rate all these entities based on their risk matrix

The Federal Government of Somalia and federal member states should collectively seek ways to resolve the country’s identification infrastructure problems. In this way, the reporting entities can implement their KYC requirements⁸⁰.

e) Integrity of Bank’s Staff

AML/CFT law 2016 Art. 22 gives directions to Banking institutions which states: 1) that the officers, employees, agents, or such other persons appointed to posts in the banks are required to keep confidential to information obtained within the scope of their duties. The directives are applicable even after the cessation of such duties, except as provided for in this Act.

2) Such information shall not be used for any purposes other than those provided for by this Act and shall only be disclosed or shared with appropriate authorities on a need-to-know basis for the purpose of detecting and preventing ML, TF and related predicate offences.

3) The banks shall adopt internal operating handbooks and procedures, including a Code of Ethics to ensure high standards of ethics, integrity, and professionalism. The banks are also obligated, in their operating handbooks and procedures, to address prohibition and mitigation of conflicts of interest and corruption. Apart from those general directives, financial institutions are vulnerable to abuse of non-confidentiality. There is no evidence with check and balance, how confidential information are handled.

Recommended Actions.

- The commercial banks should provide records and retain records demonstrating that they are following the AML/CFT law art. 22.

⁷⁹ FATF R.31

⁸⁰ FATF R.10 sec. iv, a,b,c,d

- Showing evidence such as periodic refresher trainings about the handling of the confidential information. The bank’s confidentiality policy should be in place all departments, directing employees to comply with the bank’s policy and operations manuals must be available.
- The fact that banks not retaining proper procedures and records showing the name of trainees and frequencies of trainings attended, as well as dates and signatures showing that employees understand the bank’s policy and procedures indicates that proper confidentiality policies are not being followed.

f) AML knowledge Bank’s Staff

The AML/CFT Law 2016 and relevant regulations were proposed for Somali commercial banks to adhere to the requirements as stipulated in the law⁸¹. Accordingly, the commercial banks have developed written AML/CFT policies and procedures. Banks should designate a compliance officer responsible to provide the bank’s staff members within information ongoing AML/CFT training programs.

In order to support the financial institutions, the Financial Reporting Centre “the FRC” and the Central Bank of Somalia “the CBS” have received number of AML/CFT capacity building from the World Bank, IMF and Financial Volunteering Corp⁸².

The two regulators have shared their AML/CFT knowledge with the financial institutions by conducting seminars and forums to improve the banks’ AML/CFT compliance knowledge levels. The commercial banks were offered programs designed for banks to understand their AML/CFT regulatory obligations such as complying with the AML laws and regulations and aligning with international AML/CFT standards. FRC and CBS transferring their AML/CFT knowledge to the financial services sector have positively impacted the industry.

Recommended Actions.

- The AML/CFT competent authorities need to step up effort to improve and strengthen their AML knowledge, more particularly law enforcement agencies dealing with financial crimes.
- The commercial banks should utilize their skills by designating certain financial products and services as high-risk such as real estate investment, international trade accounts, high risk customers such as PEPs and sanctioned persons. In the current environment, those types of financial products and services are most vulnerable to ML/TF.

g) Banks Effectiveness with Compliance System.

Based on the current AML/CFT law and relevant regulations, FRC, the country’s FIU has powers to supervise, monitor, and ensure commercial banks comply with requirements to combat ML/TF.

⁸¹ AML/CFT law art. 14

⁸² FSVC represents US Treasury

FRC has powers to impose sanctions in the event banks fail to comply with the regulations⁸³, which contain a range of disciplinary and financial sanctions, including the power to withdraw, restrict or give orders to relevant regulator to suspend the financial institution's license.

In this regulatory environment, the commercial banks have welcomed the country's AML/CFT law and regulations. The banking sector views the AML/CFT law with its supervisory power as an opportunity for them to re-connect to the global financial network. Consequently, banks strive to comply with their legal and regulatory obligations. The banks have also allocated resources for their compliance functions. They have developed AML policy and procedures and offer ongoing AML training programs to their staff members. Banks conduct periodic external AML audits to test the effectiveness of their AML/CFT policies and procedures. According to the information provided by the banks' executives, implementing and following AML/CFT compliance guidelines have assisted their institutions, and complying with the law and following regulations have also enhanced their staff members integrity levels.

Despite the efforts, there are other internal and internal forces that prevent Somali commercial banks from conducting effective compliance functions that are comprehensive, independent, risk-based, and well-resourced. The nature of the products offered linked with poor client base profiles, transactions patterns, cash volumes and the absence of strict cross-border transactions, are factors making the banking sector vulnerable to abuse. The banks' compliance officers are not often selected from a senior management level which is impacting their ability to operate independently.

Recommended Actions.

- To support the banking sector in achieving effective internal AML compliance functions, the banks should develop internal compliance programs that are proportionate to the country's AML risk levels, including banks retaining customer base profiles reflecting country's cross-border nature of transactions. Additionally, the country's policy makers should focus on the existing AML/CFT compliance gaps and develop strong policies and coordination.

h) Effectiveness of Suspicious Activities Monitoring and Reporting

Regulatory and supervisions available

To satisfy AML/CFT regulatory requirements, the banks are obligated to undertake customer due diligence measures⁸⁴. The banks should report to the Financial Reporting Center (the country's FIU) detailed information related to transactions of any amount suspected when the bank has reasonable grounds to suspect that the transaction, or attempted transaction(s) that may be related to ML or the proceeds of crime.

Upon request, the banks should make the customer identification information available to FRC such as: the transaction records, customer due diligence information and the overall customer

⁸³ AML/CFT law 2016 art. 27,28,29

⁸⁴ AML/CFT reg. art. 5 sections.1,2 and 3

profiles and any related correspondence between the bank and the customer in a timely manner⁸⁵. Banks should keep records obtained and maintained for at least 5 years. Despite all the legal obligations available for commercial banks; banks are poorly equipped with information systems enabling them to monitor customer transactions against their profiles. Banks lack the process which allows them to properly identify customers and verify their identity using reliable and independent sources of information.

Therefore, in the initial stages in the customer acceptance process, inadequate information is obtained from the customer, which does not help banks to effectively identify and report suspicious transactions. Moreover, due to the lack of detailed transaction records, the banks are unable to perform effective PEP screening.

Even though banks have relatively improved their AML compliance programs, other factors which are beyond their controls have hindered the progress made in complying with the AML/CFT regime. As a result, the banks' ineffective AML internal controls are grounds for the country's high level AML risk.

Furthermore, an electronic reporting system will better support the banks' suspicious transactions reporting since the current reporting filing system is manual⁸⁶.

Moreover, such conditions are also impacting the financial institutions abilities to properly identify STRs and limit their efficiencies to see the trends of the number and qualities of the STR submitted to the FRC.

The Banks should develop effective and appropriate systems for record keeping, monitoring, and STR reporting to support their AML policies and procedures. However, resolving any other limitations including those cross-cutting themes, which have been considered else in this NRA report and are beyond the control of the banks, should also be considered collectively through policy coordination with the country's competent authorities. These collective efforts are expected to pave the way for the banks to have good record-keeping systems which are pre-requisites for effective monitoring systems. Additionally, the country's AML/CFT policies and coordination are instrumental in making the suspicious transaction monitoring effective.

Recommended Actions.

- Banks should develop information systems that enable and facilitate the monitoring of the transactions of clients against their profiles.
- Banks transactional records should readily be available in a format that facilitates AML screening and monitoring.
- The established information systems should support banks in performing effective PEP screenings.

⁸⁵ AML/CFT reg. 13. Sections, 1, 2, and 3

⁸⁶ FRC plans to launch UN supported goAML system scheduled in the 3rd quarter of 2021

- Banks information systems should assist staff to effectively identify and record all complex, unusual transactions, and bank staff in effectively identifying and reporting suspicious transactions.

i) Availability and access to beneficial ownership information

The initial association of a company is the first step to collect and verify the company's beneficial ownership. A person who intends to establish a company must write an application to the office of the registrar of the Ministry of Commerce and Industry of the Federal Government of Somalia⁸⁷.

When the Registrar of Companies is satisfied that the requirements of this regulation and the company law regarding the application for the formation of company have been completed, the Registrar shall enter the details of that company in the General Register⁸⁸. The duty of the registrar is to issue a company certificate of incorporation with a unique serial number⁸⁹.

The Registrar of Companies issues two types of licenses to incorporate either a private company or public company to undertake business activity that is compliant with the Business Licensing Law, as specified in the license.

As per the requirement, the Documents to Register a Company⁹⁰ include: a) a complete application form issued by the Registrar of Companies; b) the company's articles of associations and the memorandum of association of the company; c) the company's memorandum of association must specify: i) the names of the shareholders, ii) the type of shares and the share quota; d) Copy of the passports of the founders and shareholders of the company; e) and any other information requested by the Registrar in accordance with this Regulation and the Companies Law.

Although the company law in process may satisfy the requirements necessary to collect information from legal persons during initial company registration, the financial institutions have minimum options to obtain and collect adequate information from legal persons and are vulnerable to abuse. Additionally, in the current environment, the banks are unable to take reasonable measures identifying the beneficial ownership information, perform ongoing monitoring on the business relationship⁹¹, assess beneficial ownership for legal persons⁹², and monitor high risk business relationships⁹³.

Recommended Actions.

87 Decrees art. 1 of the Ministry of Commerce and Industry (business registry) MoCI.

88 Regulation of company law art. 6

89 Regulations of the Company law art. 4

90 Regulation of company law art. 8

91 AML/CFT reg. art. 11

92 FATF R.24

93 FATF R.19

- Amend the relevant regulations with the Company registrar office to introduce provisions to comply with FATF⁹⁴ R.24, 25.
- Develop a mechanism for the collection of basic and beneficial ownership.
- Develop a mechanism for timely access of basic and BO information by LEAs and reporting entities.
- To enhance and improve the transparency relating to beneficial interests in corporations, trusts or similar entities.

j) Availability of Reliable Identification Infrastructure

Somalia lacks an identification infrastructure to support a secure national identification system with government-issued or local authority piece of identification. Moreover, there is no reliable public and private information systems to assist banks verify information provided by customers.

For transitional purposes, the AML/CFT regulator issued directives to the licensed financial institutions⁹⁵ on how to register and retain records from their clients.

While current registration and recordkeeping practices are based on temporary, procedural guidelines, the identification procedures available are not aligned with acceptable customer identification standards practices.

Consequently, current circumstances will prevent the banks from determining customer risk category, or whether to accept reject a new customer without independent and reliable sources of information. For instance, with an independent and reliable identification structure banks can access or verify clients’ past transactions patterns, customers’ commercial history, details of previous banking relationships, or present and former employers.

Additionally, the lack of collaboration between the public and private sectors are also factors preventing banks from accessing and establishing systematic independent information. For example, consumer profiles available in utility companies are useful verification items which can be used as a proof of customer payment patterns. Moreover, the information and records available in the banking sectors are not accessible to other banks, but each bank’s records are restricted for its own use. Independent sources of information and verification systems are challenges experienced across all the reporting entities.

Overall, the country lacks a foundational KYC system, which goes beyond the control of the reporting entities. The regulatory authorities and policy makers must step in and ensure that consumers have proper personal identification that is linked with public and private independent sources of information to assist the banks in developing quality customer profiles.

Recommended actions.

94 FATF. E. transparency and beneficial ownership of legal persons and arrangements
95 regulations for FI and MTBs customer registration, 2016, CBS/nbs/reg/04 articles 1-9

- The country’s KYC system is an essential element in supporting consumers to have access to financial services, which also supports consumers in accessing other social and government services. Therefore, the Federal Government of Somalia, the Federal Member States, and local governments should undertake steps to establish a comprehensive identification infrastructure for Somalia.

1.

2.

2.1.

2.1.1. Banking Products

2.1.2. Investment accounts

The list of products evaluate by the working group were active products. The risk for each product was based on the total size/value of the product, average transaction size, client base profile, existence of investment/deposit feature, level of cash deposits, and frequency of withdrawals, and the international transactions involved.

The group defined that the vulnerability of a product is correlated to the need for additional AML control specific to that product. The working group has also assessed whether the existing controls are commensurate to the products risk level, as well as the capacity of each bank to combat the identified risks.

A high rating⁹⁶ indicates that the AML vulnerability is lower while low rating means the product might be subject to ML abuse.

In Somalia, most commercial banks have existed for little over four years and the owners of the banks are not generally experienced bankers. The capital allocated for development and human resources are not attractive to qualified bankers, financiers, and qualified accountants. The security situation in Somalia, weak government institutions, and the absence of effective and enforceable contract laws, have forced the banks to invest in the least productive sectors of the economy. Majorly, banks loan portfolios are concentrated in the fixed asset sectors⁹⁷.

The out of 12 investment vehicles listed in the banks consolidated financial statement in 2018-2019, trade finance and real estate loans make up over 52% of banks loan portfolios. This is followed by 12% construction and personal household loans. Manufacturing and agriculture loans both contribute only 1% in the loan portfolio⁹⁸.

⁹⁶ Rating: (high, medium-high, medium, medium-low and low,)

⁹⁷ Commercial Banks of Somalia

⁹⁸ Central Bank of Somalia

Despite the banks being risk averse, the real estate and trade finance sectors are vulnerable to ML/TF specially the current environment that the banks are operating. For example, banks are not able to conduct robust background checks from the beneficial ownership of their clients. The following sections detail the vulnerability and the product risk rating will be justified.

2.1.3. Saving and demand deposit accounts

Diaspora Deposit account

The Diaspora Deposit account is a popular vehicle offered by most banks. It is a demand deposit account where the average transaction size is high compared to other deposit accounts. Customers attracted to this product are have high incomes or frequently travel to and from high-net-worth countries.

Despite a foreign passport being an acceptable identification for banks to ascertain a customer, banks have limited ability to conduct customer due diligence as per requirement from these types of accounts. Somalia banks do not have foreign agents or affiliates who may verify the authenticity of the foreign passports linked with the country's lack of independent source of information. Additionally, foreign passport holders are sometimes federal or federal member states executives, sometimes even politically exposed persons "PEPs". In these type relationships, banks are required to conduct enhanced due diligence "EDD"⁹⁹. When banks receive incomplete information from a customer, the transactions activity should be flagged as high risk and the activity should be monitored as red flag accordingly.

Additionally, the need for the new commercial banks to earn profits or the desire not to reject a lucrative business opportunity are incentives for banks to neglect the account monitoring guidelines, which create loopholes that the product is subject to abuse.

Recommended Actions.

- Based on the transaction sizes and the country's cash-based economy, the Diaspora deposit accounts are high risk, and as such, banks must treat them as high-risk accounts and banks should conduct EDD.

Current accounts

Current account is a demand deposit and operates as a chequing account. Customers normally established these types of accounts as their daily expense accounts. the average transaction sizes are low, while the monthly turnover exceeds 8 million USD among banks surveyed¹⁰⁰. Normally, customers transact small cash withdrawals. Domestic banking interoperability or electronic wire payments are unavailable and use of cheques is also rare.

In some instances, holders of these accounts run small, unregistered businesses (street business such as selling variety goods or small-scale business). In these situations, customers often do not disclose their reason for opening the account at account opening stage, and deposit cash proceeds from their

⁹⁹ AML/CFT reg. 10, FATF R.5, 6

¹⁰⁰ CBS Banking sector consolidated financial statement Dec. 2019.

businesses into personal bank accounts. There is a potential that these types of businesses are engaged in tax evasion which exposes the banks to high-risk customers.

Although banks require more information when transaction sizes are high, banks consider current accounts as a low-risk accounts. Consequently, controls aimed to mitigate risk against current account are also low.

Recommended Actions.

- Banks are failing to comply with their AML/CFT regulatory obligations. In the account opening stage, banks should determine and verify the intended nature and purpose of the account, more particularly whether the account is used for personal or business. Banks should also monitor account activities to ensure account transaction are inline with proposed account activities.

Saving accounts

Saving account are lower volume accounts where average transaction sizes are limited in value. Banks consider saving accounts as low-risk accounts. The consolidated value of saving accounts in 2017-2019 was \$712,405,926.25 USD, but some banks have not provided average their customer transaction sizes but the data available for saving accounts average transaction value is over \$1,000.00 USD, which is considered high, requiring banks to perform a customer due diligence.

Recommended Actions.

- To maintain consistency, the commercial banks should follow AML regulations lined with their internal control guidelines.

2.1.4. Trade finance (corporate Credits)

Trade finance products have relatively high volume, and the size of average transactions are also high. Trade financing represents 34% of bankers' investment products. Customers have a good collateral, mainly fixed assets, it offers less credit risk exposure, and its profitable business for banks.

Although AML internal controls exist, some of the risk factors are beyond the control of the banks, and thus, this type of business relationship opens a window for bankers neglect their AML compliance obligations.

The main vulnerability feature associated with trade finance products is the lack of information available for gathering from customers. Moreover, trade finance accounts are vulnerable to abuse because of the amount of cash activities involved and banks inability to perform robust CDD/EDD.

2.1.5. Real Estate Financing

Under this product, both the volume and average transaction size are high, and are cash-based transactions. Real estate finance represents 18% of the banks' investment portfolio¹⁰¹. There are mixed

101 CBS. Somalia Commercial Banks consolidated Financial Statement 2019

client profiles, including non-residents, high net worth individuals, where banks have no mechanisms to verify whether the customer is a PEP or perform a risk-based assessment to consider customer risk level.

The vulnerable features include the lack of verification of source of funds, the absence of land registration records, and the lack of credit bureaus available for banks to determine customer credit history.

The control system banks use is customer putting down collateral, thus protecting the banks from credit risk.

2.1.6. Construction Financing

Construction financing is nearly identical to, or has same AML risk exposure as real estate financing products. The volume and average transaction sizes are high and are all cash-based transactions¹⁰². Construction finance represents 12% of the banks' investment products portfolio¹⁰³. There are mixed client profiles including, non-residents and high net worth individuals. Construction financing is comprised of medium/short term loans, of which, the maximum is a 36-month term payment.

Regardless of amounts involved, longer term real estate financing is not available. Consumers should make payment within the prescribed term of payment.

The product's main vulnerable features include inadequate verification of source of funds, lack of land registration records, credit worthiness of customers beyond their capability of putting down collateral. The focus is the banks to protecting themselves from credit exposure, in relation to construction finance and other real estate accounts.

2.2. Auto Finance

A second-hand automobile is mainly available in the market. Used cars are imported from the Gulf countries mainly from the UAE. Used car finance makes up 9% of the banks' investment products portfolio, where the values and volumes of used cars sold are relatively medium.

Transactions are cash based and are subject to ML activities. The industry is not following AML/CFT law¹⁰⁴, and required regulations are not being implemented¹⁰⁵.

At the moment, the used car dealers and other Designated Non-Financial Businesses and Professionals (DNFBPs) are subject to ML vulnerability.

Car dealers are reporting entities and will dealt with DNFBPs in the sections below.

2.2.1. Personal Household Financing

Unlike other investment products, personal household is a big-ticket consumer item finance. Personal household financing represents 15% of the banks' loan portfolio. In this situation, banks require a third party, guaranteeing person and most banks require two guarantors, where the guaranteeing person is responsible for the loan payment in the event the borrower defaults the loan payment.

¹⁰² The bankers lack of interoperability system, most transactions are cash based.

¹⁰³ Commercial Banks Consolidated 2019 financial statements.

¹⁰⁴ 104 FATF R. 22, R. 23, AML/CFT law 2016, art. 4 Institutions and professionals subject to this Act.

¹⁰⁵ interpretive note to recommendation 22 (DNFBPs – customer due diligence)

Nevertheless, a credit bureau does not exist to determine customer credit worthiness and the country's poor application of contract laws and ineffective law enforcement agencies expose the banks to credit risk. In view of those risk factors, the NRA report is concerned whether the product is vulnerable to ML. The environment the banks are operating in is cash intense, the product vulnerability is high.

Recommended Actions.

- When dealing with these types of proposed loans, commercial banks should conduct CDD/ECDD, depending on customer profile and information retained mitigates ML risks of the relationship.

2.2.2. International Wire Transfers

International wire transfer service is offered by a few commercial banks, but not all banks have the access to conduct international wire transfers¹⁰⁶ or have direct, international corresponding relationships. The absence of the National Payment System for domestic wire transfers makes each bank operate in isolation.

The Money Transfer businesses “MTBs” licensed as non-bank financial services¹⁰⁷ are filling the gap to support Somalia's businesses. The Somalia MTBs have established a global network for clearing and settlement system through agent relationships. Therefore, all businesses for international payments are normally cleared through Money Transfer Businesses (MVTB)¹⁰⁸.

Since sizeable transaction amounts for incoming and outgoing funds are involved¹⁰⁹, the banks should conduct EDD and credit checks for international wire transfers, especially foreign trade related businesses. The required information is not available for Somali banks. Consequently, there is an opportunity for the international wire transfers to be used for illicit purposes.

Recommended actions.

- The banking sector must conform with AML/CFT law and with the TAFT standards the following
- improve and strengthened CDD/ECDD to properly perform RBA.
- Improve process of verifying beneficial ownership legal entities/legal arrangements and gain access for information about PEPs.
- Commercial banks should enhance internal control guidelines for wire transfers.
- Improve the quality and frequency of the suspicious transaction reporting.
- properly utilize the country's sanctions powers available through AML/CFT criminalization laws.
- Banks' senior management must be assigned to compliance positions, whose powers and decision making are fully supported by the bank's executive board members.

106 FAFT SR. 12 Section 6. A, b, c, d, e, Cross-border Qualifying Wire Transfers,

107 FATF, SRVII 14 (MVTB)

108 Informal financial services sector

109 <https://www.fatf-gafi.org/media/fatf/documents/recommendations/pdfs/fatf%20recommendations%202012.pdf>
SRVII. Additional measures for specific customers and activities

- Improve banks account monitoring capacity by installing accounts monitoring systems. Improve the identification of unusual transactions, whereas STR and LCTR reporting activities correspond or are comparable to financial sectors transaction activities.
- Banks in the private sector should take the initiative to combine their efforts, and press government institutions and regulatory agencies including LEAs and judicial systems to collaborate and enforce all AML/CFT legal requirements.
- For banks to boost the AML compliance system effectiveness, banks should develop adequate internal policies, adopt procedures to attain corporate wide AML compliance systems pertinent to their risk levels. They should conduct periodic audits to test the effectiveness of the AML compliance implementations. To improve STR and CTR reporting levels to become comparable to the current cash transaction volumes, banks should fully comply with their reporting requirements.

Ranking of Priority Areas

From the assessment, priority areas have been identified as follows:

Table 8: Priority Rankings

PRIORITY RANKING - LAST CASE/SCENARIO	PRIORITY RANKING**
Comprehensiveness of AML Legal Framework	1
Availability and Enforcement of Criminal Sanctions	3
Level of Market Pressure to Meet AML Standards	
Availability and Effectiveness of Entry Controls	4
Effectiveness of Supervision Procedures and Practices	1
Availability and Enforcement of Administrative Sanctions	2
Integrity of Banks' Staff	6
AML Knowledge of Banks' Staff	
Effectiveness of Compliance Systems	4
Effectiveness of Suspicious Activity Monitoring and Reporting	2
Availability and Access to Beneficial Ownership Information	3
Availability of Reliable Identification Infrastructure	4
Availability of Independent Information Sources	5

The smaller the number the higher the priority.

3.3. INSURANCE SECTOR

The insurance sector is categorized into General Insurance or Takaful. There are currently four general insurance companies that are registered with the regulator but are not licensed to operate as financial institutions. The information gathered below is based on interviews conducted with insurance operators and information received from the regulator, no other data is available.

According to operators, insurance transactions are conducted internationally, covering life, injuries, and insurance for cargo in transit from country of origin to country of destination. According to the information received from the managers, the insurance business activities are minimal.

Insurance contracts handled are guarantees covered by third party insurance companies outside Somalia.

As the country has no active international clearance houses, all claims, payments obligations, premium, refunds are arranged and conducted outside of Somalia¹¹⁰. While current insurance activities are relatively low, the insurance sector is operating outside the formal financial sector and the products offered are high-risk. Similar to some of the other financial services, insurance establishments have unrestricted entry controls, often start operations without securing licenses. At the time of writing this report, the regulator informed us that the insurance company law and regulation are underway.

3.4. OTHER FINANCIAL INSTITUTIONS VULNERABILITY

3.

4.

3.5. Overall Findings

The vulnerability of the other financial institution sector is also dependent on the strength of AML general controls and product specific variables. The overall sector vulnerability to ML risk is rated **Medium High**. All other input variables are rated low, medium, or medium-high performance. Some products/services offered in the other financial institutions sector seem to be high performers as result of their stage of development, without regulatory oversight the services might be vulnerable to ML abuse.

Except for the Money Transfer Businesses, which are formally licensed with the Central Banks of Somalia, other financial institutions are vulnerable to abuse because their regulatory guidelines are not established. The microfinance companies include a number of financial cooperatives financed by outside donors that are operating without regulatory oversight.

Charts 1 – 3 and figure 1, including table 1, below summarize the overall sector vulnerability adversely impacting the quality of general controls and the products risk levels.

Chart 1: Overall vulnerability

¹¹⁰ Interview Takaful/insurance company, CEO Mohamed Elmi

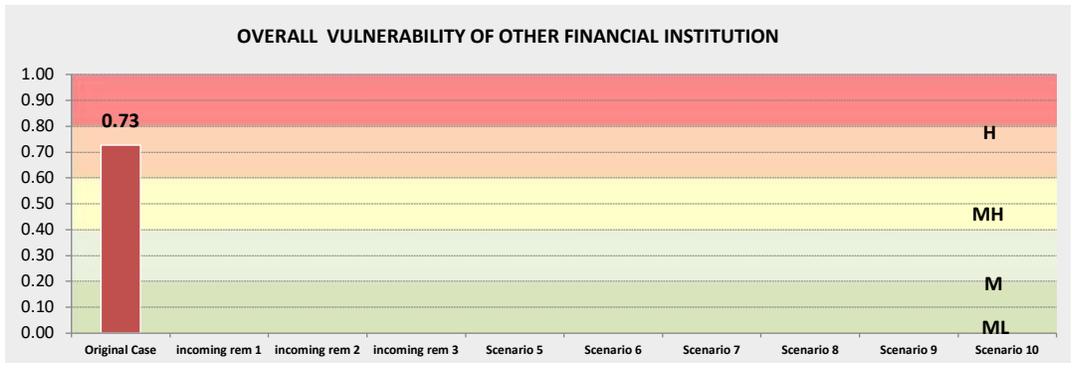


Chart 2: Quality of Customer Due Diligence framework

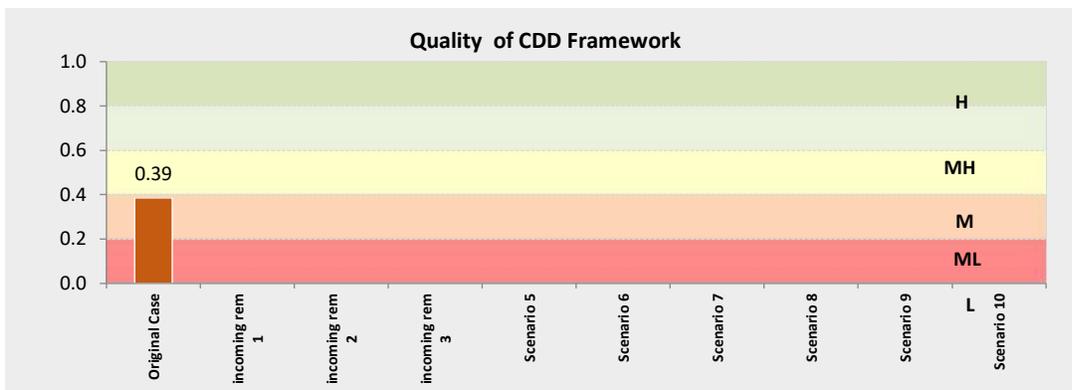


Figure 1: Other Financial Institutions Vulnerability Map

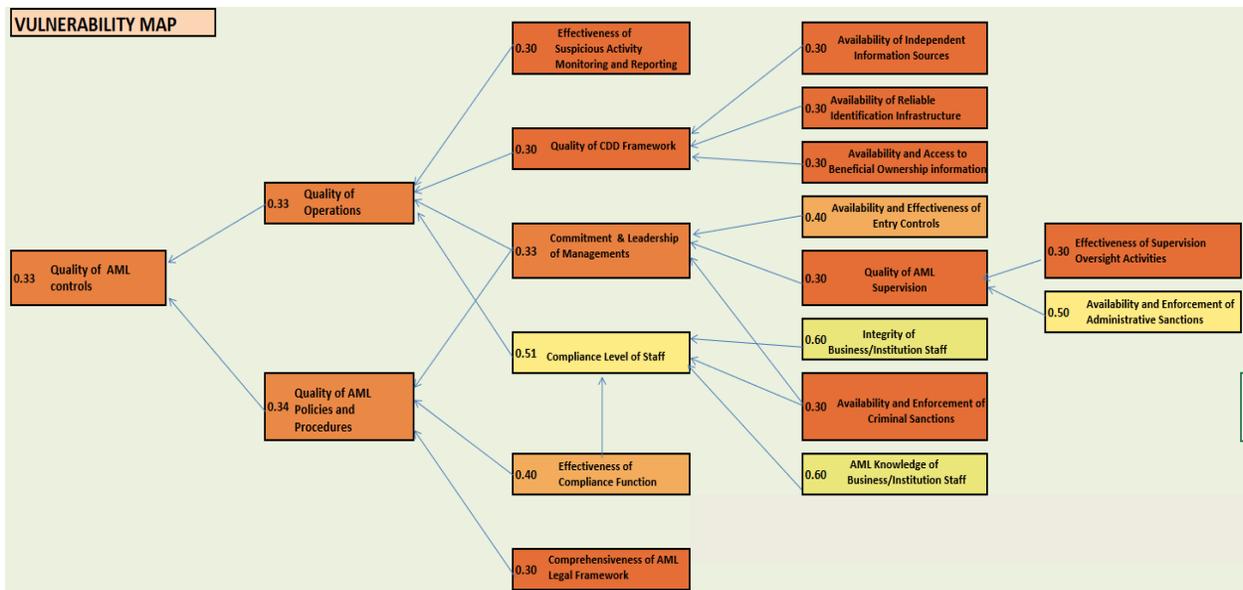


Table 1: Priority ranking AML controls

PRIORITY RANKING - LAST CASE/SCENARIO	PRIORITY RANKING**
Comprehensiveness of AML Legal Framework	1
Effectiveness of Supervision/Oversight Activities	3
Availability and Enforcement of Administrative Sanctions	4
Availability and Enforcement of Criminal Sanctions	2
Availability and Effectiveness of Entry Controls	4
Integrity of Business/Institution Staff	
AML Knowledge of Business/Institution Staff	
Effectiveness of Compliance Function (Organization)	4
Effectiveness of Suspicious Activity Monitoring and Reporting	4
Availability and Access to Beneficial Ownership information	4
Availability of Reliable Identification Infrastructure	4
Availability of Independent Information Sources	4

The key player in the Other Financial Institutions is the Money Transfer Businesses “MTB”. They are licensed to operate as financial services businesses and their activities are periodically reviewed by the regulators. MTBs comply with their reporting requirement. They report STR/LCT to the FRC (the country’s FIU).

There are 11 licensed remittance companies operating in Somalia. Remittances in Somalia are estimated to amount to \$1.4 billion USD and support 23% of the GDP¹¹¹. In the absence of corresponding banking services, remittance companies are the main mechanism to transfer money in and out of Somalia. Therefore, MTBs existence with their business activities remaining as key components for most international transactions and financial settlements. The other active financial services organizations include small time foreign exchange persons and entities, and a number of microfinance companies. They are all operating without regulatory oversight.

While their business activities, number and sizes are unavailable, the working group representing the remittance sector have raised concerns about the existences of financial services companies operating without obtaining licenses from CBS and without being registered with the country’s FIU. As there are no effective LEAs that may prevent them from operating as financial service companies, they establish their businesses by obtaining local government permits only. Thus, those types of financial services establishment might be vulnerable to ML abuse.

¹¹¹ Remittances and Economic Development in Somalia, world bank.
<http://documents1.worldbank.org/curated/en/129711468167064074/pdf/379150SO0Remittances0WP3801PUBLIC1.pdf>

The WG involved in the discussion were from financial services companies, CBS, FRC staff members, and representatives from the Somalia Remittance Association and Somalia Banker Association. These groups were more informed in the AML/CFT subject matter compared to other WGs. In their discussions, they have presented real life cases and offered material evidence to back up their debates.

3.6. Money Transfer Businesses “MTBs”

The MTBs are regulated by the Central Bank of Somalia. Their licenses are renewed annually, wherein licensing renewals are strictly contingent to the merits of their AML/CFT compliance performance. According to Financial Institution Law 2012, Chapter 1, Article 2 “Money transfer business” or “Hawala” means the acceptance of cash, cheques and other payment instruments, [also including stored-value products], in one location, and payment [disbursement] of a corresponding sum in cash or other form to a beneficiary in another location.

According to Financial Institution Law 2012, CHAPTER 7, Article 50: “A person shall not carry on or engage in money transfer business without a valid license issued by the Central Bank for that purpose.”

According to Financial Institution Law 2012, CHAPTER 7, Article 50: “every relevant person shall apply to the central bank for registration using prescribed form by the Central Bank of Somalia. Upon receipt of an application for registration the licensing and supervision department shall, within fourteen days, review the application and make recommendations, on the application, to a committee of the central bank after ascertaining the formal content and completeness of information and document requirements under Regulation”¹¹².

According to the available guidelines, MTBs identify their customers, retain transaction records and like commercial banks, MTBs submit STRs and LCTRs to the Financial Report Centre (Somalia’s FIU). When customers are receiving funds, they are required to either provide official photo identification or to provide references from a third party. Moreover, photo identification is used as part of the initial customer registration process; however, there is no electronic biometric screening available for the MTBs¹¹³. Beginning in 2015, remittances companies have received capacity building training from several multinational agencies including: the World Bank, US State Department through the US Treasury; represented by Financial Services Volunteering Corp., “FSVC”.

Remittance is a main contributor to family income and investment, with subsequent effects on poverty and inequality. Especially in times of economic depressions and external shocks, remittances have been extremely important to the Somali economy because they tend to smooth consumption and thus create a “buffer” against shocks. Remittance inflows have risen during times of drought¹¹⁴.

112 FIL 2012

113 Remittances and Vulnerability in Somalia Assessing sources, uses and delivery mechanisms Rift Valley Institute Nisar Majid, with Khalif Abdirahman and Shamsa Hassan. November 2017

114 Remittances and Economic Development in Somalia, Paper No. 38 / November 2006, by Samuel Munzele Maimbo

Most Somali remittances, which range between \$50-100 USD, are used for direct consumption by the household, particularly for education and health. Consumption accounts for at least half of remittance spending, most likely up to two-thirds. Similar to the Somali commercial banks, the MTBs have challenges in effectively combating against ML/TF.

Due to the country's lack of a National Identification System, the MTBs are unable to conduct proper Know Your Customer (KYC) procedures. Therefore, the incoming and outgoing remittances are vulnerable to ML/TF.

The country's other financial institutions are facing similar challenges as the Somali commercial banks. The AML legal framework is incomprehensive; therefore, remittance companies lack the ability to conduct customer due diligence and use a customer risk-based approach to the necessary extent. Their recordkeeping standards are weak; thus, they are unable to fully verify who are PEPs.

Additionally, the existing administrative and criminal sanctions are not enforceable until the LEAs and the country's judicial system have the capacity and the resources to effectively combat ML/TF risk. Moreover, the absence of effective AML/CFT policy implementation and coordination amongst the policy makers means the financial institutions sector regulators will have a hard time implementing the supervisory powers available.

Recommended Actions.

- The lack of a proper Identification infrastructure is a serious challenge for remittances. Therefore, to gain reliable KYC processes and ensure that MTBs properly comply with country's AML/CFT Law 2016, FGS and FMSs should prioritize the country's identification infrastructure.
- To prevent and protect the country's financial Institutions from ML/TF, the FGS needs to strengthen the country's AML/CFT policy and coordination.
- Strengthen regulatory guidelines concerning funds transfer between Somalia and two major distributions centers, namely the UAE and Kenya, to prevent ML activities, especially cash trade finance.
- The lack of coordination between stakeholders, ineffective implementation of their obligations and/or laws and regulations to achieve a comprehensive regulatory framework are all major challenges to remittances services.

3.7. Mobile Banking: E-Money

Mobile Money Transfer "MMT" has become an essential and widespread part of Somalia's economic ecosystem. Almost three-quarters (73 percent) of the population aged 16 and older use mobile money.

Therefore, the MMT is the main transaction instrument used by both individuals and businesses in Somalia. The e-money services are also offered to government bodies and non-governmental agencies.

About 36% of the country's GDP flows through mobile money systems. Mobile money balances are arguably the main monetary asset in Somalia. The value of Mobile Money Transactions in Somalia is estimated at \$2.7 billion a month. Consequently, in today's Somalia, mobile money is the main channel for accessing financial services. The demand for digital money has arisen largely from a lack of faith in the Somali shilling, having the option of using U.S. dollars for low-value transactions, and the low transaction costs and ease of use of Mobile Money Services¹¹⁵. The Mobile Money Transfers users have the options of exchanging the e-money value, which is in US Dollars, to the equivalent cash value in Somali Shillings. Normally, the funds are used for payment of goods and services.

The value for personal transaction is capped at \$300.00, but the daily transaction volume the MNOs handle are huge. Business customer transaction values are much larger than personal transaction values; thus, the business transactions are vulnerable to abuse. While mobile money presents a major opportunity to help increase access to finance, spur inclusive growth, and promote the resilience of communities, a high level of dependence on mobile money increases vulnerabilities in the absence of appropriate regulation¹¹⁶. Therefore, regulatory guidelines for MMT are an important aspect for the industry to operate legally and comply with existing AML/CFT laws and regulations.

For a long time, the mobile network operators in Somalia, "MNOs", were operating without financial regulation oversight, except through the Ministry of Communications and Technology, which has issued licenses for them to operate as telecom business operators¹¹⁷. In December 2020¹¹⁸, the CBS issued licenses to one of the largest mobile money operators, wherein other operators are also expected to follow suit. Accordingly, the CBS has now oversight powers to regulate mobile money transfer companies. The following guidelines are in place to regulate mobile money:

- Mobile Money regulation, Part I, Article 3 "mobile money service" means a payment service delivered in electronic form by a mobile money service provider must be in accordance with the mobile money regulation. Mobile Money regulation, Part II, Articles 6 (1) states every relevant person shall apply to the central bank for license using the First Schedule of the Mobile Money regulation,
- Mobile Money Regulation, Chapter 2 Articles 7 (1 and 4), the Central Bank shall consider a renewal application within ninety days and may renew or decline to renew a license for reasons stated. In addition to that, a license granted under the Mobile Money regulation shall be valid for

¹¹⁵ Rapid Growth in Mobile Money: Stability or Vulnerability? Somalia Economic Update, August 2018

¹¹⁶ Rapid Growth in Mobile Money: Stability or Vulnerability? Somalia Economic Update, August 2018

¹¹⁷ <https://mppt.gov.so/en/oversight/>

¹¹⁸ In December 2020, 3 MNOs expected to register with CBS and NCA licenses to be granted. Implementation for regulatory guidelines including STR reporting, setting AML/CFT guidelines as part of their obligations

two years and may be renewable biennially, provided that a license granted during a calendar year shall be valid up to 31st December of the end of the second year.

Despite the MNOs representing the largest portion of the country's financial activities, MMT are not in compliance with the AML/CFT law 2016 and its relevant regulations.

Recommended Actions.

- MNOs should comply with AML/CFT laws and regulations and meet their reporting obligations.
- MNOs should put adequate measures in place to control the amount of money transferred from business to business. They should also have improved sim-card registration practices and retain business ownership information as prescribed by the FRC AML/CFT regulations.
- CBS and FRC should strengthen their regulatory powers and develop effective mechanisms to monitor MNO activities.
- FRC should engage MNOs and provide ongoing AML/CFT training programs to ensure that MNOs are registered with the FRC and comply with their reporting obligations.
- Stakeholders from government bodies, agencies, and regulators together with MNOs should work together to protect the country's mobile money payment systems from ML/TF abuse.

3.8. Foreign Exchange Dealers

The collapse of the Somali government in 1991 saw the rise of unique, economic, and social outfits. One of them was the emergence of a nonconforming monetary system, controlled by warlords and rogue businessmen, who contracted foreign printers and imported counterfeit money. This left the Somalia economy in shambles, largely dependent on dollars for trade, and effectively created a freewheeling economy without a state¹¹⁹.

The Somali exchange market is not based on diverse foreign exchange markets. Most active currency exchange is fake Somali shillings against the US dollars. As a result, the only currency note available in Somalia is the 1,000 shilling, with 98% of circulating shillings considered fake by the IMF¹²⁰.

The mobile network operators are the major hub for the US Dollar E-wallet. Small exchange houses accept MMT USD e-wallet to exchange into Somali Shillings. The exchange between the USD currency to Somali Shillings is the most active foreign exchange in the retail market. It is an efficient market where inflation based on currency fluctuations is not a main concern.

The commercial banks and MTBs are not involved in these exchange activities, banks only accept USD cash or mobile money transfers. Normally, the amounts consumers exchanged using for their

¹¹⁹ QUARTZAFRICA- February 2017. Abdilatif Dahir

¹²⁰ Global Findex database 2017

daily expenses are between \$1 to \$5. The users in this exchange market are the poor population, representing the majority of the Somali people. Notwithstanding the smaller amounts exchanged, the daily transaction volumes of the market are high.

The old Somali shilling is the most trusted, but because of wear and tear, the currency is diminishing in quantity. Consumers outright rejected the new, counterfeit currency when it was introduced into the market therefore, the fake currency has become limited in supply. As part of Somalia's debt relief program, an agreement was initiated in 2018 between the Federal Government of Somalia and federal members state to not print new, counterfeit currency, discouraging some federal member states from printing additional fake Somali shillings.

According to CBS guidelines, foreign exchange businesses have the option to register with CBS while regulation pertinent to foreign exchange operators are being developed. Currently, the exchange houses are operating without registration or securing a permit from the local government.

The absence of formal recordkeeping, the fake currency circulating in the market offers an opportunity for the proceeds of criminal activities to be laundered in the local economies and perhaps even being funneled into foreign bank accounts. The exchange house's failure to verify the sources of cash, the ineffective AML/CFT regulatory enforcement, and the lack of entry controls make the foreign exchange houses vulnerable to ML abuses and not compliant with country's law and relevant regulations¹²¹. The overall vulnerability rating is **High**.

3.9. Microfinance

Microfinance can be defined as attempts to provide financial services to households and micro-enterprises that are excluded from traditional commercial banking services. The Gargaara Company Ltd and Kaah KIMS are two microfinance organizations currently registered with the Central Bank. The two companies are not licensed with the regulator as the due process is yet to be commenced.

Microfinance in Somalia including several financial services organizations are operating as informal financial services. Microfinance is not included in the existing legal framework to monitor the sector activities. It is essential for policymakers to pave the way for emerging microfinance institutions to develop an environment to formally operate and mobilize product offerings.

There is only one Microfinance institution registered with the CBS. However, the company has not been licensed with the regulator as the due process is yet to be commenced. In general terms, microfinance is the provision of a broad range of financial services to those excluded from the formal financial system. A variety of institutional models have emerged globally to serve microfinance markets including specialized microfinance banks, Non-Governmental Organizations (NGOs),

¹²¹ AML/CFT Law 2016 reg.

Gargaara company Ltd. The commercial banks in Somalia also have some accounts that focus on microfinance market segments.

Microfinance in Somalia, which includes several financial service organizations, are operating as informal financial service organizations. The existing legal framework does not include the monitoring of activities in the microfinance sector. It's essential for policy makers to pave the way for emerging microfinance institutions to develop an environment to formally operate and mobilize product offerings. KIMS is a microfinance company, the executives running the organization have a background of AML/CFT regulatory requirements, and based on a personal interview conducted, KIMS is willing to comply with the existing legal framework. KIMS has participated the NRA program and has contributed data and material for ML vulnerability assessment.¹²²

Recommended Actions.

- CBS should develop appropriate regulatory/supervisory tools to conduct proper oversight of foreign exchange houses.
- FRC should enforce AML/CFT regulations and conduct periodic off-site and on-site examinations. AML/CFT supervision guidelines should be risk-based.
- Ensure the building of the necessary capacity to efficiently enforce ML/TF regulations on MNOs companies.
- The FRC should enhance its AML/CFT supervision and regulation, and reach out to diverse unlicensed financial services companies.
- The government should speed up the introduction of the National Identification project.

Chapter 3: DNFBPs VULNERABILITY

The definition of the Designated Non-Financial Businesses and Professionals “DNFBPs” include: i) real estate agents, ii) notary public, iii) lawyers and their association, iv) accountants & auditors, v) gold, precious metals & stones dealers, vi) and second-hand car dealer. According to the current AML/CFT Law, the DNFBPs¹²³ sector should abide the AML/CFT 2016 Law and its consequent regulations. However, the law and regulations governing the DNFBPs, which should include comprehensive AML/CFT laws and regulations, have gaps in preventive measures to adequately align with FATF Recommendations¹²⁴.

Although FRC has recently started outreach programs and has developed regulations, in the moment, the DNFBPs sector is unregulated. Some professionals and businesses such as lawyers and the notary public companies are required to register with the Ministry of Justice. The other DNFBPs operate with a local or federal level permits, but they are functioning without AML/CFT oversight.

¹²² Interviewed; Mustafa Abdi Ali, executive director, other senior officers provided context material and data

¹²³ AML/CFT Law 2016, art. 4 sec. 2. (Institutions and professions subject to this Act)

¹²⁴ FATF. R.10, 11,12,13,14,15,17.

During the NRA process, the working group has contacted DNFBPs, and questionnaires were sent out for completion. However, the responses were not very informative, even though some of them responded. For instance, most sections in the questionnaires were incomplete and the quantitative information, in particular, was blank. Therefore, the following assessment is based on the discussions of the working group and the information received from the respondents.

-

a) Real Estate Agents Vulnerability

Real estate agents buy and sell on behalf of their clients in real estate transactions. Real estate agents are involved in the diversified auctioneering of several real estate properties. They represent owners who are present in Somalia or outside of the country when a real estate sale or purchase is taking place. While statistics or data are unavailable, it is estimated that real estate agent's property and lands sales are significantly high. Despite some of the agents' claim that they belong to an association, there is no way to confirm that all real estate agents are members of such an association.

During the civil war, the official land records for residential and commercial properties were misplaced or destroyed. Currently, the highly preferred property and land titles that are acceptable to buyers and sellers are older property titles version, i.e., land and property registered in 1990 and earlier. In cases where sellers have incomplete information, the verification of old titles are available in the black market.

When land exchange hands its handled through notary public and funds are cleared through the banks, or buyers and sellers have the option to pay and receive cash respectively. However, with regard to AML/CFT guidelines, banks are not retaining proper records from real estate transactions.

b) Notary Public

The notary public is licensing under the authority of the Ministry of Justice. There are 105 Notary public companies operating in the Banadir region and vicinity. Notary public companies operating in other jurisdictions outside the region of Banadir are licensed by their respective FMS local governments. There is no clear information available as to how licenses may be revoked or dismissed, or how the notary public may be deemed unfit to continue operation.

Notaries are authorized to administer oaths and affirmations, signature witnessing, authenticate documents, and perform other official acts. Notary public offices act as gatekeepers to the financial sector because before banks make decisions on contracts for loans or the transfer of assets, the documentations must be notarized.

Despite the and relevant regulations have placed specific obligations on notary public operators, they are not fulfilling their AML/CFT obligations. Additionally, the fact that operator can obtain licensing and legitimacy to operate as a notary public not based on merit, this can enable the commission of ML/TF. **The overall vulnerability rating for the Notary public is very high.**

c) Gold and Silver Dealers

There is no official list available, but there is small scale activity of gold and other metals being mined in Somalia. The majority of the miners are individuals who are not officially licensed or do not have local or federal permits. Moreover, gold and other metals dealers including silver dealers are small and medium jewelry dealers, according to the working discussions. The jewelry stores are resellers of ready-made merchandise purchased from the Middle East, wherein commodities are sold for profit in Somalia. Dealers buy unfinished gold and silver products and design work is done in Somalia.

As prescribed by the jurisdiction's AML/CFT Law and FATF R. 32, the gold and silver operators are reporting entities and are subject to follow the AML regulations. They are currently unregulated except for dealers that have store permits from local municipalities. Based on module calculations and working group discussions, the overall vulnerability rating is high.

d) Lawyers

Lawyers are those that have been through law school in Somalia and other law schools outside Somalia and have a license to practice as legal practitioners. Currently, the Ministry of Justice is the main authority that licenses lawyers to practice law in Somalia. Legal practitioners in Somalia have an association, where there is a requirement for legal practitioners to register and maintain their membership. The Somalia Lawyers Association, "UQS", has existed for a long time. Legal practitioners or companies are currently licensed through Ministry of Justice. During the National Risk Assessment process, it is difficult to measure the interaction between legal practitioners and other businesses such as real estate. Real estate transactions are mainly done through notary public offices. Unless there are legal issues, notarized documents are accepted by real estate sellers and buyers for both properties and land.

Several legal practitioners have been interviewed for the NRA stating that the business lawyers may be exposed to cash intensive business activities where customer background and purpose of the transactions end up unverified. The business activities and transactions may be subject to STR/CTR obligations. In view of all those circumstances, the working group has formed a view that the legal practitioners are vulnerable to potential ML activities/conduct, which can impact their compliance with AML obligations.

There are no AML/CFT regulations, guidelines, or other enforcement mechanisms in place, nor are there any resources committed to AML/CFT, and as such, lawyers are not adequately monitored for reporting and other obligations under the ML/TF act when they are dealing with their clients.

The UQS is the regulatory body responsible for legal practitioners adhering to Somalia's professional ethics standards, but UQS regulation does not cover AML/CFT obligations. The association, as a regulatory body, does not conduct AML/CFT supervision nor does it monitor the adequacy of reporting where legal practitioners are involved in the buying and selling of real estate; managing of client money, securities or other assets; management of bank, savings or securities accounts; organization of contributions for the creation, operation or management of companies; creation, operation or management of legal persons or arrangements; and the buying and selling of business entities.

Even though there is no evidence of the presence of indicators of potential ML activities/conduct, the absence of controls places the overall vulnerability of legal practitioners to ML as high.

e) Accountants

Somalia has no sound independent auditing standards and practices and has not yet passed a law that mandates the public and private sectors maintain financial transparency and proper and reliable accounting records. Reporting entities lack periodic mandatory independent auditing to evaluate past performance and financial statements ensuring the reporting entities are less vulnerable to criminal abuses.

Nevertheless, the Somali Institute of Certified Public Accountants "SICPA" is a self-organized accounting association. The proposed self-regulatory body was formed in 2012 and has a board structure. SICPA is registered with IFAC and has achieved membership from the Pan-African Federation of Accountants (both bodies are recognized throughout Africa).¹²⁵

In 2014, the World Bank assisted SICPA in drafting the Accounting Board Act for Somalia. Since then, the draft document is pending and waiting to be enacted by the Somali parliament. To speed up the process, SICPA board executives have held several meetings with FGS authorities.

The process is taking long and SICPA expects once the country's Accounting Act is passed, SICPA will have a legal mandate to create the required accounting board with professional members following AML regulatory guidelines adopted by the members. Consequently, without the country's Accounting Board Act, Somalia remains without audit rules, uniform quality of audits, and compliance to supervisory authorities.

In the meantime, the self-designated SICPA Board and their members are involved in accounting, auditing, and professional business activities. Additionally, the regulations drafted by SICPA, with the assistance of the World Bank Group, legislates that members follow AML regulation/guidelines.

¹²⁵ Interviewed; SICPA; Abdurahman Daud, the chairman of the organization in his presence, and Nur Muse, the CEO of the organization, also briefed the NRA Coordinator over the phone about the organization.

SICPA is a proposed Accountant Association but has no a legal mandate to operate. Therefore, a working group raised that in the absence of explicit AML/CFT regulation/guidelines, SICPA is potentially at risk to ML vulnerabilities. Consequently, without sound independent auditing standards and practices based on legislation and adhered to by the public and private sectors and due to lack of proper and reliable accounting records, the country remains deprived of financial transparency.

Unlike other DNFBPs, SICPA members' vulnerability rating is lower because SICPA business activities are lower compared to other businesses and professionals in the same group. However, the overall risk in the DNFBPs sector is **higher**, and therefore, so long as SICPA is operating without a legal mandate, in an environment with high ML vulnerability, SICPA's risk exposure is also rated as **High**.

f) Second-Hand Car Dealers

The assessment did not establish the exact number of second-hand car dealers operating in Somalia. Procedures to import second-hand vehicles for the purpose of reselling are not available. Importers have free access to import used vehicles. The majority of used vehicles available are Japanese made. Product specifications, including operator manuals, translated in the local language or other popular languages are unavailable.

Additionally, the new owners are stuck with owner operator manuals written in Japanese or far east languages. There is no association or regulatory oversight that controls them. When vehicles exchange hands, buyers have an option to test the vehicle's mechanical conditions. Once titles of ownership exchange hands the sale is final. Certainly, this process is not based on due diligence, oversight, or consumer protection.

The second-hand car dealers' transactions are cash transactions; however, the average annual turnover value is unavailable. Short-term financing is available through commercial Banks. Buyers make financing arrangements with their banker. The dealers in this situation receive their money from the buyer's bank. The fund transfer through banks is only possible when the buyer and the seller have accounts in the same bank. Interoperability between commercial banks is not available at moment.¹²⁶ Alternatively, the dealer will accept cash from the buyer's account. The process is undermining integrity of the AML regulations and is subject to ML/TF vulnerabilities.

Recommended Actions.

¹²⁶ Somalia interbank clearance and switch system is in process to be operational, at the time of this writing.

- With the real estate market and agents, self-regulatory bodies should be a priority in establishing and providing legal mandates, so its membership and mandatory registration may be recognized.
- The self-regulating bodies must also have resources available for enforcement, transaction monitoring, and reporting requirements, including conduct onsite examinations and maintaining proper recordkeeping methodologies.
- Local and federal authorities should ensure AML/CFT regulatory guidelines are included in the real estate regulations and resources are allocated for capacity building. Professionalism and ethical standards should be an industry wide practice.
- Information on real estate transactions is not publicly available, as in some instance transactions are done without ascertaining customer information wherein cash is exchanged.
- Data and relevant transactional materials should be available and accessible for national purpose, and clauses authorizing accessibility should be inserted as part of the literature (data sharing clause).
- CDD and recordkeeping requirements should be implemented to ensure full compliance with the FATF Standards
- The authorities responsible with land registration i.e., the local municipality of Mogadishu, Ministry of Industry (responsible for large land registration and licensing for investment), and Ministry of Commerce must bring to clarity their roles as regulatory authorities.
- For notary publics processing real estate transactions, authority must also mandate and enforce regulations requiring legal practitioners be part of the process of the buying and/or selling of real estate for, or on behalf, of their clients and the buying and selling of business entities on behalf of their clients. This is due to the legal nature of the real estate transactions, and them being long term commitments. There should be separate legal counsel representing buyers and sellers involved in real estate transactions, wherein there are no ambiguities in the legalities.
- Notary public offices handle diverse transactions particularly the real estate sector for the banks. Therefore, cash exchanging hands is huge compared to other DNFBPs.
- Their lack of AML/CFT training or regulatory guidelines is a serious concern for the Notary public. Notaries are not currently reporting STRs and LCTRs to FRC also puts the Notaries at a high ML/TF vulnerability.
- Legal practitioners should be mandated to register with their respective associations. Once the oversight body is in place, lawyers' business practices may be aligned with AML/CFT regulatory guidelines. This will ensure that lawyers' business activities relating to dealing with clients are closely monitored and hence, AML/CFT regulation and supervision guidelines that are applicable to reporting entities will also be applicable to the legal practitioners.
- SICPA and similar accountant associations should be legally mandated as a self-regulatory bodies governing the accountants' sector. The accountant associations mandate should be robust and extend their supervisory role to include AML/CFT issues. This will ensure that regulations and guidelines are put in place so that AML/CFT examinations are conducted regularly. Standards and ethics in the accountant associations sector must also incorporate AML/CFT regulations.
- Second-hand car dealers should set up their self-regulatory associations. In addition to regulations and obligations, second-hand car dealers must comply with AML/CFT regulations. Considering car

dealers are reporting entities, they should identify their potential car buyers, retain records, and report STRs and LCTRs.

- All records including the dealer’s business transaction activities must be available and accessible for periodic on-site examinations. Current AML/CFT law and regulations give the mandate and the powers for FRC to enforce the law.
- AML/CFT control measures should be in place, merchants licensing authority including local municipalities and the Ministry of Commerce and FRC should inform the industry operators about their AML/CFT regulatory obligations. They are required to report suspicious transactions to FRC and retain records.
- The second-hand car dealers’ market is cash based, and dealers do not retain records of buyers’ sources of funds. The assessment found indicators for potential ML activities/conduct in the second-hand car dealers’ marketplace.
- Second-hand car dealers do not have an association with board members, i.e., as self-regulating entities that can draft guidelines for good business conduct and professionalism and Consumer and Dealer practices.
- Second-hand car dealers are not in compliance with AML/CFT Law and regulations, and do not meet their reporting obligations.
- The information regarding the regulatory authority for second-hand car dealers, enforcement mechanisms, governing associations, and oversight is unavailable.
- Resources are not committed for AML/CFT regulation, controls, and transaction monitoring mechanism in the DNFBP sector, lack of detailed record keeping, sources of funds, purpose of the transaction.

Table 12: Priority Ranking Designated Non-Financial Businesses and Professionals

PRIORITY RANKING - DNFBPs SCENARIO	PRIORITY RANKING**
Comprehensiveness of AML Legal Framework	3
Effectiveness of Supervision/Oversight Activities	2
Availability and Enforcement of Administrative Sanctions	8
Availability and Enforcement of Criminal Sanctions	9
Availability and Effectiveness of Entry Controls	5
Integrity of Business/ Profession Staff	6
AML Knowledge of Business/ Profession Staff	1
Effectiveness of Compliance Function (Organization)	3

Effectiveness of Suspicious Activity Monitoring and Reporting	7
Availability and Access to Beneficial Ownership information	11
Availability of Reliable Identification Infrastructure	10
Availability of Independent Information Sources	12

Chapter 4: TERRORIST FINANCING RISK AT NATIONAL LEVEL

- 5.
- 6.
- 3.

3.10. Somalia Context for Terrorist Financing.

In effort for government to develop preventive measures to combat Terrorism and TF, in February 2016, Somalia signed into law the Countering the Financing of Terrorism Act. The prevention of Terrorism part II art. 3, criminalizes TF making it an offense liable to imprisonment for a term of 10 years.

Also, other subsections of art.3 Part II further strengthen the criminalization of TF, subsection 3a stating, “participat[ing] as an accomplice in an offence within the meaning of subsection (2); criminalizing TF stated as; even if a terrorist act does not occur or is not attempted; even if the funds were not actually used to commit or attempt a terrorist act; and regardless of the state or territory in which the terrorist act is intended to occur”. also, part II of the Act aligns with the requirements of FATF Recommendation 5 which promotes countries having the legal capacity to prosecute and apply criminal sanctions to persons that finance terrorism.¹²⁷

The criminalization of terrorism is also covered under the penal code 5, art. 185¹²⁸, [41 P.C. who bears arms against the State or serves in the armed forces of a State at war with the Somali State]. The law is aligned with Al-Shabaab who bears arms against the state and its citizens, including having an affiliation with foreign insurgents, such as Al-Qaida and ISIS.

The Federal Government of Somalia (FGS) remains a committed partner of the United States and other international partners in the ongoing fight against al-Shabaab (AS) and ISIS-Somalia. The FGS has taken

¹²⁷ FATF Interpretative notes to R.5 sec. A1

¹²⁸ *Art. 185. (Citizen Who Bears Arms Against the Somali State). As 1. A Somali penal code 5*

steps to improve the security sector and has implemented institutional reforms designed to improve its CT capabilities. In September 2016, the Federal Government of Somalia took the initial steps to implement its obligations under the United Nations Security Council and General Assembly Resolutions by adopting a National Strategy and Action Plan on Prevention and Countering of Violent Extremism¹²⁹.

In 2017, in the broader security context, the FGSa, the United Nations, international partners, and AMISOM endorsed the Comprehensive Approach to Security (CAS) integrating PCVE with military and law enforcement efforts, aiming to enable Somali authorities at the federal and state levels to provide security for their own citizens, including;

- The proposed concept “Prevention of Violent Extremism” is designed to limit the traction of terrorist groups on individuals, communities, and society at large.
- Solid analysis and evidence-based assessments of specific, settings-based factors that lead to affiliation with violent organizations are needed.
- This requires a bottom-up approach to identify root causes, push and pull factors, recruitment strategies, and drivers of violent extremism.
- It is crucial to link those efforts with a top-down approach that addresses progress required and led by the government on policies and programs to enable national and sub-national authorities and international actors to effectively take on root causes and drivers of violent extremism.
- Somali federal and state authorities have identified P/CVE coordinators and focal points in the relevant line ministries, which form the basis of a mechanism that allow for top-down and bottom-up communication flow and an implementation scheme contributing to relevant intervention and confidence building.
- Additionally, this approach provides opportunities for evidence base research and actions that if relevant and efficient can then be integrated into policies.

What is noteworthy is that even with all the action plans stated in paper, there are no records or evidence showing the FGS, FMS, and the region of Banadir have the taken steps necessary to mitigate the risk of the violent extremists. Regrettably, AS has succeeded to intensify its violent extremism, is actively engaged in contending with governments, and remains a threat to citizens’ safety.

Somalia continues to stabilize politically, but government institutions are weak. state capacity is severely constrained, and law enforcement, prosecutorial officers, and judicial offices remain understaffed and undertrained¹³⁰.

¹²⁹ pursuant to relevant UN Resolutions on CT and PCVE/UNSC Resolution [1373 \(2001\)](#), [1624 \(2005\)](#), [2178 \(2014\)](#) and the Secretary-General’s Plan of Action.

¹³⁰ US State Dept Terrorism Report 2016

Consequently, AS retains de facto control over significant portions of the country, particularly in south-central Somalia and continues to move freely, collect “taxes,” and exert governing authority in the areas under its control. Moreover, AS has conducted multiple and high-profile terrorist attacks in Somalia and appears to increasingly use targeted assassinations against key government figures and community leaders to undermine the credibility and effectiveness of Somali government institutions¹³¹.

Despite major security gains, the Somali National Army (SNA), AMISOM, and other allied militias were unable to reduce al-Shabaab’s ability to plan and execute attacks and major deficiencies the fight against the insurgency remain. Al-Shabaab has leveraged clan politics and disputes to fuel non-cooperation and distrust among local communities toward security forces operating in these areas.

Al-Shabaab (AS) has existed since the early 2000s and started their active conflict in 2006. In 2019, AS had a strong presence in Somalia, and the group has the potential to maintain actively warring with the Somalia government.

Currently, AS has its claws in every sphere of the country’s economic system, including the judicial system and the country’s intelligences services. This penetration has allowed AS to exercise their powers to generate revenue and maintain such control.

First, they execute their influence by way of intimidation and the extortion of targeted individuals, usually someone who has access to power. Secondly, AS secure support by government officials or a clan leader by offering money. Additionally, AS recruit important people who hold high positions in the government, convincing them that AS is a righteous group. Regardless of the danger involved, the target individuals have one thing common: upon receiving instructions, their job is to execute what they are asked to do and when they are asked to do it. Usually, those individuals block and interrupt government services, making it possible for AS to conduct serious, and violent crimes. With AS having access to internal collaborators, AS has majorly impacted the government’s abilities to enforce rules and regulations and prohibit or hinder its collaboration between government bodies, making the government ineffective in managing the country’s economy and security.

Al-Shabaab has also exploited poor economic conditions to recruit new fighters. These vulnerabilities have helped to undermine AMISOM and SNA territorial gains. Federal, local, and regional security authorities lack sufficient capacity and efficient command and control to prevent most of al-Shabaab’s attacks.¹³²

Despite Al-Shabaab experiencing increased defection rates and weakened leadership, the group has retained the capacity to conduct asymmetric attacks throughout Somalia. They executed attacks

¹³¹ Country Reports on Terrorism, CT Bureau
¹³² Country Reports on Terrorism, CT Bureau

against harder targets in Mogadishu, including the Aden Adde International Airport, the Presidential Palace, and popular hotels that had security guard forces present. Al-Shabaab has also increased the frequency of assassinations of government personnel, many of whom were associated with AMISOM, Somali security services, or held other federal government positions.¹³³

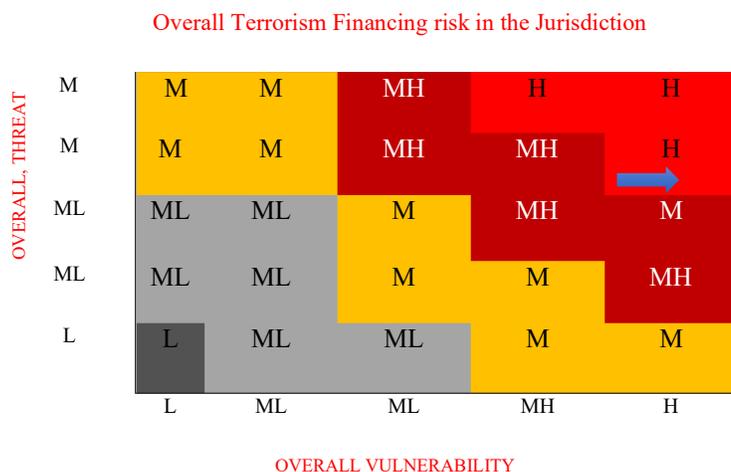
Somalia remains a safe haven for terrorists who use their relative freedom of movement to obtain resources and funds, recruit fighters, and plan and mount operations within Somalia and in neighboring Kenya.

Additionally, while ISIS senior leadership did not formally recognize a Puntland-based ISIS-aligned faction in 2016, they have provided some support to establish a branch in East Africa. In October 2016, the ISIS Somalia faction temporarily took control of Qandala, a coastal town in Puntland’s Bari Region. Puntland’s security forces organized an operation that dislodged the ISIS fighters with little resistance, forcing them into mountainous camps south of the coast¹³⁴. Despite these challenges, Somalia is committed to combat terrorism and TF within Somalia.

3.11. OVERALL NATIONAL TF RISK ASSESSMENT

Figure 2: Risk level functionality Threat compared to Vulnerability.

The overall National TF risk for Somalia is **high**, encompassing the overall threat, which is rated **High** and the overall vulnerability which is rated also as **High**. The findings and details that underlie this assessment are found below:



¹³³ Country Reports on Terrorism, CT Bureau
¹³⁴ US State Dept Terrorism Report 2016

Al-Shabaab has organized their financing robustly within Somalia and the Group's threat level is escalating.¹³⁵ The future trends of AS activities appear to raise the levels of personnel size and assets. AS' methodology of finance is becoming more sophisticated and expansive, which has increased the threat level in Somalia. Moreover, as the group's organization is expanding, their need for finance is also increasing.

AS continues to threaten Somalia and the region and raises funds through multiple sources. AS uses illicit finance processes to raise funds, move funds, pay for expenses, and store the residuals. The source of funds is classified as illegal donations, illegal taxations, and other forms of income such as, taxing agriculture, trade finance, and real estate transactions.

AS also illegally taxes vehicles, commodities, livestock, imports, exports of charcoal, and construction activities, and raises revenue through extortion. In addition, when the group is short on cash, donations from clan heads are expected to fill the group's financing gap.

AS is involved in smuggling weapons and explosive materials into the country for the use of attacking the public institutions and civilians. AS moves funds through remittances, Somali banks, cash carriers, and mobile money via telecommunication service providers. Cash and assets are typically transferred through similar mechanisms.

AS employs a secure financial management system based on following rules strictly: funds are accounted for and receipts and records are maintained. In the process, expenses are paid, and residual funds are securely stored in safe locations.

Currently, AS is generating a large amount of money through diverse sectors in the economy. Funds generated in Somalia are used for AS operations and it is likely that AS is not receiving funds generated from other jurisdictions. However, there are possibilities that funds generated in the home jurisdiction are used for operations in foreign jurisdictions. There are indications that AS uses several transit points in south and central Somalia in remote locations in Somalia making it difficult to monitor, intercept and identify when and where funds are moved, particularly funds moved outside Somalia is unknown.

It is important to note that current AS financing methods are different from conventional sources of insurgency financing. Normally, violent extremists have raised their finance through meagre donations from sympathizers or sourced by state sponsored TF. However, with other viable solutions for their revenue generation, AS is competing in generating more revenue than the government of Somalia, in which, AS has succeeded to surpass government in raising revenues.

¹³⁵ TF information provided in this section is received, and its combination of information from intelligence authorities, and other sources that are deemed to be credible by the jurisdiction, including open-source information, such as reports from government agencies, international organizations, civil society organizations, and academic literature or credible news sources. Please note, no other references will be quoted here in this section.

The revenue generation within the jurisdiction is estimated to raise 25M USD per year, which is a 20% increase from 2019 to 2020. AS retains more money than they collect. In 2019, AS expenses were 74% of their revenue and the retained proceeds were estimated to exceed 57% of the group's revenue in the same year.

3.13. National vulnerability to TF

Consequences of the terrorist acts are significantly affecting the country's security, and their dangers have prevented people from freely moving around the country, more particularly in southern and south-central Somalia. In the main cities like Mogadishu, people live in constant fear and under the threat of intimidation. Clan elders, federal and state ministries, and members of parliament are targeted and are prevented from going around the capital city of Mogadishu unless accompanied by security guards.

Given the security situation, the only mode of transportation through the southern and central Somalia is by air as Al-Shabaab controls most of these areas in Somalia. Government staff members or civil servants are unable to visit their native towns inside Somalia. There are several vulnerabilities that negatively impact the capacity of Somalia to combat TF. AS' highest salary is \$25,000.00 per month paid to the Emir and lowest is \$30.00 paid to the Jabhat (new cadet). The next step up is Hisbah (trained cadet) and Jabhat driver are paid \$70.00. Apart from brainwashing the youth with religious doctrines and other fabrications, AS recruiters entice the youth with these meagre salaries. The youth salary is good enough to buy food and support their families. There is poverty and extreme levels of unemployment in Somalia specially for the youth who represent over 70% of the population. AS recruiters take advantage of this dynamic and offer the youth jobs and income.

Moreover, it is presumed that the combined FGS and FMS road taxes are lower than AS taxes. However, cargo truck operators prefer paying to AS, given it is a one-time payment at a checkpoint where a trucker is issued a receipt that secures travel through the group's-controlled territories. Alternatively, FGS and FMS tax collectors may have charged the same trucker multiple times and little or nothing would have gone towards the government revenue.

Consequently, such corrupt practices by government officials create an environment whereby AS incidentally supports AS TF efforts. In some situations, the AS judicial system is swift and completed within a short period of time and some public services are offered free of charges. Another vulnerability is the government's inability to supply food to poor people in remote AS controlled areas. Often, international donors have addressed this situation by providing goods to the needy in AS controlled areas. However, for the goods to be allowed access into the affected areas, the donors are forced to pay taxes on the commodities and road taxes to AS. The funds

usually collected by the check point guards and receipts issued¹³⁶. Additionally, the taxes or fees collected will not guarantee the protection of anyone from AS violence. Farmers are not allowed to use the river and its canals unless they pay special taxes for irrigation.

Among the TF vulnerabilities identified are the authority's poor policy coordination. One positive aspect is the existence of laws and regulations; however, due to the lack of coordination and collaboration among agencies responsible for collectively prosecute criminals, the existing laws and regulations are not adequately applied by LEAs and the judiciary to appropriate to prosecute the criminals.

Another vulnerability is that the LEAs and judiciary are not effectively aligned with the country's laws and regulations with the successful targeted financial sanctions regime¹³⁷ in compliance with UN Security Council resolutions relating to TF¹³⁸.

The country's judiciary, law enforcement, and intelligence gathering agencies lack the capacity and institutional framework to collaborate and coordinate. Moreover, the clandestine nature of the country's national security agencies and policing system negatively impact bringing perpetrators to justice. These agencies do not utilize an effective and coordinated policy approach and lack the ability to work with communities and develop an outreach mechanism that supports the effective prosecution of criminals.

Other relevant laws are traditional and are used among clans, such as so called "xeer" - an operative vehicle that is sometimes above the law whereby clan elders intervene the judicial process regardless of the nature of the cases involved.

Additionally, the quality of intelligence gathering is extensively weak, causing insurmountable challenges, and impacting the intelligence agencies' capacity to combat AS not only in terms of collecting funds from the public, but also preventing them from conducting suicide attacks.

The intelligence agencies lack the capacity to gather quality intelligence and the lack the aptitude to process TF related data and lack the right specialization concerning the financial aspects of terrorism. The TF related STR and monitoring of suspicious activities are ineffective. Additionally, the number of STRs submitted related to TF and the number of cases forwarded to LEAs for investigation related to TF are insignificant.¹³⁹ Likewise, the capacity and commitment of reporting institutions to comply with the UN sanctioning regime and screening requirements are unavailable.¹⁴⁰

¹³⁶ Currently, most international donors are opted to pay cash to the needy.

¹³⁷ FATF judicial or administrative measures not conditional upon the existence of criminal proceedings

¹³⁸ <https://www.fatf-gafi.org/media/fatf/documents/recommendations/BPP-Fin-Sanctions-TF-R6.pdf>

¹³⁹ part v. supervision and monitoring of compliance

¹⁴⁰ <https://www.fatf-gafi.org/media/fatf/documents/reports/Guidance-Countering-Proliferation-Financing.pdf>

The adequacy of human resources for CFT including specialized investigators, an FIU, intelligence officers, prosecutors, and judges, and the financial resources allocated to terrorism financing investigations are all major obstacles. As part of the main crosscutting themes, the military courts and national intelligence agencies have not cooperated; therefore, they are not utilizing their resources, knowledge, and details of TF cases. For instance, in the military courts system, it is unknown whether the judges who preside over TF and related AF cases can function effectively. If the criminal bench is adequately structured, funded, and staffed by persons with appropriate skills and background both on the defense and prosecution. It is also unclear that they have the training or skills, especially in financial crimes (including TF and AF), financial products/services, and the financial process, or are provided with sufficient financial, technical, and other resources to perform their functions. Additionally, it is unknown whether prosecutors can obtain access to all the necessary documents or whether the prosecutors have access, information, and witnesses and/or other relevant individuals for use in prosecutions that have the knowledge of specifics related to TF and typologies and present such cases to the court. Therefore, if all of this information is unavailable mainly because of the lack of cooperation, and where it is desirable to have set of obligatory guidelines to appropriately combat with Terrorism and TF.

There is also a lack of domestic data in regard to legal requests received on TF cases and same is applicable to mutual legal request from abroad. The country's FIU lacks the resources to perform its functions, and effectively utilize financial intelligence gathering. The agency is in its early stages in evolving in the formulation of national CTF policy and coordination strategy. Despite the fact that by law, LEAs have enough powers to use compulsory measures to produce records held by FIs, DNFBPs, NPOs and other legal persons, for the search of the persons and premises, taking witness statements, and the seizure and obtaining of evidence.

There are ineffective mechanisms to ensure that the competent authorities use the right process to identify assets subject to confiscation, without prior notice to the owners and bring them to justice. Moreover, because of ineffective laws and practices, safeguards are not in place to preserve the integrity of the investigators. Due to cross-cutting issues, there is a lack of cooperation between the Federal Government of Somalia and regional states on TF offenses. This is a huge factor limiting the abilities of the country's LEAs to effectively investigate suspected terrorists, and terrorism incidents committed or taking place in the Federal Member States, including the main Banadir region where Al-Shabab activities are heavily concentrated.

There is no coordination and a lack of political commitment and support in the fight against TF, specifically concerning supporting the designated authority or national coordination committee or high-level interagency committee ("coordinating authority") that oversees the formulation, coordination, and implementation of CFT policies and strategies. Additionally, the coordination of the authority's powers and responsibilities are not clearly laid out in law or regulation. Even though, Somalia's Ministry of Internal Security has proposed to head all of the LEAs including

country's border officials, there is a lack of policy and strategy based on an up-to-date scheme for Somalia to effectively formulate its national CFT strategic policies and prevention programs in relation to de-radicalization.

Somalia's porous borders have contributed to regional insecurity as al-Shabaab and others continue to move freely bringing income and goods or carrying cash outside the country.

There is lack of a comprehensive customs regime with an absence of the capacity to protect and detect the physical cross-border transportation of cash, intercept or restrain cash that is suspected of being related to TF, and intercept or restrain cash falsely declared or disclosed on the suspicion of TF. There are also ineffective legal powers to implement and apply appropriate sanctions for making a false declaration or disclosure and enabling the confiscation of cash that is related to TF or the effectiveness of the operations. Similarly, the immigration controls are not effective in preventing and detecting illegal goods in most the border control locations. Moreover, Somalia does not have a central or shared terrorist screening watchlist, nor does it possess biographic and biometric screening capabilities at most of ports of entry.

Additionally, research shows that in countries where 60% of the population is under 30, like Somalia (70%), the risk of civil conflicts is much higher.¹⁴¹ These rapid demographic factors combined with high unemployment rates may facilitate terrorist activity, thus increasing the country's vulnerability to TF.

Recommended Actions.

- Designate an authority or national coordination committee or high-level interagency committee (“coordinating authority”) that oversees the formulation, coordination, and implementation of CFT policies and strategies:
 - Coordinating authority's powers and responsibilities should be clearly laid out in law or regulation, and the authority is headed by a ministerial or deputy ministerial level official.
 - Policy and strategies should also be included de-radicalization and prevention programs.
- Policy and strategy should be based on the finding of the NRA that has been conducted with all relevant government departments and agencies (including intelligence agencies); and private sector and government participants were not unduly restricted from sharing relevant information and data.
- Develop comprehensiveness of Somalia's asset forfeiture laws, enabling competent authorities to seize, freeze, and forfeit proceeds and instrumentalities of crime.

¹⁴¹ <https://worldpopulationreview.com/countries/somalia-population>

- Clearly define the extent of the asset recovery laws to property, that is, the proceeds of, or used in, or intended or allocated for use in, the financing of terrorism, terrorist acts or terrorist organizations, and property of corresponding value held by the criminal defendant or third parties; provide authorities with a legal basis to identify and trace such property; permit authorities to carry out rapid provisional measures, such as seizing or freezing of such property, to prevent the transfer or disposal of the property; provide authorities with a range of asset forfeiture tools, including criminal forfeiture, non-conviction based (NCB) forfeiture, enforcement of foreign NCB orders, and administrative forfeiture, consistent with domestic law; and ensure that the rights of bona fide third parties are safeguarded.
- FRC combating of TF is currently unable to function effectively and efficiently. The Agency is not adequately structured, funded, and staffed by persons who have appropriate training and skills, and they have limited understanding of financial products and financial processes. Therefore, FRC should be provided with sufficient financial, technical, and human resources to perform its functions. There should be an understanding that the FRC has sufficient operational independence and autonomy, free from any undue political, government, or industry influence or interference to carry out its functions freely, including the autonomous decision to analyze, request, and/or disseminate specific information; safeguards are in place to preserve the integrity of the staff (in law and in practice); staff of the FRC must maintain high professional standards (including those related to confidentiality and integrity); the STR system must work effectively, including reporting, analysis, and dissemination. FRC should be able to disseminate, spontaneously and upon request, information and the results of its analysis to relevant competent authorities and have timely access to databases of other domestic agencies and commercial sources and be able to obtain additional information from reporting entities for its analysis; and have the capacity to detect cross-border activities.
- Strengthen the quality of FRC intelligence gathering and processing on TF: the agency must have the capacity, resources, independence, and autonomy in practice to perform its activities without fear or favour. The agency should also develop the skills, experience, and powers to trigger and support TF and AF investigation.

Chapter 5: Non—Profit-Making Organizations (NPOs/NGOs)

Non-Profit organizations “NPOs” and Non-Governmental Organizations “NGOs” are types of charity organization operating in Somalia. Their activities are consistent with the FATF R.8 definition of NPO¹⁴². NPOs/NGOs represent vital roles in the communities in Somalia including working with people in the remote areas in the country. Thus, the NPOs and NGOs business focus and operations are similar, but they are different in their setting. The NPOs are non-profit organizations that are locally registered, and their activities are limited in the national level.

¹⁴² See FATF R.8

Although, some NGOs are also locally established charities, NGOs are normally arranged and registered from other locations outside Somalia.

According to the Ministry of Planning NPOs/NGOs registrations office, there are 106 NPOs and 144 active NGOs registered as local non-profit organizations. The Ministries responsible to regulate the NPOs/NGOs are: the Ministry of Interior “MoIFAR”, the Ministry of Planning “MoPIED”, and the Ministry of Finance “MoF”. There is information available on the website of the Ministry of planning “MoPIED”; however, the ministry has not responded to our multiple requests for the rest of the available information, which we have been told that includes monitoring and evaluation and may have further details.

Somalia received \$1.887 billion USD in 2019, and \$2.102 billion USD in 2020 in official development assistance¹⁴³ (ODA), comprised of roughly equal volumes of humanitarian and development aid¹⁴⁴. The Somalia Development and Reconstruction Facility (SDRF) serves as both a coordination framework and a financing architecture for implementing the National Development Plan (NDP). The vulnerability in the SDRF disbursement is that it is cash intense as there is no overseas banking and correspondent services. Moreover, the share of development aid channeled through SDRF funds system in 2014-2020 is much smaller than the share of development aid channeled outside of the SDRF systems¹⁴⁵. Therefore, the transparency in aid management diminishes when funds are channeled outside the government system¹⁴⁶.

Part III of AML/CFT law 2016, Art. 4: “Institutions and professions subject to this Act¹⁴⁷”, sec. 3, only states “such other entities as may be prescribed in regulations by the Financial Reporting”. However, the Regulation 6 of Compliance Programs, secs. 6.18, 1-5 stipulate a clear direction given to reporting entities, including the financial institutions and DNFBPs, to conduct Customer Due Diligence and perform Enhanced CDD and monitor their activities when dealing with the NPOs/NGOs¹⁴⁸.

There is a lack of cooperation to identify: the information requested for review when available and evaluate the NPOs/NGOs quality of governance; the quality of financial management; quality of project management; quality of staff vetting and oversight; level of ethical commitment. Additionally, the information, if made available, would have supported the responsible agencies in knowing more about the profiles of the NPOs/NGOs operating in Somalia, their sizes, activity type, the complexity of their controls and structures, level of accountability, level of verifiability of fundraising methods,

¹⁴³ <https://aims.mop.gov.so/envelope-report> and <https://fts.unocha.org/countries/206/summary/2021>.

¹⁴⁴ MoPIED, aid flows

¹⁴⁵ MoPIED, use of SDRF funds, 2014-2020

¹⁴⁶ **On Budget:** Aid is integrated into the budgeting process and is reflected in the appropriation act. Only aid delivered on treasury in Somalia can also be reflected fully on budget, whereas aid channeled outside the treasury is considered off budget. **On Treasury:** Aid is disbursed into the Treasury Single Account (TSA), recorded on the Somalia Financial Management Information System (SFMIS), and managed through government systems.

¹⁴⁷ AML/CFT Law 2016

¹⁴⁸ FRC – AAML/CFT Governance and Compliance Regulations, (revised 2019)

disbursement, and number of cash transfers. Also required to evaluate the length of operational chain and the level of professionalism.

Despite the poorly managed charities organization, which is far from the FATF objective of R.8 ensuring that NPOs are not misused by terrorist organizations or pose as legitimate entities; however, there is no information regarding no cases, charges, or cases of the diversion of funds; NPOs/NGOs affiliated with terrorist activity or support to recruitment efforts; or the raising funds for terrorist or terrorist organization. The NPOs/NGOs are mostly use Somali money transfers for their disbursement of funds and remittance. There is no information available as to who and why they pay, and which parties they are on their behalf there are disbursing funds.

These organizations have contributed to Somalia's economy by raising or disbursing funds for purposes such as charitable, religious, cultural, educational, and social purposes, or carrying out of other types of "good works". There is little or no information available about their budget, financial records, and the government authorities accountable have not shared relevant financial data with the team working on this report.

This paragraph would benefit from more information about any reports submitted by NPOs/NGOs on the regulatory agency of their financials. If there are none, they should identify and explain why this has occurred. The NGOs/NPOs should apply focused and proportionate measures, in line with the risk-based approach, to protect their activities from TF abuse. Additionally, the NGOs/NPOs rely on foreign based donors for their budgetary support. Despite being non-compliant with standards and best practices for charity organization, NGOs/NPOs only channel of delivery available to receive and remit funds is through Somalia Remittances Services Companies. Those factors are the main drivers putting the Remittances companies and Somalia charity organizations at high risk.

Recommended Actions.

- The country's AML/CFT Laws 2016 should be updated to comply with the FATF R.8 with its interpretive notes, to make the country laws align the international standard and best practices.
- The FRC should develop regulations and guidelines that require that high-risk NGOs/NPOs retain records and set up internal controls, and to make their books available to competent, supervisory, and investigative authorities upon request.
- The FRC should focus on those NPOs/NGOs that have been identified via a risk-assessment as high risk for TF.
- The adequacy of the AML/CFT 2016 law and relevant regulations should be reviewed in line with the findings of this NRA Report of 2020. Somalia should use effective approach involved in the following:
 - Sustained outreach, targeted risk-based supervision or monitoring, and effective investigation and information gathering
 - Develop effective mechanisms for international cooperation.

- The Country’s competent authority should initiate and strengthen the quality of outreach and by educating the stakeholders involved in the country’s charitable organizations.
- Review and revise the quality of NPO policies; the scope of registration of NPOs that ensuring they meet the FATF definition; the accessibility of accurate NPO/NGO information; and the actions to prevent the disruption of legitimate NPO/NGO activities.

Chapter 6: FINANCIAL INCLUSION PRODUCTS VULNERABILITY ASSESSMENT

The current AML/CFT regulatory environment is weak, therefore the regulators are utilizing current standards and practices to effectively regulate the banking sector, specifically in regard to offering financial products to serve the unbanked segment of the communities, proposed as financial inclusion.

However, in assessing the risk and mitigation of financial inclusion, proportionate, risk-based AML/CFT controls may be applied to products or services intended to support financial inclusion, based on the nature and on the level of assessed ML/TF risks associated with these products or services. The products and services provided to newly banked people are often entry-level products and services with limited functionality or with restricted use¹⁴⁹. These types of products and services, by their own nature, may carry less ML/TF risks than other banking products and services. Therefore, in less risky environments, those types of accounts are eligible for exemptions from some AML/CFT controls or CDD depending on the extent of lower risks¹⁵⁰.

Although the banks are not following standard financial inclusion AML/CFT policies, the commercial banks and other financial services providers continue to offer diverse products and services such as mobile money, remittances, funds transfers, and e-money, which have facilitated unintended financial inclusion and the use rate is growing substantially. Consequently, the commercial banks are attracting a good number of customers by offering those types of products and services.

Financial inclusion in Somalia

Globally, close to one-third of adults – 1.7 billion – are unbanked, and about half of unbanked people include women poor households in rural areas or out of the workforce¹⁵¹. Economic theory and recent empirical evidence suggest that access to savings, payment and credit services can play a key role in poverty alleviation. Despite the benefits, significant financial exclusion persists across sub-Saharan

¹⁴⁹ FATF guidance AML/TF Measures and Financial Inclusion. 2017

¹⁵⁰ <https://www.fatf-gafi.org/media/fatf/content/images/Updated-2017-FATF-2013-Guidance.pdf>

¹⁵¹ The Global Findex database 2017

Africa. Savings, payment, and credit services facilitate household level consumption smoothing, help to insure against risk and allow investments in education and other forms of capital.¹⁵²

In Somalia, the mobile money sector has increasingly been positioned to serve the unbanked segment in the community. Mobile money products are used for sending and receiving funds, storing funds, and useful for basic financial transactions. Progress made in the mobile money industry may soon influence how the low-income consumers connect with banks and even potentially seek small loans from the commercial banks.

Inadvertently, MNOs have taken some steps to prevent the threat of ML and TF, by putting a cap on the value stored on users' devices. However, FIs are required to comply with AML/CFT regulations and to identify customers before accounts are opened, with proper identification promoting financial inclusion. Additionally, it is imperative that financial institutions and other financial services providers, including the MNOs, adopt FATF based financial inclusion guidelines.

Identification documents that are being allowed by the banks include: a letter from a traditional leader, a letter from an employer, an identity card from employer, a letter from a college or a school identity card, with official stamps and passport-sized photos of the bearer.

According working group discussions, the bank savings accounts, current accounts, and other similar basic accounts pose low ML vulnerabilities. However, given the Somalia's lack of proper identification infrastructure, this limits the ability for financial services companies to conduct proper CDD and EDD procedures. Moreover, the lack of set thresholds on the number and value of transactions, account monitoring challenges, and the lack of proper guidance by regulators on what should be allowed as simplified identification requirements, causes confusion and amplifies the frequency of financial services providers classifying certain accounts under financial inclusion.

The below assessment is based on financial inclusion products such as basic bank savings accounts, bank credit accounts, accounts deducted for certain groups of the community, i.e., women, such as the Marwa and Mandeeq accounts, student accounts, family designated tuitions and school accounts, mobile and e-banking, local money transmission, and micro-credit. Those are products are given different names by different financial institutions.

The assessment targeted banks, mobile payment service providers, local cash remitters, and micro-finance institutions. There are twelve banks operating in the country, one mobile payment provider, and one microfinance company, twelve Money Transmitter Businesses, and Gargaara Company Ltd¹⁵³, which is a public owned company promoting financial inclusion.

¹⁵² Financial Inclusion in Africa, 2013 - African Development Bank (AfDB)

¹⁵³ Newly established public funded microfinance company, profit-making institution.

Establishing a bank account is primary condition for Gargaara. Once the account is set up, credit application for small loans is considered for new patrons where the SME loan application is processed. Although, Gargaara is adding synergy to the loan market, Gargaara is facing challenges in the financial marketplace. (The challenges, see annex 3)

7.

8.

Basic Savings Account

The basic savings bank account is offered by the commercial banks. Bank branches are limited in the sense that all banks relatively early in their development stages. Most banks have branches available in federal member state main cities in areas in Puntland, Galmudug, Hirshabelle, Southwest and Jubaland. Depending on the population of each member city, branches also vary in size and services offered. The banks also apply slightly different measures for this type of product based on account activities, the quality of identification documents allowed, the transaction limits allowed, and other attributes.

Micro Deposit and Credits

Similar to savings accounts, the volume and transaction sizes are low under microdeposits and the product is mainly accessed by low-income earners. The source of income is usually difficult to determine, as holders of these type accounts lack strong identification, and permanent address information is unavailable. Account holder's deposits and withdrawal amounts are smaller. Without access to the formal financial system, unserved or underserved customers will resort to cash and unregulated channels, which limits transparency and increases the risk of crime and ML¹⁵⁴.

The following are the types of FI accounts offered by Banks and Microfinance institutions:

Table 7: FI Accounts Offered by Banks and Microfinance Institutions

Financial institutions	Type of financial products	Deposits and credits	Limitation
Banks	<ol style="list-style-type: none"> 1. Hajj/umrah saving acct. 2. Maandeeq. Acct. (female) 3. Student saving acct. 4. Marwo saving acct. (female) 5. Youth saving acct. 		Unspecified

¹⁵⁴ <http://www.fatf-gafi.org/publications/fatfgeneral/documents/financial-inclusion-cdd-2017.html>

Microfinance establishments	<ol style="list-style-type: none"> 1. Murabaha 2. Qard-hasan 3. (Credit without charges) 4. Deposits and savings 		Unspecified
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Mobile Banking

The mobile banking product allows customers to carry out transactions using mobile phones. This product is different from internet or online banking as it only requires one to have a phone that is connected to a mobile phone network. The transactions possible with this product include balance inquiry, mini-statement, funds transfer, bill payment, and airtime top up. The product, which is account-based, allows customers the flexibility of transactions and the reduction of costs of accessing bank services, especially those staying in rural and other remote areas.

Local Money Remittance

Local Money Remittance is offered to enable people from various areas to send and receive money. The product brand is based on the US dollar and remittances are offered by:

1. Remittances companies (MTBs)
2. Mobile Network Operators (MNOs)

Recommended actions.

- Financial inclusion is a very important ingredient of any financial system in a country and requires deliberate efforts to promote it. the following steps are recommended to promote financial inclusion:
 - a) A special basic savings account should be established for customers who are disadvantaged. Regulators should advance establishment of this account and attributes or conditions such as transaction limits pertaining to this account should be clearly set and formally communicated to financial sector players in Somalia.
 - b) For preventive measures and proposed customers under simplified identification requirements, transaction threshold amounts should be on the lower side. Account activity should frequently be monitored, for customers to qualify under simplified identification requirements.
 - c) Regulators should develop guidelines for specific financial inclusion products, which will allow them to perform RBA and achieve simplified due diligence for qualifying accounts.
 - d) There is a need for the regulators to provide training to banks to effectively deal with financial inclusion products.
 - e) MFIs currently offering credit and financing for small businesses should set thresholds amounts to avoid being used by potential money launderers.

- f) Financial institutions whose staff members have insufficient knowledge in AML/CFT regulatory should be adequately trained.
- g) Administrative penalties should be in place and implemented, addressing any negligence committed by financial services providers.
- h) To continue to further assess ML/TF risks arising from those types of products, and mitigate them, regulators should develop and implement a legal framework addressing the risk associated with financial inclusions.

Annexes

Annex 1

Commercial Banks

Financial Institution Law 2012, Chapter I, Article 2 “Commercial bank” means any bank in Somalia whose business includes the Acceptance of deposits withdrawable by cheque, issue of short term and medium-term loans, guarantees, foreign exchange transactions and such other activities as the Central Bank may by regulation classify.

Financial Institution Law 2012, CHAPTER II, Article 1 A person who intends to engage in banking business in Somalia must first obtain a license issued by the Central Bank.

Financial Institution Law 2012, CHAPTER III, Article 4 An application for bank license shall be made in writing in the form prescribed by the Central Bank of Somalia. The application must be accompanied by all required supporting information and documents, and the prescribed application fee. Additionally, to that The Central Bank may require any other information from the applicant, shareholders, significant shareholders, directors, officers and/or third parties that it deems necessary to complete its assessment of a bank license application.

Financial Institution Law 2012, CHAPTER II, Section 14 Article 1, 2 and Section 15 (1), Section 16, and Bank Resolution on 31st December 2017 Central Bank of Somalia requires all commercial banks should maintain Minimum Capital Requirements of 7,000,000 in which 1,500,000 deposit at Central Bank of Somalia and maintain all time a Capital Adequacy Ratio which equals or exceeds twelve percent (12%) and a Core Capital Ratio which equals or exceeds eight percent (8%). A liquidity ratio which equals or exceeds twenty (20%) is also required.

Financial Institution Law 2012, CHAPTER 9 Section 67 Article 1, Central Bank of Somalia requires that no person or group of related person’s shareholders of licensed commercial banks direct or indirect owns or controls more 25%.

Money Transfer Businesses (MTBs)

Financial Institution Law 2012, Chapter 1, Article 2 “Money transfer business” or “Hawala” means the acceptance of cash, cheques, and other payment instruments, [also including stored-value products], in one location, and payment [disbursement] of a corresponding sum in cash or other form to a beneficiary in another location.

Financial Institution Law 2012, CHAPTER 7, Article 50 A person shall not carry on or engage in money transfer business without a valid license issued by the Central Bank for that purpose.

Financial Institution Law 2012, CHAPTER 7, Article 50 every relevant person shall apply to the central bank for registration using prescribed form by the Central Bank of Somalia. Upon receipt of an application for registration the licensing and supervision department shall, within fourteen days, review the application and make recommendations, on the application, to a committee of the central bank after ascertaining the formal content and completeness of information and document requirements under Regulation.

Annex 2

Mobile Money Services

Mobile Money regulation, Part I, Article 3 “mobile money service” means a payment service delivered in electronic form by a mobile money service provider in accordance with the Mobile Money regulation Regulations. Mobile Money regulation, Part II, Articles 6 (1) every relevant person shall apply to the central bank for License using the First Schedule to the Mobile Money Regulations. Mobile Money regulation, Chapter 2 Articles 7 (1 and 4) the Central Bank shall consider a renewal application within ninety days and may renew or decline to renew a license for reasons stated. In addition to that, a license granted under the Mobile Money Regulation shall be valid for two years and may be renewable biennially; provided that a license granted during calendar year shall be valid up to 31st December of the end of the second year.

Annex 3

Gargaara Company Ltd

Currently, the Gargaara Company Ltd offers its products through the existing Somali commercial banks where parties share the proceeds of the loan income. However, based on surveys taken with the commercial banks, and limited qualifying loan applicants available in the market, the commercial banks rarely promote Gargaara’s products for customers seeking small business loans, but they sell their own products. Additionally, there are no clear differences in benefits or flexibility between the two products. Benefits such as attractive loan term and flexibility factors such as qualifying first time business owners and longer, more flexible payments terms could have been better ways to promote credit loans and financial inclusion. Commercial banks currently authorized to offer Gargaara’s products should also inform a potential small business borrower of the existence of the Gargaara products, specifically loan offerings available for customers seeking short and medium-term loan arrangements. Commercial banks should also post the loan offerings available on their banks.

Action plan and timelines

In process to be completed.