

**AML/CFT Regulation and Supervision of Financial  
Institutions  
in the Republic of Tajikistan**

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September, 2022

Master's Thesis Presented to Ritsumeikan Asia Pacific University  
in Partial Fulfillment of the Requirements for the Degree of  
Master of Science in International Cooperation Policy

## TABLE OF CONTENTS

CERTIFICATION PAGE.....	4
ACKNOWLEDGEMENTS .....	5
ABSTRACT.....	7
LIST OF TABLES .....	9
LIST OF FIGURES .....	10
LIST OF ABBREVIATIONS .....	11
CHAPTER 1: INTRODUCTION .....	13
1.1 Research Background.....	13
1.2. Research Objectives, Questions and Hypothesis.....	16
1.3. The Significance of the Study.....	17
1.4. Limitations and potential problems.....	18
1.5. Research Outline.....	19
CHAPTER 2: LITERATURE REVIEW.....	20
2.1. Money laundering .....	20
2.2. Terrorism Financing.....	23
2.3. FATF Standards .....	26
2.4. AML/CFT Mutual Evaluations.....	30
2.5. Mutual Evaluations of the Republic of Tajikistan.....	31

2.6. Summary.....	35
<b>CHAPTER 3: METHODOLOGY.....</b>	<b>37</b>
3.1. Research Context .....	37
3.2. Research Methods.....	38
3.3 Data Collection and Analysis.....	39
3.3.1 Analysis of the Primary Data .....	39
3.3.2 Analysis of the Secondary Data.....	41
3.4. Limitation and Ethical considerations.....	42
<b>CHAPTER 4. IMPLEMENTATION OF THE SUPERVISION</b>	
<b>RECOMMENDATIONS IN THE EAG COUNTRIES .....</b>	<b>45</b>
4.1. Rating Level of the implementation of Recommendations and underlying factors.....	45
4.2. Implementation of RBA requirements in Tajikistan, Belarus, the Kyrgyz Republic, China and Russia.....	54
4.2.1. Countries with minor shortcomings: Republic of Belarus and Russian Federation.....	54
4.2.2. Countries with moderate and low shortcomings.....	57
4.3. The power of supervisory authorities to impose sanctions for violation of AML/CFT legislations in FIs.....	60
4.3.1 Compliance in the Republic of Belarus.....	60
4.3.2 Compliance in the Russian Federation.....	65

4.3.3 Compliance in the Kyrgyz Republic.....	67
4.3.4 The case of China.....	68
4.3.5 The Republic of Tajikistan.....	70
4.4. Summary and observations.....	71
CHAPTER 5: THE LEVEL OF COMPLIANCE OF SUPERVISORY RECOMMENDATION IN THE REPUBLIC OF TAJIKISTAN .....	73
5.1. Supervision and Regulation of FI's in the Republic of Tajikistan.....	73
5.2. Limited Work Experience of FIU staff.....	76
5.3. Challenges in Conducting Audits in FI's Especially using RBA Requirements.....	78
5.4. Sanctions.....	83
CHAPTER 6. CONCLUSION AND RECOMMENDATION .....	88
6.1. Conclusions on the research objectives.....	88
6.2. Conclusions on the hypotheses.....	90
6.3. Recommendations .....	91
6.4. Suggested directions for future research .....	93
LIST OF REFERENCES .....	95
APPENDIXES.....	99

## **CERTIFICATION PAGE**

I, DZHURAEVA ZEBO KOMRONOVNA (Student ID 51220632) hereby declare that the contents of this Master's Thesis/Research Report are original and true, and have not been submitted to any other university or educational institution for the award of degree or diploma. All the information derived from other published and unpublished sources has been cited and acknowledged appropriately.

Dzhuraeva Zebo Komronovna

June 10, 2022

## ACKNOWLEDGEMENTS

I would like to mention that it was impossible to complete this research without the support and help of many individuals and organizations and I would like to express my gratitude and sincere thanks to them here.

Firstly, I would like to thank the Government of Japan through the Japan International Cooperation Organization (JICA) and Japan International Cooperation Center (JICE) for their kindness and support to the young generation who are seeking knowledge and want to contribute to future generations and society by improving themselves. Also, I would like to thank the Government of the Republic of Tajikistan and the National Bank of Tajikistan for supporting me and my candidacy in this scholarship.

Secondly, I would like to mention the efforts of the two professors of Ritsumeikan Asia Pacific University who become the part of my family, my dearest supervisor, Otsuka Kozo, and my Academic English professor, Blackwell James. I was able to complete this study thanks to their continuous support, motivation, advice, enthusiasm, encouragement and extraordinary patience. Moreover, thanks to their guidance I could improve my research skills. From working with them I learned that no matter where you are and who you are the most important thing is that you love and respect the profession you choose. Then you can encourage and even give wings to those who want to fly up into the sky of knowledge.

A special word also and my deepest thanks to my dearest mother, to the person who became for me not only my mom but my father and my best friend, for inspiring me and being with me in whatever I pursue. Also, I want to thank my

beloved brother, mother-in-law and father-in-law whose love and prayers are with me every time.

Most importantly, I wish to pass my deep appreciation and thank to my beloved husband - Mirzoburhon and my little guardian angel Sumaya for supporting me mentally and believing in me and my achievements.

Finally, I would like to dedicate this achievement to the soul of my beloved father, whose memory has sustained me through the hardships of my life. I hope he would have been very proud of me.

## **ABSTRACT**

This study explores the progress made by the Republic of Tajikistan in developing systems to combat money laundering and the financing of terrorism (AML/CFT systems). As relatively little research exists in this area, an important motivation for this study was to examine developments with the AML/CFT system in Tajikistan, with a particular emphasis on the regulation and supervision of financial institutions in the field of AML/CFT and the powers and responsibilities of AML/CFT supervisory authorities.

To this end, this study employed qualitative methods, principally a questionnaire and interviews, to collect data on the current state of AML/CFT efforts in Tajikistan. Questionnaires were delivered to specific organizations and individuals in charge of AML/CFT regulations in the Republic of Tajikistan and were followed up with interviews as the primary sources of data for this research. Additionally, various secondary sources were consulted to conduct a comparative analysis of the level of implementation of supervisory recommendations among 5 EAG countries (including the Republic of Tajikistan, the Republic of Belarus, the Kyrgyz Republic, the Peoples Republic of China and the Russian Federation).

In terms of the findings, this study will show that, although the Republic of Tajikistan passed the 2nd round of AML/CFT mutual evaluations in 2018, gaps and omissions are still observable in the country's AML/CFT system (MER RT, 2018). It will propose that such gaps need to be addressed to develop an AML/CFT system for financial institutions to conform to recommendations effectively and to ensure the security of the country's economy. As a positive outcome, this study will show



that Tajikistan is making progress with its efforts to establish risk-based supervision of financial institutions by adopting special instructions and establishing these requirements in legislation. At the same time, however, it will show that more work needs to be undertaken in the practical implementation of these measures, meaning that that the risk-based supervision in financial institutions is not well-established yet.

## LIST OF TABLES

Table 1. Types of FIs and DNFBs with their Supervisory authorities in the Republic of Tajikistan;	34
Table 2. The level of implementation of Supervisory Recommendations in EAG countries according to the MER of each country;	41
Table 3. Abbreviation and Definition of Table 2;	42
Table 4. Schedule of EAG mutual evaluation;	46
Table 5. The Rating Levels of Recommendations in Tajikistan, Belarus, Kyrgyz Republic, China and Russia based on their MERs;	47
Table 6. Definitions for used abbreviations in Table 5;	47
Table 7. The results of MER related to Recommendations 26,27,28 and 35 in the five EAG countries;	49
Table 8. Number of FIs controlled by NBRB in each risk category (The given Table adapted from MER of the Republic of Belarus, 2019, p. 113);	55
Table 9. Risk classifications of financial institutions (Table adopted from MER of Russian Federation, 2019);	57
Table 10. NBRB applied sanctions to identified violations in the Banking Sector (Table adapted from the MER of the Republic of Belarus, 2019, pp. 122-123);	61
Table 11. NBRB applied sanctions to identified violations in non-credit financial institutions sector (Table adapted from the MER of the Republic of Belarus, 2019, p. 125);	63
Table 12. Sanctions applied to identified violations in gambling organizations (Adapted from the MER of the Republic of Belarus, 2019, pp. 127-128);	64
Table 13. AML/CFT sanctions against credit institutions (Adapted from the MER of the Russian Federation, 2019, p. 177);	65
Table 14. AML/CFT sanctions against non-credit institutions (Adapted from the MER of the Russian Federation, 2019, p. 177);	66
Table 15. AML/CFT sanctions against real estate agents and DPMS (Adapted from MER of the Russian Federation, 2019, p. 181);	66
Table 16. AML/CFT sanctions against financial institutions (Adapted from MER of the Kyrgyz Republic, 2018, pp. 101-102);	68
Table 17. Number of penalties applied by the PBC (Adapted from MER of the China, 2019, p. 134);	69
Table 18. AML/CFT audits conducted on FIs during the period 2010-2020 (Republic of Tajikistan);	74
Table 19. The results of MER related to sanctions (adapted from the Mutual Evaluation Report of the Republic of Tajikistan, 2018.)	84
Table 20. Sanctions applied to identified violations in financial institutions of the Republic of Tajikistan.	86

## LIST OF FIGURES

Figure 1. Respondents Work Experience	77
Figure 2. Figure 2. Challenges that supervisors and regulators while conducting audits of FIs	79

## LIST OF ABBREVIATIONS

AML-Anti-Money Laundering;

AML/CFT-Anti-Money Laundering and Countering the Financing of Terrorism;

BoR - Bank of Russia;

CoAO - Code of Administrative Offences of the Republic of Belarus;

DNFBPs-Designated Non-Financial Businesses and Professions;

EAG - Eurasian Group on combating money laundering and financing of terrorism;

ESAAMLG-Eastern and South Africa Anti-Money Laundering Group;

EU – European Union;

FATF-Financial Action Task Force;

FDI – Foreign Direct Investment;

FIs-Financial Institutions;

FIU-Financial Intelligence Unit;

FMD – Financial Monitoring Department under the National Bank of Tajikistan;

FSRB-FATF Style Regional Body;

FT-Financing of Terrorism;

GDP – Gross Domestic Product;

ICRG-International Co-operation Review Group;

IMF-International Monetary Fund;

KR – Kyrgyz Republic;

ML-Money Laundering;

ME – Mutual Evaluation;

MER – Mutual Evaluation Report;

NBT – National Bank of Tajikistan;

NBRB - National Bank of the Republic of Belarus;

NRA-National Risk Assessment;

PBC – People’s Republic of China;

RBA-Risk-Based Approach;

RT – Republic of Tajikistan;

TF-Terrorism Financing;

UK – United Kingdom;

UN-United Nations;

UNSCR - United Nations Security Council Resolution;

USA – United State of America;

WB – World Bank;

## **CHAPTER 1. INTRODUCTION**

The purpose of this research is to analyze the regulation and supervision of financial institutions of the Republic of Tajikistan with the application of AML/CFT (anti-money laundering and combatting the financing of terrorism) recommendations. More specifically this research aims to explore the implementation and impact of the FATF Recommendations, especially Recommendations 26 (Regulation and supervision of financial institutes), 27 (Powers of supervision), 28 (Regulation and supervision of DNFBPs) and 29 (Financial Intelligence Unit) during two rounds of AML/CFT Mutual Evaluations of the Republic of Tajikistan.

With these considerations in mind, this research will employ the following methods to examine the efforts undertaken by the government of Tajikistan so far:

1. An analysis of the theoretical basis of AML/CFT issues;
2. A comprehensive verification of 2 rounds of the AML/CFT Mutual Evaluation in the Republic of Tajikistan (ME of RT);
3. A series of interviews in order to understand the analytical framework behind the issues.

### **1.1. Research Background**

These days money laundering and terrorism financing have become serious issues worldwide. The term “money laundering” started to rise to prominence in the early nineties, and due to an increase in this threat in 1989, G7 member countries decided to create a unique body to combat ML and related offenses (Pieth & Aiolfi,

2004). This organization is known as the Financial Action Task Force (herein, FATF). Nowadays FATF is one of the main rule-making bodies to combat money laundering and terrorist financing threats. From 2005, according to the United Nations Security Council Resolution (UNSCR) 1617, FATF developed recommendations that became recognized as international standards in the field of AML/CFT. Almost 200 regions introduced the FATF standards into their national legislation and endorsed them as international standards for AML/CFT (Hopton, 2009).

For the Republic of Tajikistan, financial monitoring is a new phenomenon which arose in connection with the setting-up of a system of combating money laundering and terrorist financing. During the 11 years of its existence, the Tajik system of financial monitoring developed and improved. The special and significant role of financial monitoring can be seen in the development of the AML/CFT system, the successful passing of mutual evaluations of AML/CFT, and the improvement of the country's economic security.

In 2007 and 2018, the Eurasian Group on Combating Money Laundering and Financing of Terrorism (EAG) which is a FATF-style regional body, conducted a mutual evaluation of Tajikistan in accordance with the procedures of FATF standards. The objective of the mutual evaluation was to evaluate the implementation of the FATF 40 Recommendations in the Republic of Tajikistan and to issue the detailed report of the findings by the end of evaluation (ME of RT, 2018).

The mutual evaluations show the level of each country's compliance with AML/CFT International Standards including the regulation and supervision of

financial institutions, the powers and responsibilities of AML/CFT competent authorities, and the level of the country's economic security. If a country is recognized as being non-compliant with FATF Standards, then it may fall on other countries and the International Financial Institutes to enforce the standards and support their establishment in national legislation. Also, countries can face other pressure such as suspension from the FATF or the FSRB's until they comply with international AML/CFT requirements. In this case, the economy of the country will be classified as not safe and not secure for cooperation and investment (Regulation of the EAG, 2009).

Considering the points mentioned above, this research analyzes the Mutual Evaluation Report (MER) of the Republic of Tajikistan conducted by the EAG in 2018 and provides a comparative analysis of the MERs of the five EAG countries with the aim of examining the extent to which Tajikistan has succeeded in implementing the recommendations contained in the MER, specifically Recommendations 26 (Regulation and supervision of financial institutes), 27 (Powers of supervision), 28 (Regulation and supervision of DNFBPs), 35 (Sanctions).

The primary methodological framework employed for this purpose is qualitative and the following points were considered when developing the specific methodology for this study:

- I. Firstly, this research is aimed at gaining a deeper understanding of the AML/CFT system of the Republic of Tajikistan;



- II. Secondly, it aims to provide an explicit rendering of the FATF Standards, especially Supervision Recommendations among the individuals in charge of the AML/CFT regulations;
- III. Thirdly, it aims to explore how the participants understand the meaning of the FATF Standards, and how these meanings influence the process of Mutual Evaluations;
- IV. Fourthly, this research uses observation (in the form of a structured questionnaire) as the primary method of data collection. This type of research instrument is useful for generating in-depth descriptions of the implementation of AML/CFT regulations and the supervision of financial institutions in the Republic of Tajikistan to obtain information that may otherwise be inaccessible, and for conducting research when no other suitable methods are available.
- V. Finally, this study can be considered descriptive in nature, as it analyzes the procedures, participants and characteristics of AML/CFT regulations. This is in line with descriptive approaches employed in other studies of economic conditions which require a responsive and flexible approach (see for example, Creswell, 1994).

## **1.2. Research Objectives, Questions and Hypothesis**

The main objective of this study is to determine the level of AML/CFT supervision in The Republic of Tajikistan in accordance with the ML/TF risk-based approach by investigating how FATF Recommendations are implemented by competent authorities at the time of regulation of financial institutions.

The secondary objective of the study is to examine the regulation and supervision of financial institutions in the AML/CFT area and explain why this concept became important during the two rounds of AML/CFT Mutual Evaluations in the country.

In order to realize the objectives of this study, the following research questions will be proposed:

1. To what extent is the mechanism of risk-based supervision for financial institutions established in The Republic of Tajikistan?
2. In what ways are the supervisors in Tajikistan intensifying their work with imposing sanctions for violations of AML/CFT legislation?
3. To what extent is Tajikistan's AML/CFT legislative and institutional capacity effective in regulating and supervising financial institutions?

In addition to the above objectives this research aims to test the following hypotheses:

- I. The mechanism of risk-based supervision is not established in the Republic of Tajikistan.
- II. The supervisory authorities lack power to apply sanctions for violation of AML/CFT legislation and they imposed sanctions only on credit and micro deposit organizations.

### **1.3. The Significance of the Study**

The purpose of establishing the FATF was to implement the Vienna Convention program which calls for countries to combat illicit incomes from drug traffic and related offenses. Accordingly, it was important for the FATF to develop

the International Standards to combat ML threats which can be implemented by member states and later, by all countries.

One of the main tasks of the FATF is to perform mutual evaluations on member states with the aim of examining the level of the national legislation and current practices in the sphere of combating or preventing money laundering and terrorist financing based on the FATF recommendations. In 2018, The Republic of Tajikistan passed the 2nd round of AML / CFT mutual evaluations. However, in the country's AML / CFT system, gaps and omissions are still visible (MER RT, 2018). These gaps need to be addressed to improve the AML/CFT system for financial institutions so that they can conform to recommendations at a high level and ensure the security of the country's economy.

The significance of this work rests on the fact that there is no scholarly literature on the Republic of Tajikistan's AML/CFT system, especially with regard to regulation and supervision of financial institutions in the field of AML/CFT and the powers and responsibilities of authorities who oversee AML/CFT. This study evaluates the national AML/CFT legislation and MERs in Tajikistan and identifies the obstacles to an effective AML/CFT regime for improving the AML/CFT system of financial institutions to ensure the economic security of the country.

#### **1.4. Limitations and potential problems**

The main limitation of this study is the lack of previous research on the topic. For instance, there is almost no research on AML/CFT regulation and supervision of financial institutions, the MER for Tajikistan or the AML/CFT system in Tajikistan. Secondly, there are limits imposed by the security of some

information. Additionally, the researcher needed to obtain permission to use a large amount of material and data from the EAG Secretariat and FIU of Tajikistan, meaning that there are some restrictions and limitations on access to data. Furthermore, there were some delays in data collection due to the need to obtain permission to conduct the research. Moreover, due to the impact of COVID 19, the author experienced difficulties with conducting field trips and interviews. These issues were carefully considered as the research proceeded in order to minimize their impact on the completion of this project.

### **1.5. Research Outline**

This study is divided into five main chapters following the introduction (Chapter 1). In Chapter 2, the key terms and concepts that form the subject of this research are reviewed, and in Chapter 3, the research context, methodological procedures, collection of data and methods of analysis employed in this study are described. This is followed by the research findings, including in Chapter 4, a comparative analysis of five EAG countries (The Republic of Tajikistan, The Kyrgyz Republic, The People's Republic of China, The Republic of Belarus and The Russian Federation) and Chapter 5, an analysis of the interviews and transcripts that form the primary source of data for this study. Chapter 6 presents the conclusion of the study and offers specific recommendations related to the findings and suggestion for further research in this field.

## CHAPTER 2: LITERATURE REVIEW

This section reviews the key terms and concepts that are the subject of this research. At first, it looks at definitions of money laundering and financing of terrorism and then explores the operation of FAFT, ME and finally, it presents some options for the methodological framework outlined in the following section (Chapter 3).

This study is based on a number of sources, primarily Cox's (2014) work on money laundering, Parkman and Peeling's (2007) AML/CFT handbook for financial services, Pieth and Aiolfi's (2004) analysis of AML/CFT system in Singapore, Switzerland, the United Kingdom. and the United States of America, Zubkov and Osipov's (2008) work on the Russian Federation in the International Framework of Combating Legalization (Laundering) of Criminal Proceeds and Financing of Terrorism etc. and related documents from the FATF website. Additionally, Mutual Evaluation Reports on AML/CFT systems in the Republic of Tajikistan, and the RT's national risk assessment report of AML/CFT regime, will also be presented.

### **2.1. Money laundering**

*Money laundering and financing of terrorism* have become major issues for world leaders in recent times. The term money laundering (herein "ML") came to the fore in the early 1990s and has various definitions. The primary meaning of this term is the "process of turning illegally gained money into legal and lawful money with the purposes to disguise the original source of criminal or illegal money and

to eliminate the trail and flow of illicit money” (Vienna Convention, 1988). According to Zubkov and Osipov (2008) According to Zubkov and Osipov (2008), the ML reference is affiliated with one of the American criminals Al Capone and his business activities. The main reason was that Capone was generated illegal income from alcohol trading, and due to make them legitimate comingled them with his incomes from the laundromat business. In contrast, Robinson (2004) argues that this is just a story and predicates that the ML concept originated from the process of legitimate the "dirty" (illegal) incomes via mixing them with legal funds.

According to the United Nations (UN) 2000 Convention (UNODC, 2004), money laundering is the process of legitimizing criminal funds through transferring and mixing them with the incomes from the legal business, with the understanding that they are illegal incomes. The main goal of this action is to dissimulate the originality of the illegally generated income with the aim of integrating it into the legal financial system without highlighting law enforcement and tax agencies (Compin, 2008).

According to Buchanan (2004, p. 117) the money laundering process can be described in three phases or steps: placement, layering, and integration. Each step is outlined briefly below.

Firstly, Placement. In this step illegal income enters the financial system through deposits with the aim of disguising the origin from authorities. This can be done through shell corporations by purchasing checks or making money orders.

Secondly, after the funds have entered the financial system, the layering step is carried out. In this case, launderers try to find legitimate methods to move money, such as creating a network of financial transactions that often resemble legitimate

financial transactions in frequency, complexity and volume. Criminals can also disguise transfers as payments for goods or services to make them appear legitimate. Here offshore financial centers fulfill an important function.

The final stage is integration when funds go into the non-shadow economy. Various financial instruments are used to achieve this goal, namely letters of credit, bonds, banknotes, bills of lading, and guarantees.

In 1998, during the FATF plenary meeting in Paris, the then Director of the International Monetary Fund highlighted the issue of money laundering and noted that the amount of money laundered was estimated at two to five percent of global gross domestic product (GDP) (Camdessus, 1998). In this regard, it is possible to observe the connection between money laundering and the economy or, stated differently, the effects of money laundering on the economy and its security.

A number of scholars have investigated the effect of money laundering on economic and financial systems around the world. For instance, Picard and Pieretti (2011) examined the implementation of AML regulations on offshore financial centers. Their observation shows that pressure policies such as blacklisting and sanctions can be the contributory cause for offshore banks to apply AML regulations. In other words, the pressure policies can be harmful for an offshore financial center's reputation and their investors.

The issue of money-launderers was central to Malm and Bichler's (2013, pp.365-368) study on this subject. After carrying out the research they found that the money laundering drug market is bigger than other illegal markets. Also, their investigation shows that there are three types of money-launderers:

1. Professionals - often criminals can hire financial experts such as accountants or real estate agents with the aim of laundering their illegal incomes;

2. Opportunistic laundering - the person who works for someone they know (relatives, friends, someone from the same trade network).

3. Self-laundering - criminals who clean their own incomes.

In 1988 The United Nations adopted the first steps to target the threat in this field, otherwise known as the Convention against Illicit Traffic in Narcotic Drugs and Psychotropic Substances or the Vienna Drug Convention. The second global response occurred in 1989 when FATF was established, and laundering money was designated as an offense. Following these initial efforts, several steps were taken over subsequent years to combat money laundering, especially in relation to international terrorism and its financing. These steps will be outlined in the following sections.

## **2.2. Terrorism and Terrorism Financing**

After the 9/11 attacks, the world started to learn the details of terrorism and terrorist financing and it became the main issue for debate during international organizations' plenaries. The first discussions in the UN began concerning the adoption of terrorism and terrorism financing definitions. In July 2005, under the leadership of UN Secretary-General Kofi Annan, a universal definition of terrorism was adopted (Nasser-Eddine, Garnham, Agostino, & Caluya, 2011).

In addition, according to Ozhegov (1983 p. 1066), the term terrorism is derived from the Latin word "terror" which means "intimidating of political opponents, expressed in physical violence, up to their destruction".



In the present context, the legislative definition of terrorism used by the Tajikistan government is outlined in Article 3 of Law of the Republic of Tajikistan "About the fight against terrorism" (1999). For the purposes of this study, the definition is included in full, as follows:

Terrorism, that is violence or threat of its application concerning physical persons, coercion or threat of its application concerning legal entities, and also destruction (damage) or the threat of destruction (damage) of property or other material objects of physical persons or legal entities creating the danger of death of people, causing significant property damage or approach of other socially dangerous effects performed for the purpose of violation of public safety, intimidation of the population or rendering impact on adoption of the decisions by authorities profitable to terrorists or satisfaction of their illegal valuable and (or) other interests; and also infringement of life of the state or public figure for the purpose of weakening of bases of the constitutional system and safety of the state, and is equal for the purpose of the termination of the state activities or other political activities or is made as revenge for these activities; and also attempt at life, the causing bodily harm to the state or public figure or the public agent made in connection with their state or public work for the purpose of destabilization of situation or impact on decision making by state bodies or hindrance of political or public work; and also attack on the representative of the foreign state or the employee of the international organization using international protection or the family members living with it,

and is equal on office either premises or vehicles of persons using international protection if these actions are made for the purpose of provocation of war or complication of the international relations.

Terrorists' character or psychology and the question of why terrorists commit these acts is another issue of investigation. For instance, Thackrah (2004) noted that terrorists are emotionally unstable and for most of them it is impossible to be in a relationship with their own identity which causes them to choose violence. Moreover, Feeney (2002) suggests that the third-party effect directs terrorists, and they act under a type of hypnosis. However, Ibrahim (1980) and Sageman (2011) in their study on this subject found that terrorists were normal and well-educated young people and there is no evidence of them suffering from mental illness.

It should also be mentioned that terrorism is a worldwide threat and the task of the each nation is to combat this threat. However, in order to degrade terrorist activities, it is necessary to keep in mind that the main component of terrorism is money. As Madinger (2012) points out, terrorists and terrorism require funding because their attacks are their major expenses, since they need weapons and need to maintain them. Leonard & Kaunert (2012) observed that, in order to conduct attacks, terrorists do not need large amounts of money, but they need money for their security, for instance to create false identification documents. Also, propaganda and training newborn terrorists in special camps, including their grooming, can be costly for terrorists. Moreover, in contrast to money launderers, terrorist financiers can have legal and illegal incomes (FATF, 2008; FATF, 2018).

The term *terrorist financing* is the act of financing or sponsoring to individual terrorists or terrorist groups involved in terrorist engagements and activities. Freeman's (2011, p 463-465) theory of terrorist financing consider that terrorist raising the funds in accordance to the six criteria: quantity, legitimacy, security, reliability, control, and simplicity. Moreover, these criteria propose that terrorist also wants to increase their funds and resources (Freeman, 2011). Therefore, to prevent terrorism, governments need to combat terrorism financing. According to the FATF Special Recommendation II, countries must criminalize the financing of terrorism, terrorist acts and terrorist organizations, in accordance with Article 2 of the Convention against Financing of Terrorism, and make sure that such offenses are designated as money laundering offenses (FATF Recommendations 2012).

### **2.3. FATF Standards**

The *Financial Action Task Force on Money Laundering* (or FAFT), an intergovernmental policy-making-body, was created during the 1989 summit in Paris by G7 member countries which included the leaders of the United States, United Kingdom, France, Japan, Germany, Italy and Canada, as well as the President of the European Commission (FATF, 1991).

According to Pieth and Aiolfi (2004), in 1988 during the G7 summit in Harrisburg the President of the USA came up with the idea of establishing a task force to deal with ML threats. However, France objected to this proposal. In 1989 during the next G7 summit France made the same proposal and it was approved by member countries (Pieth and Aiolfi, 2004). Accordingly, FATF was formed with

the aim of facing off against drug problems which demanded urgent action with a one-year mandate.

The FATF proposed a comprehensive framework in 1990 for countries around the world to deploy in developing their own measures against ML. This covers the criminal system and its regulation, and international cooperation. The framework just outlined is based on the Vienna Convention (1988), the Palermo Convention, and the Statement of Principles for the bank supervisors, which was issued on 12 December 1988 by the Basel Committee on Banking Supervision. These principles are recognized as cornerstones and are referred to as the Forty Recommendations on Money Laundering (FATF, 1991). The main objective of the 1990 Forty Recommendations was to establish policies at national and international levels with the aim of combatting money laundering, especially in view of drug trafficking and other organized crime activities. In the beginning, none of the Recommendations were terrorist specific. (Pieth & Aiolfi, 2004).

As Pieth and Aiolfi (2004) noted, due to the achievement of satisfactory results FATF members suggested that the recommendations be revised periodically to deal with emerging threats. In this regard, after the 9/11 terrorist attacks in the USA in October 2001, FATF enhanced its mandate to combat terrorism financing and created Special Recommendations on Terrorist Financing. In 2012, the Recommendations were overhauled, and the 40 Recommendations were applied to deal with new threats, including, among others, the financing and proliferation of weapons of mass destruction (FATF, 2021).

FATF was established with a number of objectives to achieve outcomes in combating related threats. The FATF needs to set AML/CFT international standards

and encourage effective implementation of legal and regulatory levels in the international financial system (FATF, 2021). Moreover, with the aim of implementing the objectives according to its mandate, FATF (2021) monitors' implementation and the progress of the Recommendations through mutual evaluation of member jurisdictions. In addition, in accordance with UNSCR 1617, all member countries are required to implement the comprehensive international standards listed in the 40 AML/CFT Recommendations (Ryder, 2012).

In 2019 FATF celebrated its 30th anniversary. Due to their achievements, FATF's membership grew from the 16 members (1989) to the current 38 members and nine FATF-style regional bodies (FSRB). Additionally, during this time, 205 countries became part of the FATF Global Network (FATF, 2019).

FATF and nine FSRBs, which are officially recognized as FATF Associate Members, are independent organizations. In its early stages the FSRBs assessed implementation of the FATF recommendations in accordance with their own procedures but in 2004 they agreed to evaluate their member countries based on the FATF methodology and became a mediator between FATF and its own members. Together they became known as the FATF Global Network (FATF, 2019).

In order to comply with FATF Recommendations countries need to concentrate their efforts in the following areas (see Gilmore, 2004):

1. Improvements to national legal systems;
2. Enhancement of the role of the financial system; and
3. Strengthening of international cooperation.

Verdugo Yepes in his (2011) study of "Compliance with the AML/CFT International Standard: Lessons from a Cross-Country Analysis" which assess 161 countries and their compliance with AML/CFT standards from 2004 to 2011, remarked that weaknesses or shortcomings in one of these areas may impair effective implementation of FATF standards in general. Therefore, it is important for countries to address all three of the above elements in their efforts to comply with the FAFT.

Mark Pieth and Gemma Aiolfi in their (2004) study of "A comparative guide to anti-money laundering: a critical analysis of systems in Singapore, Switzerland, the UK and the USA" conducted an empirical analysis of the implementation of FATF standards in 4 jurisdictions. The results of their research show that the US and the UK created reliable AML/CFT regimes. However, these jurisdictions also fell short on their compliance with AML/CFT legislation. Thus, as mentioned above, it is important for countries to improve their national legal systems too.

Additionally, a country's compliance with FATF standards directly influences foreign direct investment (FDI). In this regard, Nkrumah (2019) conducted a comparative study of the efforts to implement FATF Standards in 74 FATF member countries. This included data on FDI net inflows during the period 2004 to 2016. Based on his analysis he noted that "AML/CFT compliance is actually a significant driver of Foreign Direct Investment" (Nkrumah, 2019). This conclusion support the position that a country's FDI and its economic security depends on its compliance with FATF Standards. Moreover, international financial institutions are the members of the FATF and their financial support of jurisdictions is influenced by the results of a country's MER. The importance of MERs will be discussed further in the next section.

## **2.4. AML/CFT Mutual Evaluations**

As regular assessment of progress is the most effective mechanism of any system, one of the main goals of FATF is to perform mutual evaluations to assess the implementation of the 40 Recommendations by member countries. In this regard, Gesase (2013) in his study of the AML/CFT Mutual Evaluation of Tanzania proposed that there should be a mechanism for securing implementation of FATF Standards by each state. This mechanism is known as a mutual evaluation exercise, which is performed in accordance with a standard methodology published by the FATF. Moreover, Gesase reported that, after joining the ESAAMLG (a FAFT-styled Regional Body), Tanzania recognized the importance of mutual evaluations and the necessity of international cooperation in combating ML/FT (Gesase, 2013).

In accordance with the FATF, a team of five to six expert assessors (consisting of at least one legal, one financial, and one law enforcement expert) and up to two members of the FATF Secretariat will evaluate the compliance of a country with the FATF Standards. In the process of evaluation, experts will follow the FATF Recommendations and Interpretative Notes and the prescribed Methodology (FATF Universal Procedures, 2021).

Moreover, every FATF and FSRBs member jurisdiction will be evaluated using two types of assessment: 1) a technical compliance assessment and 2) an effectiveness assessment. The technical compliance assessment considers the specific requirements of the FATF Recommendations, as they relate to the relevant legal and institutional framework of the country, as well as the powers and procedures of the competent authorities. These assessments represent the fundamental “building blocks” of the AML/CFT system (FATF Methodology,

2013 - 2020). The effectiveness assessment, on the other hand, differs considerably from the technical compliance assessment. It aims to evaluate the level of implementation of the FATF Recommendations and typically identifies the extent to which a country achieves a prescribed set of outcomes that are at the core of a strong AML/CFT system. Thus, the focus of the effectiveness assessment is concerned with the extent to which the legal and institutional frameworks produce the expected results (FATF Methodology, 2013 - 2020).

By the end of a mutual evaluation, assessors are required to prepare a report (herein a "MER"), and after review in the FATF plenary meeting, this report will be published. If a country is determined to be non-compliant in any aspects of the evaluation, then it will be subject to pressure from other countries to correct the problem. (FATF Universal Procedures, 2021). Also, a country can be required to adhere to rigorous compliance procedures, which could include, at the most serious level, being added to a list of Non-Cooperating Countries and Territories (NCCT) until it complies with FATF requirements (FATF Universal Procedures, 2021).

In such cases, the economy of the country will be categorized as unsafe and not secure for cooperation and investment. Moreover, mutual evaluation results are one of the key instruments referenced by the World Bank and the IMF when extending loans and grants to countries (Alexander, Dhumale, & Eatwell, 2005). Generally, developing countries use the service of these institutions and therefore face more pressure from them due to the implementation of FATF Standards.

## **2.5. Mutual Evaluations of the Republic of Tajikistan**

Considering the above, an important objective in the present study is to investigate the implementation and effects of the FATF Recommendations in



pursuit of AML/CFT objectives in the Republic of Tajikistan. To date, however, there is no scholarly literature on the AML/CFT regime implemented by the Republic of Tajikistan. However, the results of the AML/CFT mutual evaluation of the Republic of Tajikistan are published on the EAG and the FATF websites as part of the Mutual Evaluation Report of Tajikistan (MER of RT, 2018). Therefore, and with the permission of the EAG, these reports will be used as secondary data in this research.

The first round of the AML/CFT mutual evaluation of the Republic of Tajikistan was conducted in 2008 by experts from the World Bank. By the end of the evaluation, and as reported in the MER, experts identified the lack of an AML/CFT legal framework in Tajikistan (MER of RT, 2018). Moreover, Tajikistan was put in an enhanced EAG follow-up process and became a subject of FATFs International Cooperation Review Group (ICRG) process (MER of RT, 2018).

Countries are referred to the ICRG if, according to the mutual evaluation report (MER), a majority of Recommendations are rated as non-compliant. This means the country is under increased monitoring and is placed on a "grey list".

In 2014, after making progress and resolving gaps in the AML/CFT legal framework, Tajikistan was removed from these lists and processes. Additionally, in 2018, the EAG conducted the second round of the mutual evaluation of Tajikistan in line with the procedures set out in the FATF standards (MER of RT, 2018). According to the report prepared by the assessors, Tajikistan was rated “non-compliant” and “partly compliant” in twelve of the Recommendations and was evaluated as having a low to moderate level of effectiveness in attaining eight of the Immediate Outcomes. Due to this outcome, the Republic of Tajikistan is now

working under an enhanced follow-up process (Tajikistan Second enhanced follow-up report, 2021). This process is summarized as follows in the FAFT:

Following the discussion and adoption of a MER, the country could be placed in either regular or enhanced follow-up. Regular follow-up is the default monitoring mechanism for all countries. Enhanced follow-up is based on the FATF's traditional policy that deals with members with significant deficiencies (for technical compliance or effectiveness) in their AML/CFT systems, and involves a more intensive process of follow-up (Procedures for the FATF 4<sup>th</sup> AML/CFT Mutual Evaluations, 2021).

In this regard, it should be noted that in 2007, during the first round of the Mutual Evaluation, the AML/CFT legislation of Tajikistan was non-compliant with the FATF Standards as there was no AML/CFT Law and no FIU. However, the Republic of Tajikistan made a great deal of effort to implement the FATF Recommendations over an 11-year period (until the 2nd round of Mutual Evaluation in 2018) and improved its AML/CFT system. According to the second round of the MER (in 2018) weaknesses and gaps still exist which must be resolved.

As mentioned above the AML/CFT system of the Republic of Tajikistan was first evaluated by World Bank experts in 2007 and the report of this evaluation was published in 2008. In the results of the evaluation and due to having an under-developed ML/CFT legal and institutional framework Tajikistan was placed in an enhanced EAG follow-up process and became a subject of FATFs International Cooperation Review Group (ICRG) process (MER of RT, 2018).

In response, the government of Tajikistan worked to address the deficiencies that were identified and strengthen the AML/CFT system. For example, various laws and codes were enacted to regulate financial institutions, such as the AML/CFT/CPF Law, the Criminal Code, the Criminal Procedure Code, the Code of Administrative Offences, the Civil Code, the Law "On Banking", the Law "On State Registration of Legal Persons and Individual Entrepreneurs", the Law "On the Securities Market" and others. In this regard, the Financial Monitoring Department under the National Bank of Tajikistan (FMD) is the “designated competent authority” in the AML/CFT regime. Therefore, the FMD is responsible for the regulation and supervision of the AML/CFT system of the country with the goal of preventing ML/TF threats. It can be categorized as an administrative type of FIU (MER, 2018).

In October 2019 the FIU of Tajikistan celebrated its 10<sup>th</sup> anniversary and in connection with this event a panel conference on “Achievements of the Republic of Tajikistan in strengthening the national AML/CFT/CPF system” was held. During the panel conference the heads of the supervisory authorities and law enforcement agencies expressed their high regard for the contribution of the FMD in the supervision and regulation of the AML/CFT system in the country.

To manage the compliance requirements of the AML / CFT legislation in financial institutions, the FIU and the supervisory authorities must conduct audits of these institutions. A list of the FI’s and DNFBPs of the Republic of Tajikistan with the supervisory authorities is provided in **Table 1**.

***Table 1. Types of FIs and DNFBs with their Supervisory authorities in the Republic of Tajikistan***

<b>Type of FIs and DNFBPs</b>	<b>Supervisory Authorities</b>
Credit institutions: - banks - non-bank credit institutions - micro-finance institutions, insurance companies	National Bank of Tajikistan
Pochtai Tojik	Communications Agency under the Government of the Republic of Tajikistan
Professional securities market participants (brokers/dealers and the central depository)	Ministry of Finance (the Agency for the Development of the Securities Market and the Special Registrar of the Ministry of Finance of the Republic of Tajikistan)
Casinos	Prohibited by law
Real estate agents	FIU
Lawyers	FIU
Legal professionals	FIU
Notaries	Ministry of Justice
Auditors and audit firms	Ministry of Finance
Accountants	Ministry of Finance
Dealers in precious metals and precious stones	Ministry of Finance
Trust and company service providers	FIU
Pawnshops	Ministry of Finance
Organizations owning sweepstakes and betting offices and holding lotteries and other games	Ministry of Finance

**(adapted from the Mutual Evaluation Report of the Republic of Tajikistan, 2018.)**

## **2.6 Summary**

In summary, this section has presented a preliminary overview of the literature on AML/CFT, FATF Standards and its mutual evaluation exercises. As mentioned earlier (see the introduction section), money laundering and terrorism

financing are still considered to be problematic, a situation which still affects international society. This section also introduced the issue of money laundering and the phenomenon of terrorism financing, gave a brief overview of FATF standards and the main goal of FATF and its body type groups. Thus, it is possible to understand the importance of the FATF Recommendations and mutual evaluation for all countries and how these may affect a country and its economy. With the above background in mind, this study will now turn to the methodology employed to investigate the current level of implementation and the impact of the FATF Recommendations on AML/CFT policies in the Republic of Tajikistan.

## **CHAPTER 3. METHODOLOGY**

This Chapter describes the research context, methodological procedures, collection of data and methods of analysis used in this research.

### **3.1 Research Context**

The focus of this study was the supervision and regulation of the Republic of Tajikistan's financial institutions in the area of AML/CFT. As outlined in the following sections, the research methodology employed in this study is largely qualitative and survey questionnaires were employed as the primary instrument for collecting data. The surveys were delivered to specific organizations and individuals in charge of AML/CFT regulations in the Republic of Tajikistan, as follows:

- The Financial Intelligence Unit (FIU) staff of the Republic of Tajikistan. These included;
- The Ministry of Finance of the Republic of Tajikistan;
- The Ministry of Justice of the Republic of Tajikistan.

The principal reason for carrying out interviews with people working directly in AML/CFT field and with FATF standards was to discover the gaps with and difficulties of implementing Supervision Recommendations and the passing of Mutual Evaluations.

In addition to the data collected via the interviews, this study also reviewed various secondary sources, principally the Mutual Evaluation Reports of the Republic of Tajikistan which were submitted in 2008 and 2018 and the annual

report of the FIU of Tajikistan for the period 2011-2019. To provide a basis for comparison between the Republic of Tajikistan and other countries sharing similar experiences, the Mutual Evaluation Reports of 5 EAG countries were reviewed and compared with the Mutual Evaluations of the Republic of Tajikistan regarding AML/CFT regulation and supervision of financial institutions. The specific techniques and procedures employed to analyze the primary and secondary data are outlined in the following section.

### **3.2 Research Methods**

With this context in mind and, as mentioned above, a qualitative approach was selected as the primary methodological framework in this research. Qualitative methods were deemed to be the most appropriate, since the focus of this research was to analyze a particular aspect of a phenomenon in one country and carefully work towards the implementation of FATF standards, specifically Supervision Recommendations.

Moreover, analysis of sources shows the effectiveness of using a qualitative approach in this field under analysis in this study. Multiple studies, for instance, have employed qualitative methodologies in support of research on money laundering such as Gesase's (2013) report on the impact of MERs in Tanzania, Sharipov's (2017) research on raising Awareness and Sensibility in AML/CFT Network and Simchitma's (2019) study on the AML/CFT system in the Russian Federation.

As mentioned above, the primary mechanism for collecting data in this study is via structured interviews which were carried out with individuals who have

responsibility for the AML/CFT regulations in Tajikistan. In terms of the other sources mentioned above, the AML/CFT Mutual Evaluation Reports of the Republic of Tajikistan and the annual report of the FIU of Tajikistan for the period 2011-2019 were consulted as secondary source material in this research (see Section 3.1 above).

### **3.3 Data Collection and Analysis**

#### **3.3.1 Analysis of the Primary Data**

An interview approach was employed as the primary source of data collection. Mingers (2003) in his study on "The paucity of multimethod research: a review of the information systems literature" describes interviews as a type of conversation and mentions that interviews can range from structured formats to unstructured or open-ended formats. Additionally, Bryman (2008, p.437) mentioned that in order to "maximize the reliability and validity of measurement of key concepts", more structured interviews should be conducted.

With the above in mind and in order to enlist interviewees and enhance communication with them, a set of structured interview questions were designed and delivered with a cover letter by email to the Financial Monitoring Department of the National Bank of Tajikistan, the Ministry of Finance and the Ministry of Justice. Additionally, follow-to up telephone calls were made to these organizations to remind the respondents of the submission deadline. In the end, a total of 22 interviews were conducted with staff from these three main AML/CFT supervisory authorities of the Republic of Tajikistan. The question of the conducted interview presented in **Appendix 1** by the way of example.



In this regard, in terms of the discussion of data sampling, purposive sampling was chosen. This type of sampling gives the researcher the opportunity to interview people connected to the research area (Bryman, 2008). Additionally, purposive sampling allows for research based on quality rather than quantity by allowing the researcher to analyze and interpret the responses of a small group of interviewees (Bowen, 2005)

Pope, Ziebland, and Mays (2000) points out that interview transcripts and observations do not provide immediate insights into the interpretation of the data (Pope, C., Ziebland, S., & Mays, N., 2000). The researcher is required to carefully analyze and look for patterns in the collected data. In this regard, the generally analytical process employed in this study was based on grounded theory. In grounded theory, the researcher develops theories about specific points in the data by studying patterns that emerge and then codes them. In qualitative data analysis, grounded theory is frequently used as the basis for developing analytical techniques (see Bryman, 2008). Two notable aspects of grounded theory include: developing theories from the data (Cresswell, 1998, Matsuo et al., 2008); and adopting an iterative approach to data analysis to refine the analytical procedures (Miles and Huberman, 1994). With the above in mind, the interview transcripts were analyzed and coded, and remarks were added “in the margins” to facilitate interpretation of the patterns observed. According to Miles and Huberman (1994), marginal remarks help to develop codes, obtain ideas and reach new interpretations of the data. Throughout the coding process applied in this study, attention was given to Strauss's (1987) recommendation that “the excellence of the research rests in large part on the excellence of the coding” (Strauss, 1987, p.27). Therefore, careful attention was given to developing and refining an appropriate set of codes.

Following the procedures set out by Saldana (2016), a set of codes were refined that summarize the key patterns and themes that emerged from the survey data. A summary of the codes is presented in **Appendix 2** by way of example.

### 3.3.2. Comparative analysis of the Secondary Data

In addition to the procedures outlined above to analyze the primary data, the researcher also conducted a comparative analysis of the level of implementation of supervisory recommendations among 5 EAG countries (including the Republic of Tajikistan, the Republic of Belarus, the Kyrgyz Republic, the Peoples Republic of China and the Russian Federation). This was achieved by reviewing the 2<sup>nd</sup> round of Mutual Evaluation Reports for these countries.

Examples of these analyses are provided in **Table 2** and **Table 3** below. **Table 2** shows the results of ratings of effectiveness and technical implementation in the 5 EAG countries and **Table 3** provides an explanation of the abbreviations mentioned in Table 3. Key findings from the analysis of the MERs are presented in the following Chapter (4).

**Table 2. The level of implementation of Supervisory Recommendations in EAG countries according to the MER of each country**

№	Country	IO.3	R.26	R.27	R.28	R.35
1	Republic of Tajikistan	ME	PC	LC	PC	PC
2	Republic of Belarus	ME	LC	LC	PC	LC
3	Kyrgyz Republic	ME	LC	LC	NC	LC

4	People's Republic of China	ME	PC	LC	NC	PC
5	Russian Federation	ME	LC	LC	LC	LC

**Table 3. Abbreviation and Definition of Table 2**

Abbreviation	Definition
IO.3 (Immediate Outcome 3)	Supervision
R.26 (Recommendation 26)	Regulation and supervision of financial institutes
R.27 (Recommendation 27)	Powers of supervision,
R.28 (Recommendation 28)	Regulation and supervision of DNFBPs
R.35 (Recommendation 35)	Sanctions
ME	Moderate level of effectiveness - The Immediate Outcome is achieved to some extent. Major improvements needed.
C	Compliant
LC	Largely compliant - There are only minor shortcomings.
PC	Partially compliant - There are moderate shortcomings.
NC	Non-compliant - There are major shortcomings.

### 3.4. Limitation and Ethical considerations

Despite the care taken by the researcher, some issues arose that created limitations for the collection and analysis of data in this study. One limitation was the lack of previous research on the topic. For instance, there is almost no research on AML/CFT regulation and supervision of financial institutions in the Republic of Tajikistan, nor the MER or the AML/CFT system in Tajikistan. This is because

AML/CFT system is new phenomenon in Republic of Tajikistan. Secondly, there were limits imposed by the security of some information. Obviously, state institutions are restricted in the amount of confidential information that they can provide to researchers or the public. Similarly, the staff of these institutions may be restricted in the amount of information that they can provide due to employment regulations or other factors within their departments or institutions as a whole.

A second limitation concerns the nature of research sampling which can cause bias in the data collected. As mentioned above, due to the nature and characteristics of the research topic, a purposive sampling approach was selected in this study. In this regard, the researcher selected interview respondents which means that interviews were conducted with a single target group. Therefore, in using this kind of approach some form of bias can apply. In order to avoid any kind of bias, interviews were conducted with 20 employees from 5 different divisions of the Financial Monitoring Department under the National Bank of Tajikistan, 1 employee from the Ministry of Justice, and 1 employee from the Ministry of finance. Lastly, there were some delays in data collection due to the need to obtain permission to conduct the research.

In addition, due to the impact of COVID 19, there were difficulties with conducting the planned field trip to and interviews in the Republic of Tajikistan. These issues were carefully considered as the research proceeded in order to minimize and mitigate their impact on the collection of data and the completion of the research.

Finally, due to the sensitive nature of the research subject, this study faced some ethical issues which the researcher had to consider. Most importantly, the

interviews were conducted with individuals working directly in the AML/CFT field, and if their identities were not kept confidential, they could have faced pressure at work which would have created risks for their careers. Therefore, all interviews were conducted in accordance with APU's research ethics guidelines and with the aim of protecting the identity of the respondents. Additionally, and before conducting the research, all participants were informed that their responses to the questionnaire will remain private and confidential and will only be viewed by the researcher and researcher supervisor at APU.

Following the above procedures and taking into consideration the various limitations mentioned, the researcher proceeded to collect and analyze the data from the primary and secondary sources. The findings of these analyses are presented for discussion in the next chapter.

## **CHAPTER 4. IMPLEMENTATION OF THE SUPERVISION RECOMMENDATIONS IN EAG COUNTRIES**

This chapter presents the findings of a comparative analysis of EAG countries on their implementation of the Supervisory Recommendations. Specifically, it looks at the implementation of a risk-based approach while conducting audits of financial institutions and the imposition of sanctions in case of the identification of violations of AML/CFT requirements. The comparative analysis is based on the results of the findings data collected from the Mutual Evaluation Reports (MERs) of each country.

The chapter begins with an analysis of the rating level of the implementation of Recommendations 26,27,28 and 35 including IO.3 and the factors underlying the rating in Section 4.1; the implementation of Core Principle of Recommendation 26 specifically using a risk-based approach while conducting audits of financial organizations in Section 4.2; and the power of supervisory authorities to impose sanctions in the case of the identification of violations of AML/CFT requirements in Section 4.3 and the summary of this chapter is noted in Section 4.4.

### **4.1. Rating Level of the implementation of Recommendations and underlying factors**

In October 2003, during the FATF Plenary Meeting the Russian Federation suggested to establish a FATF Style Regional Body (FSRB) for the Eurasian region countries which were not included in any existing FSRBs. Later, in October 2004 the Eurasian Group on Combating Money Laundering and financing of terrorism (EAG) was established and included six countries which later become nine. These included Belarus, China, India, Kazakhstan, Kyrgyz Republic, Russia, Tajikistan,

Turkmenistan, Uzbekistan. Following this, the regional intergovernmental organization EAT, according to its program of mutual evaluations from 2017, started to conduct the 2nd round of mutual evaluations in its member countries. During the mutual evaluation assessors evaluated the effectiveness of compliance with FATF Recommendations in the countries and by the end of the evaluation published a report. Information regarding the schedule of EAG mutual evaluations is provided in **Table 4**, adapted from the EAG web page (<https://eurasiangroup.org/en/general-information>).

**Table 4. Schedule of EAG mutual evaluation**

<b>State</b>	<b>Evaluating Body</b>	<b>Dates of the On-site mission</b>	<b>Dates of discussion of the MER at the EAG Plenary</b>
Kyrgyzstan	EAG	March 2017	November 2017
Tajikistan	EAG	March 2018	November 2018
China	FATF/EAG/ APG	July - August 2018	August 2019
Belarus	EAG	March 2019	November 2019
Russia	FATF/EAG/MONEYVAL	March 2019	October - December 2019
Turkmenistan	EAG	March 2021	November 2021
Uzbekistan	EAG	March 2021	November 2021
India	FATF/EAG/APG	October 2021	November 2022
Kazakhstan	EAG	April 2022	November 2022

*(Adapted from EAG web page)*

As mentioned earlier, based on the findings of the mutual evaluation, assessors present a report which includes detailed information regarding findings,

recommendations and the rating for 40 FATF Recommendations. **Table 5** provides an overview of the level of implementation of Supervisory Recommendations in five EAG countries: Tajikistan, Belarus, the Kyrgyz Republic, China and Russia. **Table 6** following provides a list of abbreviations used and their definitions.

**Table 5. The Rating Levels of Recommendations in Tajikistan, Belarus, Kyrgyz Republic, China and Russia based on their MERs.**

№	Country	IO.3	R.26	R.27	R.28	R.35
1	Republic of Tajikistan	ME	PC	LC	PC	PC
2	Republic of Belarus	ME	LC	LC	PC	LC
3	Kyrgyz Republic	ME	LC	LC	NC	LC
4	People's Republic of China	ME	PC	LC	NC	PC
5	Russian Federation	ME	LC	LC	LC	LC

**Table 6. Definitions for used abbreviations in Table 5**

Abbreviation	Definition
IO.3 (Immediate Outcome 3)	Supervision
R.26 (Recommendation 26)	Regulation and supervision of financial institutes
R.27 (Recommendation 27)	Powers of supervision,
R.28 (Recommendation 28)	Regulation and supervision of DNFBPs
R.35 (Recommendation 35)	Sanctions
ME	Moderate level of effectiveness - The Immediate Outcome is achieved to some extent. Major improvements needed.



C	Compliant
LC	Largely compliant - There are only minor shortcomings.
PC	Partially compliant - There are moderate shortcomings.
NC	Non-compliant - There are major shortcomings.

Firstly, in terms of the general findings of the comparison of the five countries, **Table 5** shows that the Russian Federation achieved the highest rating of this grouping, scoring Largely Compliant (LC) in each of the four recommendations (26, 27, 28 and 35). This result may be attributed to the fact that the Bank of Russia (BoR) started conducting risk-based supervision in 2013, and with the results of the National Risk Assessment from 2017 their RBA policy was strengthened. However, while evaluating the implementation of Immediate Outcome 3 (Supervision) in the Russian Federation, assessors concluded that ML/TF risk understanding was, for the most part, improved after conducting the NRA with the only minor shortcoming being that the supervisory authorities needed to improve their understanding of the sectors, specifically they had to establish RBA measures for auditing the lawyers and notaries.

Following the Russian Federation, Republic of Belarus received an LC score for three of the recommendations (26, 28 and 35) and PC for Recommendation 28. Against this background, minor shortcomings were identified with some sanction procedures. In the case of implementation of the Core Principles of Recommendations 26, risk-based supervision is established in legislation and all financial institutions were subject to supervision. However, as the shortcomings that were identified were relatively minor and FATF Standards were largely

implemented, the established AML/CFT policy of the Russian Federation and Republic of Belarus can be viewed as more successful among these EAG countries.

In comparison, the Republic of Tajikistan may be viewed as moderately successful, with a score of LC in one recommendation (27) and scores of Partially Compliant (PC) in the others. In this sense Tajikistan compares more favorably than the People's Republic of China and the Kyrgyz Republic, which registered at least one non-Compliant score (NC) each for Recommendation 28. In fact, China and the Kyrgyz Republic don't have any regulation and supervision measures regarding the DNFBPs and they have not implemented the requirements of Recommendation 28 at all, even though these countries received LC scores for the other Recommendations. Based on these findings, it is possible to observe that China and the Republic of Tajikistan, in comparison with the other EAG countries, are making progress in their efforts to implement the FAFT recommendations, placing them on a good footing to make further improvements in the years ahead.

Additionally, it is important to point out that the rating of each recommendation is based on the implementation of the given criteria. By the end of the evaluation, assessors must apply the criteria underlying the rating of recommendations. **Table 7** provides details of the specific criteria underlying the rating of Recommendations 26,27,28, and 35 in five EAG countries. Reading from left to right, **Table 7** shows the name of the country, the name of the recommendations, the rating level of the recommendation and, in the column to the far right, the details of the criteria underlying these ratings.

***Table 7. The results of MER related to Recommendations 26,27,28 and 35 in the five EAG countries***

Country	Recommendation	Rating	Criteria underlying the rating
<b>Tajikistan</b>	26. Regulation and supervision of financial institutions	PC	<ul style="list-style-type: none"> <li>➤ There is no requirement for the owners and beneficial owners of insurance and securities market participants to have no criminal record;</li> <li>➤ Supervision over FIs is not fully in line with the Framework Principles;</li> <li>➤ The frequency and intensity of on-site and off-site AML/CFT supervision of financial institutions are not determined based on a risk-based approach;</li> <li>➤ There is no requirement for the supervisors to review the assessment of the ML/TF risk profile of a financial institution, or when there are major events or developments in the management and operations of the financial institution.</li> </ul>
	27. Powers of supervisors	LC	<ul style="list-style-type: none"> <li>➤ The Communications Agency under the Government of the Republic of Tajikistan has no authority to carry out inspections of postal service providers for compliance with the AML/CFT Law;</li> <li>➤ The Communications Agency lacks the powers to compel the production by reporting entities of any information relevant to monitoring compliance with the AML/CFT requirements;</li> <li>➤ Financial sector supervisors other than the NB lack the powers to impose sanctions for non-compliance with AML/CFT requirements:</li> </ul>
	28.Regulation and supervision of DNFBPs	PC	<ul style="list-style-type: none"> <li>➤ Supervisors over auditors and dealers in precious metals and precious stones are not authorized to conduct on-site and remote inspections, including monitor compliance with AML/CFT requirements;</li> <li>➤ There is no requirement to take the necessary measures to prevent criminals or their associates from holding a controlling interest in a DNFBP;</li> <li>➤ The shortcomings noted in R.35 also apply to criterion 28.4(c);</li> <li>➤ Supervisors are not authorized to apply sanctions against DNFBPs for failure to comply with the AML/CFT Law;</li> <li>➤ Supervision over DNFBPs is not based on the risks identified</li> </ul>
	35. Sanctions	PC	<ul style="list-style-type: none"> <li>➤ A broad range of effective, proportionate, and dissuasive sanctions against the senior management of FIs (except for credit institutions) and DNFBPs are absent.</li> </ul>

<b>Republic of Belarus</b>	26. Regulation and supervision of financial institutions	LC	<ul style="list-style-type: none"> <li>➤ Licensing restrictions do not apply to persons who may be involved in committing crimes other than economic crimes, involving financing or other complicity in terrorism and extremism;</li> <li>➤ legal entities and individual entrepreneurs have the ability to carry out leasing activities without being included in the register under certain conditions• no checks are made for the professional participants of the securities market (who are not banking institutions) against the founders and shareholders or ben. owners.</li> <li>➤ Existing requirements do not apply to affiliated persons.</li> <li>➤ Except for Banks there are no requirements and procedures for determining the frequency and depth of AML/CFT supervision of financial institutions and groups based on the ML/TF risks existing in the country for other categories of FIs;</li> <li>➤ Other than the NBRB, there is no obligation for supervisors to review the assessment of the ML/TF risk profile of a financial institution or group (including the risks of non-compliance) periodically, or when there are significant events or changes in the management and operations of the financial institution or group for the remaining categories of FIs.</li> </ul>
	27. Powers of supervisors	LC	<ul style="list-style-type: none"> <li>➤ There are no direct obligations to revoke, limit or suspend the license for violation of AML/CFT measures (except for banking legislation)</li> </ul>
	28.Regulation and supervision of DNFBPs	PC	<ul style="list-style-type: none"> <li>➤ The requirements of the law do not apply to affiliated persons;</li> <li>➤ No licensing requirements for the beneficial owners and persons with controlling interest,</li> <li>➤ The established forms of supervision do not fully comply with the EPR model recommended by criterion 28.5</li> </ul>
	35. Sanctions	LC	<ul style="list-style-type: none"> <li>➤ No direct obligations for suspension or termination of the license for AML/CFT violations, except for banking legislation,</li> </ul>
<b>Kyrgyz Republic</b>	26. Regulation and supervision of financial institutions	LC	<ul style="list-style-type: none"> <li>➤ Licensing/registration procedures do not apply to leasing companies and commodity exchanges;</li> <li>➤ Measures designed to prevent criminals from holding a controlling or management function in pawnshops, leasing companies, commodity exchanges and insurance brokers are absent;</li> </ul>

			<ul style="list-style-type: none"> <li>➤ The requirement to apply a RBA to supervision has not been fully complied with.</li> </ul>
	27. Powers of supervisors	LC	<ul style="list-style-type: none"> <li>➤ Some supervisors (Gosfinnadzor and the SIT&amp;CC) lack the powers to revoke licenses and impose financial penalties;</li> <li>➤ Certain types of financial institutions (pawnshops, leasing companies and commodity exchanges) are not subject to AML/CFT supervision.</li> </ul>
	28.Regulation and supervision of DNFBPs	NC	<ul style="list-style-type: none"> <li>➤ AML/CFT supervision over the activities of real estate agents, notaries and independent legal professionals is absent. The Finance Ministry's Precious Metals Department, which is tasked with monitoring compliance by persons carrying transactions with precious metals and precious stones, is under no obligation to prevent criminals and their accomplices from being professionally accredited, or holding (or being the beneficial owner of) a controlling interest, or holding a management function in the said accountable entities. There are also no mechanisms allowing it to apply sanctions against these entities for noncompliance with AML/CFT requirements.</li> </ul>
	35. Sanctions	LC	<ul style="list-style-type: none"> <li>➤ A range of sanctions applied against financial institutions accountable to Gosfinnadzor for noncompliance with the AML/CFT requirements lack sufficient measures to target officials;</li> <li>➤ A range of sanctions applied against DNFBPs for non-compliance with AML/CFT requirements is insufficient;</li> <li>➤ The size of penalties imposed in accordance with the Administrative Code is relatively small for large financial institutions.</li> </ul>
China	26. Regulation and supervision of financial institutions	PC	<ul style="list-style-type: none"> <li>➤ The online lending sector is not subject to the AML Law and is not supervised for AML/CFT requirements. This scope issue has an impact on all aspects of R.26 (except c.26.2).</li> <li>➤ The main shortcoming with regard to c.26.3 is that in most sectors the minimum period that directors and managers must be crime-free is limited to between three to five years.</li> </ul>
	27. Powers of supervisors	LC	<ul style="list-style-type: none"> <li>➤ Sanctions are not in line with the standards set out in R.35.</li> </ul>

	28.Regulation and supervision of DNFBPs	NC	<ul style="list-style-type: none"> <li>➤ There are no measures for regulation and supervision of DNFBPs, except for trust companies and DPMs. This scope issue has an impact on all aspects of R.28.</li> </ul>
	35. Sanctions	PC	<ul style="list-style-type: none"> <li>➤ There are concerns that the sanctions applicable to the financial sector are not effective, dissuasive and proportionate given their low scale and cap compared to the size and composition of the financial sector in China.</li> <li>➤ No sanctions applicable to designated DNFBPs.</li> </ul>
<b>Russia</b>	26. Regulation and supervision of financial institutions	LC	<ul style="list-style-type: none"> <li>➤ The criminal record checks do not clearly cover criminal associates and the wider array of criminal offences.</li> <li>➤ There are minor shortcomings for supervision of Core Principles institutions.</li> <li>➤ Off-site supervision and unscheduled inspections can only be carried out on the ground of potential violation of the AML/CFT legislation by law, and not on the basis of other risk considerations.</li> </ul>
	27. Powers of supervisors	LC	<ul style="list-style-type: none"> <li>➤ Sanctions are not fully in line with the standards set out in R.35.</li> </ul>
	28.Regulation and supervision of DNFBPs	LC	<ul style="list-style-type: none"> <li>➤ There is no designated supervisor for legal professionals</li> <li>➤ There are no mechanisms to accredit legal professionals and to prevent criminal infiltration.</li> <li>➤ absence of measures to prevent criminal associates from being professionally accredited or from holding a significant or controlling interest in all DNFBPs.</li> <li>➤ There are no provisions or measures establishing the risk-based approach in supervision especially for lawyers and notaries</li> </ul>
	35. Sanctions	LC	<ul style="list-style-type: none"> <li>➤ Monetary sanctions are not fully dissuasive.</li> <li>➤ The penalties related to TFS violations are not sufficient to be proportionate and dissuasive</li> </ul>

*(Adapted from the Mutual Evaluation Report of these countries.)*

**Table 7** shows that there are shortcomings and gaps that each country will need to fill to develop their institutional and legal framework. For example, according to the criteria underlying the recommendation ratings in **Table 7**, it is possible to argue that none of the countries fully implemented the requirements of supervision recommendations. According to the results, each country has

shortcomings regarding the use of a risk-based approach since they regulate the financial institutions or the sanctions and their procedures.

With this in mind, the following sections of this chapter deal with the main weaknesses identified with the supervision recommendations, namely the regulation of financial institutions according to a risk-based approach and the imposition of sanctions in case of identification of violations of AML/CFT legislation.

## **4.2. Implementation of RBA requirements in Tajikistan, Belarus, the Kyrgyz Republic, China and Russia.**

Compliance with the Core Principle of Supervisory Recommendations requires all countries to promote risk-based supervision in every type of financial institutions. From the analysis of the MERs of the five EAG countries, it is possible to observe that this requirement is implemented well by the Republic of Belarus and the Russian Federation. Also, the Kyrgyz Republic would present significant progress in the implementation of RBA requirements, while the Peoples Republic of China and the Republic of Tajikistan are in discharge and have weaknesses related to the abovementioned requirements.

### **4.2.1. Countries with minor shortcomings: Republic of Belarus and Russian Federation.**

For example, in the Republic of Belarus all supervisory authorities carried out risk-based supervision of financial institutions. Moreover, this requirement is set in a law and supervisors can conduct audits in financial institutions according to

the prescribed methodology. In the MER of this country the assessors noted the following:

344. Criterion 26.5

(a) Article 16 of AML/CFT Law as well as 2nd part of the paragraph 2 of the Decree of 16.10.2009 No. 510, part 2 of paragraph 9 of the Decree of 16.10.2009 No. 510, paragraph 84 of the Regulation on the order of inspections, approved by the Decree of 16.10.2009 No. 510 sets out the list of government agencies responsible for monitoring compliance with the AML/CFT/CPF requirements, as well as their requirements for frequency and intensity of inspections (on-site and off-site). As part of these requirements, targets for inspections are selected on the basis of the risk assessment criteria, including ML/TF risks, as well as the findings of analysis of the information available to the controlling (supervisory) body - results of the analysis of the internal control rules and other procedures, legislation violations and other relevant information). (MER, 2019)

Additionally, the National Bank of the Republic of Belarus (NBRB) started conducting risk-based audits in its controlled financial institutions from 2014. This type of inspection references established indicators and risk categories of financial institutions under supervision. **Table 9** summarizes the information regarding this supervision activity. The first two rows of the table show the years when audits were conducted and the risk level. The letters “H, M and L” mean “High, Moderate and Low”. In the first column (to the left) the types of financial institutions are listed.

***Table 8. Number of FIs controlled by NBRB in each risk category***



	2014			2015			2016			2017			2018		
	H <sup>1</sup>	M	L	H	M	L	H	M	L	H	M	L	H	M	L
Banks	8	5	18	6	8	12	9	8	7	4	8	12	4	10	10
Non-bank financial institutions	0	0	0	0	0	1	0	0	3	0	0	3	0	0	4
Development Bank	0	0	0	0	0	0	0	0	1	0	1	0	0	1	0
Leasing organizations	0	0	0	9	0	90	21	0	74	25	0	78	13	0	84
Microfinance institutions	0	0	0	0	0	0	35	55	25	50	57	14	44	48	12
Forex companies	0	0	0	0	0	0	6	0	0	10	0	0	10	0	0
National Forex Center	0	0	0	0	0	0	0	0	1	0	0	1	0	0	1

(The given Table adapted from MER of the Republic of Belarus, 2019, p. 113)

By the end of the evaluation assessors noted that the NBRB established an effective mechanism for risk-based supervision and from 2018 the supervisory authorities began to implement this mechanism with their controlled financial institutions.

In the case of the Russian Federation, as mentioned above, the BoR carried out risk-based supervision from 2013, however, during that time, this some aspects of RBA requirements were implemented. Therefore, by the end of the NRA, risk-based supervision was improved. Likewise, the BoR has been ranking the risk level of financial institutions based on three criteria: transaction risks, non-compliance with AML/CFT legislation and risk of AML/CFT system inefficiency. Based on these results, in Russian Federation, financial institutions can be ranked on three levels: high, medium and low. **Table 9** summarized the rankings. Later, depending of the risk level, related types of inspection can be conducted in each financial institution. For **Table 9**, the first column shows the group of financial institutions, the second provides the level of assigned risk and the following three columns show the risk percentage of financial institutions in the years 2016, 2017 and 2018.

**Table 9. Risk classifications of financial institutions in Russian Federation**

Sectors	Risk ratings	2016	2017	2018
<b>Credit Institutions</b>	high	22%	16%	9%
	medium	15%	16%	9%
	low	63%	68%	82%
<b>Securities Market Professionals</b>	high	0.6%	0.9%	0.7%
	medium	0.0%	0.0%	0.0%
	low	99.4%	99.1%	99.3%
<b>Insurance Entities</b>	high	4.1%	3.0%	0.9%
	medium	2.9%	2.1%	0.1%
	low	93%	94.9%	99%
<b>Micro-Finance Organisations</b>	high	2.9%	2.7%	2.7%
	medium	0.5%	0.2%	0.3%
	low	96.6%	97.1%	97%

(Table adopted from MER of Russian Federation, 2019)

The main gap in risk-based supervision in the Russian Federation is the absence of any mechanism for a risk-based approach that covers lawyers and notaries. Furthermore, off-site and unscheduled supervision are not based on risk considerations.

#### **4.2.2. Countries with moderate and low shortcomings.**

From this perspective the FIU of China, which was established within the People’s Bank of China, conducts AML/CFT audits in financial institutions based on the results of the risk assessments provided. Assessors drew the following conclusions:

d) Financial sector supervisors have a moderate level of understanding of ML/TF risk (except for the insurance regulator who demonstrated a higher level of understanding). DNFBP sector regulators have a low level of understanding of

ML/TF risk and undertake virtually no AML/CFT supervision (MER of China, 2019, p. 119)

Additionally, the Kyrgyz Republic began to implement a risk-based approach from 2016, however by the end of on-site visits and evaluations, assessors concluded that the established risk-based supervision mechanism was unclear and not implemented fully. Also, the follow-up report on the Kyrgyz Republic shows that risk-based supervision is evaluated as low and includes the following.

Resolution No.606 requires the inspection authorities to apply the risk-based approach (RBA) in course of inspections of the supervised entities and establishes the procedure of application of the RBA to supervision. The inspection authorities are prescribed to apply the RBA based on understanding of risks, develop and use the risk assessment criteria, and reallocate their resources for inspecting, in the first turn, those entities that are exposed to high risk (Follow up report of KR, 2019)

According to the outcomes mentioned above, it is possible to argue that, in comparison with the Republic of Tajikistan and Kyrgyz Republic, the three other EAG countries namely the Republic of Belarus, the Russian Federation and the Peoples Republic of China could apply relatively strong risk-based supervision mechanisms.

For example, in Republic of Belarus, the method for categorizing the risks to financial institutions in the targeted group is based on three vectors: 1) risk by organization profile, 2) risk by geographic region and; 3) risk by the organization's products. Therefore, all information collected and related to the organizations has been analyzed in accordance with the above-mentioned vectors and based on the results the related level of risk is determined using a matrix. Moreover, this

mechanism is employed not only by the supervisory authorities but also by the financial institutions. Due to enhancements in the AML/CFT system financial institutions established their own algorithm of appropriation to determine the level of risk to their clients in accordance with the AML/CFT law of the country and the guidance prepared by the NBRB.

Additionally, the People's Republic of China improved its AML/CFT national legislation and, with the aim of ensuring the financial security of the country by regulation and supervision of financial institutions in accordance with a risk-based approach, adopted the "Measures for the Supervision of Anti-Money Laundering and Counter-Terrorist Financing of Financial Institutions". In accordance with this document China enhanced the power of supervisory authorities and provide detailed information related to the risk-based supervision of financial institutions.

Moreover, during their mutual evaluations, the Republic of Belarus, the Russian Federation and China were able to present to experts on the effectiveness of their established risk-based mechanism by providing detailed statistics. Specifically, the results and numbers of conducted audits and the mechanism of risk analysis were provided in related tables and diagrams which could demonstrate the effectiveness of the system in these countries.

Consequently, among the five EAG countries reviewed here, Tajikistan would appear to return the lowest level of compliance with the Supervision Recommendations. Therefore, in order to demonstrate a safe financial system and enhance economic security, the AML/CFT system of the country must give attention to these gaps and weaknesses and resolve them as soon as possible. The details of findings regarding the implementation of the Supervisory

Recommendations in the Republic of Tajikistan are mentioned in Chapter 5 of this study.

### **4.3. The power of supervisory authorities to impose sanctions for violation of AML/CFT legislations in FIs**

Implementation of FATF Standards regarding sanctions is another shortcoming among the five EAG countries. The requirements call for countries to apply effective, proportionate, and dissuasive sanctions in accordance with Recommendation 35 available to deal with any failure to comply with the specified AML/CFT requirements. Moreover, these requirements assert the authority of the supervisors and demonstrate their effective regulation over financial institutions.

In this regard, the results of the analysis of mutual evaluation reports of five EAG countries show that none of them are fully compliant with Recommendation 35. The Republic of Belarus, the Russian Federation and the Kyrgyz Republic ranked as largely compliant with the implementation of Recommendation 35, however some minor gaps exist in this area.

#### **4.3.1 Compliance in the Republic of Belarus**

For example, supervisory authorities in the Republic of Belarus have broad powers to impose sanctions in case of identification of violation of AML/CFT legislation. Furthermore, they are applying sanctions according to the characteristics of the violations. Moreover, the response measure of supervisors depends on the indicators and numbers of the detected violation. For example, in case of the identification of violations for sending special forms, supervisors can

apply sanctions by way of sending official letters to recommend the elimination of deficiencies or to reduce the bonus of staff in the organizations. However, in case of repeat violations, the sanctions may be stricter and could include fines and license revocations.

In this regard, **Table 10** and **11** show the NBRB applied sanctions against the banking sector and the non-credit financial institution sector of the Republic of Belarus. In **Table 10** the first column shows the number and types of violation, the second provides information regarding the indicators and the last five columns present the number of imposed sanctions from 2014 to 2018. In **Table 12** in the first column shows the sanctions indicators and the last twelve columns provides information regarding the number of applied sanction by the type of the financial institutions.

*Table 10. NBRB applied sanctions to identified violations in the Banking Sector*

Indicator/year		2014	2015	2016	2017	2018
1. Bringing to administrative responsibility						
1.1.	Number of fines (pcs), including:	45	21	28	8	4
	<i>Art. 11.72 para. 1 (violation of AML/CFT/CPF measures)</i>	2	0	0	0	0
	<i>Article 11.72 part 2 (violations of the questionnaire procedure)</i>	6	7	6	0	1
	<i>Art. 23.20 (violation of registration of financial transactions)</i>	36	13	22	8	3
	<i>Art. 23.16 (failure to provide documents, reports)</i>	1	1	0	0	0
1.2.	Total amount of fines (USD), including	13 397	119	139	43	23
	<i>Art. 11.72 para. 1 (violation of AML/CFT/CPF measures)</i>	13 232	0	0	0	0
	<i>Article 11.72 part 2 (violations of the questionnaire procedure)</i>	21	30	30	0	6
	<i>Art. 23.20 (violation of registration of financial transactions)</i>	116	55	109	43	17
	<i>Art. 23.16 (failure to provide documents, reports)</i>	28	34	0	0	0
1.3.	Average fine amount (US dollars)	298	6	5	5	6
1.4.	Number of warnings for violation of AML/CFT legislation	10	14	13	33	6
2. Dissemination of information						
2.1.	Publication of information about the bank's administrative responsibility on the official website of the National Bank in the Internet	0	0	0	0	0
3. Application of supervisory response measures						
3.1.	Number of directed regulations, including	7	6	12	6	3
	Elimination of violations identified during the inspection	7	6	12	6	3
	licensing power limitation				1	0
	sending a letter to management bodies to review the issue of management bonuses	1	0	1	0	0
	Request for a letter stipulating the obligation to eliminate the identified violation (deficiency) and/or action (inaction) within a certain period of time	7	6	12	6	3
3.2.	Number of recommendations on elimination of identified deficiencies or conditions contributing to violations made on the basis of the results of inspections and monitoring, including	6	5	11	6	8
	consideration of the issue of increasing the number of employees in the special division	0	1	2	0	0
	Introduction (improvement) of automated control procedures aimed at detecting suspicious financial transactions	4	4	7	4	2
	Finalization of the database of customer profiles	0	2	7	2	1
	Amendments and additions to the local legal acts (ICR, orders, etc.)	5	2	6	3	2
	Updating customer profiles	2	0	2	1	0
	Improvement of the software complex where currency exchange transactions are carried out	0	0	1	0	0
	Conducting training activities and knowledge tests	5	8	7	1	0

	Adjusting the indicators of suspicious financial transactions	0	0	1	0	0
	appoint responsible persons and establish quality and correctness control	0	1	2	2	0
	follow-up inspection	1	2	2	0	0
	Development of additional internal control procedures for identification of non-resident individuals	0	0	0	0	1
	Analyse the activities of customers conducting suspicious financial transactions	0	0	0	0	2
	Ensure proper internal control	0	0	0	0	4

(Table adapted from the MER of the Republic of Belarus, 2019, pp. 122-123)

**Table 11. NBRB applied sanctions to identified violations in non-credit financial institutions sector**

Indicator	non-lending financial institutions											
	leasing companies			microfinance institutions						Forex companies, National Forex Center		
	2015*	2016	2017	pawn shops	funds	CCC	pawnshops	funds	CCC	2015	2016	2017
				2016			2017					
Number of fines for violation of AML/CFT/CPF legislation		6	9	0		0	2			0	0	0
Including under Art. 11.72 part 1 (violation of AML/CFT/CPF measures)		0	2	0		0	1			0	0	0
including Article 11.72 part 2 (violations of the survey procedure)		0	3	0		0	1			0	0	0
Including under Art. 23.20 (violation of registration of financial transactions)		6	4	0		0	0			0	0	0
Total amount of fines for violation of AML/CFT/CPF legislation (USD)		30	1 228	0		0	549			0	0	0
Including according to Article 11.72 part 1 (to the legal entity)		0	1 087	0		0	543			0	0	0
Including according to Art. 11.72 part 2 (natural person)		0	120	0		0	5			0	0	0
including Art. 23.20 (special forms)		30	22	0		0	0			0	0	0
Average amount of fine (US dollars)**		5	136	0		0	274			0	0	0
Number of warnings for violation of AML/CFT/CPF legislation (pcs.)		3	1	0	0	0	0			0	0	0
Number of revoked licenses (business discontinuances, exclusions from the register)	0	0	0	0	0	0	0		0	0	0	0
Number of prescriptions sent to legal entities on AML/CFT/CPF violations (pcs.)	7	6	6	3	0	0	8	0	1	0	0	0
Number of recommendations, letters on elimination of deficiencies (pcs.) (on sending to the SF, on organization of work, on identification procedure)	3	1	0	2	2	2	0	0	0	0	2	1

(Table adapted from the MER of the Republic of Belarus, 2019, p. 125)

In addition of the above, sanctions against gambling organizations were imposed by the Ministry of Taxes of the Republic of Belarus according to the norms of Code of Administrative Offences of the Republic of Belarus (CoAO). **Table 12** summarizes this information, showing (from left to right) the norm of CoAO, the number of issued resolutions and, the type of sanctions applied to gambling organizations.



**Table 12. Sanctions applied to identified violations in gambling organizations**

Norm of CoAO	number of resolutions issued	Sanction	
		warning notice	Penalty USD
<b>Part 10 Article 12.11 (other violations in the field of gambling)</b>			
Inadequate CDD measures	10		320
violation of the established procedure for recording winnings in the winnings register	88	3	1371
payment of the winnings without presentation of identity documents	3		140
<b>Total:</b>	<b>101</b>	<b>3</b>	<b>1831</b>
<b>2015</b>			
<b>Part 10 Article 12.11 (other violations in the field of gambling)</b>			
Inadequate CDD measures	15		580
violation of the established procedure for recording winnings in the winnings register	27	7	270
payment of the winnings without presentation of identity documents	21		1128
<b>Article 23.20 (CoAO, violation of the established procedure for sending a special forms)</b>			
	1		8
<b>Total:</b>	<b>64</b>	<b>7</b>	<b>41986</b>
<b>2016</b>			
<b>Part 10 Article 12.11 of the Administrative Offences Code (other violations in the field of gambling)</b>			
Inadequate CDD measures	16	1	982
violation of the established procedure for recording winnings in the winnings register	1		49
Payout of winnings without registration in the «SCCS»	1		58
<b>Article 23.20 (CoAO, violation of the established procedure for sending a special forms)</b>			
	5	1	177
<b>Total:</b>	<b>23</b>	<b>2</b>	<b>1266</b>
<b>2017</b>			
<b>Part 10 Article 12.11 (other violations in the field of gambling)</b>			
Inadequate CDD measures	20	3	645
<b>Total:</b>	<b>20</b>	<b>3</b>	<b>645</b>

(Adapted from the MER of the Republic of Belarus, 2019, pp. 127-128)

It is important to point out, however, that despite the establishment of a responsive mechanism to identify violations in financial institutions, minor shortcomings still exist in Republic of Belarus. The main weak point here is the

absence of special requirements for revoking, limiting or suspending licenses in case of non-compliance with AML/CFT legislations.

### 4.3.2 Compliance in the Russian Federation

Turning now to the case of the Russian Federation, AML/CFT supervisory authorities have wide powers to take measures in cases where violation of AML/CFT legislation is identified. Tables 16, 17 and 18 provide a summary of the sanctions imposed by supervisory authorities in the Russian Federation against financial institutions. **Table 13**, for instance, shows measures applied for AML/CFT violation by credit institutions and **Table 14** summarizes the sanctions applied to non-credit institutions. In each table the left-most column shows the type of measure and the columns to the right show the number of measures by year from 2013 to 2018.

**Table 13. AML/CFT sanctions against credit institutions**

	2013	2014	2015	2016	2017	2018
Warnings	247	233	0	0	0	0
written notice to the BOD/management about the shortcomings in its activities	181	196	509	334	307	598
Meetings	15	14	21	53	15	20
Fines on CIs	218	234	117	209	232	332
Average amount of fines on CIs (thousand RUB)	67.4	71.3	223.4	554.3	734.3	309.2
Fines on officials	55	69	61	102	133	87
Average amount of fines on officials (thousand RUB)	15.8	16.4	21.0	24.7	28.8	31.1
Limitation on certain transactions <sup>60</sup>	97	128	136	109	44	38
Bans on individual banking operations <sup>61</sup>	17	10	12	7	1	3
Orders on elimination of AML/CFT violations	136	95	226	189	159	359
Total number of licences revoked (includes AML/CFT reasons)	32 (8)	86 (36)	93 (34)	97 (35)	51 (24)	60 (35)
Number of revocations of licences only due to AML/CFT violations	2	11	10	0	0	2

(Adapted from the MER of the Russian Federation, 2019, p. 177)

**Table 14. AML/CFT sanctions against non-credit institutions**

	2014	2015	2016	2017	2018
<b>Preventive measures</b>			-	709	892
<b>Warnings (Total)</b>	<b>363</b>	<b>485</b>	<b>529</b>	<b>782</b>	<b>554</b>
Securities	33	30	31	9	10
Insurance	86	51	32	38	17
Micro-finance	133	198	239	324	235
CCC	88	158	215	395	276
Management Co.	12	15	7	16	14
Private pension funds	11	33	5	0	2
<b>Fines (No. [amount] in thousand RUB)</b>	<b>47[6,120]</b>	<b>64[5,100]</b>	<b>107[9,632]</b>	<b>113[10,750]</b>	<b>109 (8588)</b>
Securities	6[960]	9[650]	8[550]	2[400]	1 (50)
Insurance	6[1100]	14[1090]	18[1121]	12[805]	5 (870)
Micro-finance	25[2860]	25[2500]	42[4901]	39[2585]	27 (2950)
CCC	9[500]	11[610]	31[2510]	59[6910]	43 (4718)
Management Co.	1[700]	1[50]	1[50]	1[50]	0 (0)
Private pension funds	0	4[200]	7[500]	0	0 (0)
<b>Orders to eliminate AML/CFT Violations</b>	<b>0</b>	<b>1060</b>	<b>921</b>	<b>1927</b>	<b>1626</b>

(Adapted from the MER of the Russian Federation, 2019, p. 177)

The case of the Russian Federation is continued in **Table 15**, which provides an overview of the sanctions applied to DNFBPs, especially against Real Estate Agents and DPMS. The first column of the table shows the name of the DNFBP, the second shows the type of measures and the following five columns show the numbers of sanctions applied over a 5-year period.

**Table 15. AML/CFT sanctions against real estate agents and DPMS**

		2014	2015	2016	2017	2018
Real Estate Agents	Fines on entities	158	138	76	68	65
	Fines on officials	193	144	61	59	64
	Amount of sanctions (thousand RUB)	22578	21520	13041	8004	8342
DPMS	Orders on entities	36	63	23	149	174
	Orders on Officials	93	111	94	151	192
	Fines on entities	127	54	50	94	101
	Fines on officials	89	48	49	68	84
	Amount of sanctions (thousand RUB)	15,732	5,011	3,470	11,625	21491

(Adapted from MER of the Russian Federation, 2019, p. 181)

Despite the extent of implementation of requirements related to applying AML/CFT sanctions the Russian Federation, like the Republic of Belarus has minor shortcomings, especially related to monetary sanctions. Assessors consider that, in the Russian Federation, monetary sanctions are not fully dissuasive.

#### **4.3.3 Compliance in the Kyrgyz Republic**

Furthermore, in the context of the development of supervisory powers in the Kyrgyz Republic, it is notable that the supervisory authorities could ensure the implementation of requirements related to imposing sanction for the violation of AML/CFT requirements. As mentioned earlier, the Kyrgyz Republic was rated as a largely compliant in implementing these requirements. **Table 16** summarizes the measures applied by supervisory authorities in identifying violations of AML/CFT legislation in its financial institutions.

According to **Table 16**, sanctions were applied against most financial institutions. It can be concluded, then, that the country is currently in the process of improving the AML/CFT system and enhancing mechanisms for taking measures against violations of AML/CFT legislation. However, some supervisory authorities can only take administrative action; they don't have the power to apply financial sanctions. Also, assessors noted that in the Kyrgyz Republic "The range of sanctions applied against DNFBPs for non-compliance with AML/CFT requirements is insufficient" (MER KR,2018).

In Table 16, the first column (to the left) shows the type of financial institutions mentioned, the second shows the number of these institutions, and the following column provides information regarding inspections conducted in 2015,

2016 and 6 months of 2017. The remaining columns show the types of sanctions applied in 2015, 2016 and 6 months of 2017.

**Table 16. AML/CFT sanctions against financial institutions**

Reporting entities	Total	Inspections conducted			Remedial instructions issued following inspections			Fines imposed		
		2015	2016	6 mo. 2017	2015	2016	6 mo. 2017	2015	2016	6 mo. 2017
Commercial banks	25	31 (incl. 11 targeted)	14 (1 targeted)	8 (2 targeted)	47	28	12	11/KGS 61,000 (\$897) <sup>64</sup>	3/KGS 137,000 (\$2014)	-
Microfinance organizations	159	91	82	25	161	111	33	11/KGS 42,000 (\$617)	3/KGS 105,000 (\$1544)	-
Exchange offices	384	230	114	29	58	8	2	3/KGS 7,000 (\$103)	-	-
Credit unions	114	82	68	30	91	63	31	1/KGS 1,000 (\$15)	1/ warning	1
Leasing companies (financial)		-	-	-	-	-	-	-	1/ warning	-
Insurance/reinsurance companies	18	13	10	10	-	-	-	4/KGS 8,000 (\$118)	-	1/ warning
Professional securities market participants	105	3	2	5	-	-	1	-	-	-
Lottery organizers	25	11	10	2	-	-	-	-	-	-
Organizations managing investment funds or private pension funds	1	-	-	1	-	-	-	-	-	-
Persons engaged in transactions with precious metals and precious stones, jewellery made therefrom or scrap thereof, where they carry out any cash transactions with customers	468	329	327	127	-	-	-	7/KGS 24,000 (\$353) 6 warnings	5/KGS 35,000 (\$515) 5 warnings	-
Postal and telegraph organizations providing money transfer services	1	19	10	-	3	-	-	1/KGS 1,000 (\$15)		

(Adapted from MER of the Kyrgyz Republic, 2018, pp. 101-102)

#### 4.3.4 The case of China

In terms of the implementation of Supervisory Recommendations among the five EAG countries selected for comparison in this study, China is one of the countries with a low rating for compliance with the above-mentioned

recommendations. One important finding by the assessors during the evaluation of the AML/CFT system in China was that the supervisory authorities in the People’s Republic of China lack power. The main issue here is that measures to address violations of AML/CFT legislation are not established in the AML/CFT law of the country and sanctions can be applied only for implementation of internal controls in accordance with the sectors legislation. Moreover, due to the lack of supervisory power and the FATF Standards not being established in national legislation, no sanctions were applied against the DNFBPs and online lending institutions.

However, the Peoples Bank of China (PBC) can apply the remedial measures for violating AML/CFT law in accordance with the sectors legislation. **Table 17** shows the results of these measures for the period from 2012 to 2017. The first column of the table provides an explanation of the numbers provided in the following columns which contain figures for 2012-2017.

**Table 17. Number of penalties applied by the PBC**

	2012	2013	2014	2015	2016	2017
Number of penalized institutions	58	102	122	117	154	255
Number of penalized individuals	32	168	147	173	483	695
Aggregate Amount of penalties applied (RMB million Yuan)	13.09	21.54	27.42	26.87	49.61	107.4

**(Adapted from MER of the China, 2019, p. 134)**

In addition to the findings mentioned above, the assessors also noted the following in their evaluation:

The assessors doubt whether the sanctions available are effective, dissuasive and proportionate given their low scale and cap compared to the size and composition

of the financial sector in China, which includes four G-SIFIs (see further discussion in IO.3). No sanctions are applicable to designated DNFBPs (MER of China, 2019, p.134)

#### **4.3.5 The Republic of Tajikistan**

From this perspective, the Republic of Tajikistan can be viewed in the same way as China, that is, Tajikistan has not fully implemented the requirements for applying preventive measures for violation of AML/CFT legislation in FIs. However, in contrast to China, legislation in Tajikistan imposes sanctions in cases of identification of violations of AML/CFT legislation and AML/CFT legislation is established by law in the CoAO of the Republic of Tajikistan. However, serious weaknesses regarding the application of sanctions exist in the country (for more information see Chapter 4). In the mutual evaluation results, assessors made the following observations:

39. Sanctions for non-compliance with AML/CFT requirements are regularly applied against credit institutions, which is due to the broad sanctioning powers of Tajikistan's National Bank. Other FIs were not sanctioned due to the lack of appropriate authority and attention from other supervisors to the enforcement of compliance with AML/CFT requirements in their sector. Sanctions for AML/CFT violations were not used in respect of DNFBPs (MER of Tajikistan, 2018, p 8).

444. The Tajik law provides for liability of FIs and DNFBPs, including their officials and directors, for failure to comply with the AML/CFT Law. However, the sanctions provided for are not effective, proportionate or dissuasive. In addition, the range of sanctions is limited (MER of Tajikistan 2018, p 164).

According to the above mentioned outcomes, it is important to note that, the number of applied sanctions are depending on number of conducted audits in financial institutes. Therefore, the reviewed data among of five EAG countries shows that Peoples Republic of China and the Republic of Tajikistan didn't establish the effective regulation over all financial institutions. Moreover, there is no settled

requirement in AML/CFT Law of the Peoples Republic of China regarding the taking measures for non-compliance with AML/CFT legislation. Also, in case of the Republic of Tajikistan it is notable that AML/CFT supervision was conducted regularly in micro deposit and banking organization and measure for non-compliance with AML/CFT legislation was taken only toward these organizations. Due to this, it is possible to argue that the supervisory authorities of the Peoples Republic of China and the Republic of Tajikistan have the lack of the supervisory powers and the regulation of financial institutions is not with the line of the AML/CFT International Standards.

Additionally, AML/CFT supervisory authorities of the Republic of Belarus, the Russian Federation and the Kyrgyz Republic Russian Federation have wide powers to take measures in cases where violation of AML/CFT legislation is identified. Consequently, these countries could develop the effective mechanism of applying preventive measure and the Republic of Belarus, the Russian Federation regularly conducting AML/CFT audits in all type of financial institutions.

#### **4.4. Summary and observations**

In summary, in light of the detailed account regarding the powers of supervisory authorities presented above, especially the risk-based supervision and application of sanctions in five EAG countries, it is possible to argue that in all of these countries, gaps and weaknesses still exist. However, fundamental gaps can be observed in the AML/CFT system of the Peoples' Republic of China and the Republic of Tajikistan. The main shortcoming in this regard is that these countries did not establish FATF requirements in their national legislation completely. Also, a lack of understanding of FATF Standards by supervisory authorities, especially



regarding the risk-based approach, was identified. In addition, another hidden element that can be identified is the failure on the part of supervisory authorities to fulfil their responsibilities.

Therefore, despite minor shortcomings with their risk-based supervision mechanisms and preventive measures, the Republic of Belarus and Russian Federation can be used as examples of good practice by other EAG countries. Additionally, in the case of the Kyrgyz Republic it is notable that despite being rated as Largely Compliant, some serious weaknesses remain unsolved, specifically regarding the AML/CFT in DNFBPs.

Taking the above mentioned into account it is important to emphasize that the level of implementation of FATF Standards in every country influences the level of guarantee of their economic security. Thus, countries have to be prepared to implement these standards and present their financial system as safe and secure.

Next, this study turns to the case of the Republic of Tajikistan and presents detailed findings on the implementation of Supervisory Recommendations in the Republic of Tajikistan.

## **CHAPTER 5. THE LEVEL OF COMPLIANCE WITH THE SUPERVISORY RECOMMENDATIONS IN THE REPUBLIC OF TAJIKISTAN**

This chapter presents the data collected for analysis and discussion. The chapter is organized into four main sections based on patterns that emerged from the data. These include the supervision of FI's (in Section 5.1) issues of work experience (in Section 5.2), the challenge of conducting audits (Section 5.3) and finally the matter of sanctions and their application (Section 5.4).

In terms of the first four sections, the results primarily consider the implementation of the FATF Recommendations, especially Recommendations 26 (Regulation and supervision of financial institutes), 27 (Powers of supervision), 28 (Regulation and supervision of DNFBPs) and 35 (Sanctions) in the Republic of Tajikistan. The results and findings of the implementation of the abovementioned recommendations consist of data collected from interviews and secondary data from AML/CFT Mutual Evaluation Reports.

### **5.1. Supervision of Financial Institutions**

The AML/CFT system of the Republic of Tajikistan is regulated by law and the main laws are the AML/CFT/CPF Law, the Criminal Code, the Criminal Procedure Code, the Code of Administrative Offences, the Civil Code, the Law "On Banking", the Law "On State Registration of Legal Persons and Individual Entrepreneurs", the Law "On the Securities Market" and others. In this regard, the Financial Monitoring Department under the National Bank of Tajikistan (FMD) is designated as the competent authority in the AML/CFT regime. Therefore, the

FMD is responsible for the regulation and supervision of the AML/CFT system of the country and is tasked with the prevention of ML/TF threats. It can be categorized as an administrative type of FIU (MER, 2018).

**Table 18** summarizes the audits conducted by the FIU (that is the FMD of the National Bank of Tajikistan) on Financial Institutions (FIs) in the period 2010 to 2020. The types of financial institutions where AML/CFT audits were conducted are mentioned in the first column and the number of audits conducted on each FI during the period 2010-2020 is shown in the columns to the right of the table.

**Table 18. AML/CFT audits conducted on FIs during the period 2010-2020**

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020
<b>Banks (credit organizations)</b>	0	1	20	31	12	20	26	22	27	32	22
<b>Insurance companies</b>	0	0	0	0	0	0	0	0	2	2	1
<b>Notarial companies</b>	0	0	0	0	0	0	0	0	0	19	0
<b>Betting shop</b>	0	0	0	0	0	0	0	0	0	2	0
<b>Pawnshop</b>	0	0	0	0	0	0	0	0	0	2	0

As the table shows, AML/CFT audits starts from 2011 and they were regularly conducted only on credit organizations (Banks and MCOs). Later in 2018 this was extended, and the first audits of insurance companies were conducted. Additionally, in 2019, the FIU together with the Ministry of Finance and Ministry of Justice conducted several audits of notaries, companies, betting shops and pawnshops.

In this regard, the overview of information from MER of EAG countries shows the importance of regulation and supervision all type of financial institutions. For example, the information below presents the cases of money laundering through the insurance companies. The case studies were adapted from the Mutual Evaluation Reports of the Russian Federation and Republic of Belarus.

**Case 1. Identified case of money laundering and tax evasion through the insurance company in Russian Federation.**

In 2013, Rosfinmonitoring conducting strategic analysis of financial transaction reports and identified more than 2 300 reports in an amount of around RUB 42 billion. These transactions related to insurance companies and reinsurance contracts. As a result of Rosfinmonitoring analysis, it was suspected that it was an organised channel to transfer funds overseas. The scheme included loan payments into accounts of companies, controlled by the mastermind if the scheme – individual T –, and followed by transfers to insurance companies and subsequent transfer abroad within reinsurance contracts.

In parallel, LEAs were investigating a criminal case related to tax evasion by a company «E» and in co-operation with Rosfinmonitoring it identified that «E» was using cashing out services, provided by individual T. Individual T conducted illegal business activity, incl. cashing out for a fee, and received a criminal income in a total amount of more than RUB 450 million..

As a result, individual T was charged with illicit business activity (part 2 of CrC Article 171) and complicity to tax evasion (part 5 of CrC Article 33 and part 2 of CrC Article 199).

(Adapted from MER of the Russian Federation, 2019, p. 58)

## **Case 2. Identified case of the insurance fraud in the Republic of Belarus**

The citizen of Belarus was a member of an organized criminal group, which for a long time in 2004-2009 was engaged in criminal activities related to the purchase of cars obtained by criminal means, forgery of registration documents and their subsequent sale in the territory of Belarus. The exchange of information with regard to this criminal group was carried out through Interpol by sending requests to various countries where the citizen of Belarus may be located, including Germany and Lithuania. This organized group was engaged in insurance fraud (article 209 part 3 of the Criminal Code), staging and processing fictitious traffic accidents with these vehicles, which allowed to illegally receive insurance benefits in various insurance companies in Belarus. Subsequently, members of an organized criminal group executed various financial transactions related to the purchase and sale of cars in the territory of Belarus with a view to distorting the sources of their purchase and the nature of their origin (Article 235 part 2 of the Criminal Code).

**(Adapted from MER of the Republic of Belarus, 2019, p. 147)**

Considering the above money laundering cases presented above, it is possible to make the case that the regulation and supervision of financial institutions and the strategic analysis of the activities of these institutions may affect the level of money laundering and economic security of the country. Therefore, countries have a responsibility to implement the FATF Standards and to enhance the power of AML/CFT supervisors.

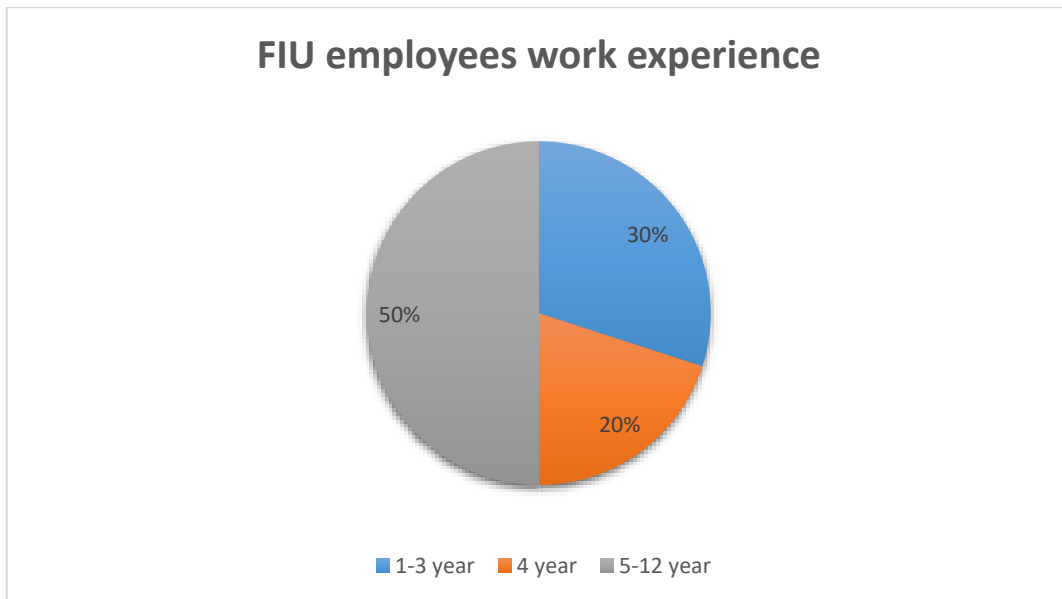
In addition to the shortcomings identified in auditing the financial institutions, the other deficiency in the AML/CFT regulations is the issue of sanctions. According to the findings of this study, sanctions for non-compliance with the AML/CFT requirements were applied only against credit and micro deposit organizations. The issue of sanctions will be discussed further in Section 4.4 below.

### **5.2. Limited Work Experience of FIU staff**

The findings from the analysis of the interview transcripts reveal that the limited work experience of FIU staff is also an issue. According to the data collected, the FMD now has 22 employees who work in 5 Divisions and a Training Center. After receiving approval, the researcher conducted interviews with the 20

above-mentioned FMD staff. The results show that 50% of interview respondents did not participate in the second round of AML/CFT Mutual Evaluations for the Republic of Tajikistan. **Figure 1** summarizes the work experience of the respondents.

**Figure 1. Respondents Work Experience**



Considering the data and the results summarized in **Figure 1**, it is notable that 50% of FMD employees have fewer than 5 years' work experience in the sector. In this regard, it is possible to argue that with limited work experience it is difficult for these employees to possess sufficient knowledge of the AML/CFT requirements in terms of auditing and this may affect the implementation of Supervisory Recommendations. Supervision is one of the key components of FATF Recommendations. A good evaluation of AML/CFT supervision can demonstrate that a particular country has installed an enhanced AML/CFT regime. Also, the supervisory regime of the country can be effective if supervisors have ample knowledge and can identify, maintain, and understand the ML/TF risks in FI's and

other sectors and between different sectors and types of institutions, and between individual institutions (FATF, 2015). As the FAFT explains:

*AML/CFT supervisors assess institution's policies, procedures and controls for identifying and managing ML/TF risk and take remedial action where appropriate. It is not a "tick the box" approach; it requires judgement in understanding the characteristics and situation of every financial institution. (FATF, 2015)*

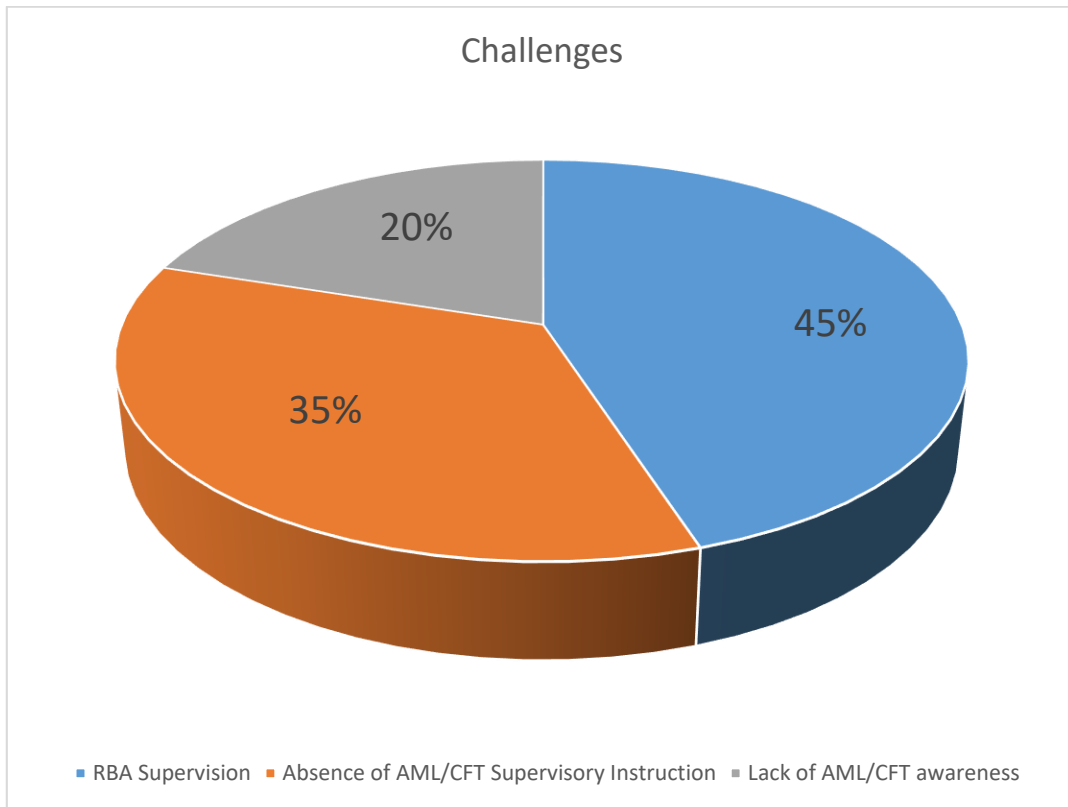
In this regard, work experience and a good understanding of the AML/CFT regime plays a significant role in conducting audits in FI's. Moreover, it may also have a negative effect on countries during their AML/CFT Mutual Evaluation.

### **5.3. Challenges in Conducting Audits in FI's Especially using RBA Requirements**

The mechanisms for AML/CFT supervision and regulation of financial institutions need to be periodically improved in order to be able to mitigate and combat the risks associated with the ML/TF with the aim of ensuring economic security and stability in the country. Therefore, it is important to identify the challenges in AML/CFT regulation and **Figure 2** summarizes the findings from the interview transcripts regarding the challenges in AML/CFT regulation. According to the results of the analysis of the interview transcripts the auditors mainly faced three challenges while conducting audits in FI's. The first one is conducting supervision in accordance with risk-based approaches. The second is the absence of AML/CFT supervision instructions or guidelines and the third is the lack of AML/CFT awareness. These three challenges are summarized in the figure below,

in blue, grey and orange color and corresponding definitions are provided at the bottom.

**Figure 2. Challenges that supervisors and regulators while conducting audits of FIs**



As **Figure 2** shows, 45% of respondents faced challenges with the risk-based approach to supervision (see the blue portion of the chart). The actual answers of some respondents to the interview question on what challenges they faced in conducting inspections of financial institutions are summarized below.

- The main challenge was to start conducting audits in FI’s using a RBA. However, we are making our first steps in this regard”
- “The first one was conducting audits without any Inspection Instructions and the other one auditing in accordance with RBA requirements...”
- “The main challenge was to conduct audits in accordance with risk based requirements...”



In this regard, it should be mentioned that one of the main responsibilities of supervisors is to understand, identify and manage the ML/TF risks of each sector. Moreover, conducting RBA supervision is the Core Principle of the Supervisory Recommendations, as outlined in the following FAFT recommendations:

Recommendation 26 (R.26) requires risk-based supervision of financial institutions, Recommendation 28 (R.28) requires the risk-based supervision or monitoring of DNFBPs and Recommendation 15 (R.15) requires the risk-based supervision of or monitoring of VASPs. 4 INR 15, 26, and 28 recommend that supervisors should allocate their supervisory resources based on risk. This requires supervisors to understand the ML/TF risk in their jurisdiction, sector, and entities and have onsite and off-site access to all information relevant to those risks (FATF, 2021).

In 2018 during the 2<sup>nd</sup> round of Mutual Evaluation of the Republic of Tajikistan experts assessed the implementation of the Core Principle of Supervisory Recommendations in the country and by the end of evaluation they noted the following:

333. Tajikistan has designated supervisors for FIs. In addition, the Tajik law requires all FI institutions to be licensed. Notably, Tajikistan has taken robust measures to prevent criminals and their associates from holding a controlling interest or management function in FIs. However, there are serious weaknesses in the supervisory regime, in particular, the regulation and **supervision are not in line with the Core Principles, and supervision is not based on the RBA** (MER, 2018 p. 150)

Additionally, in response to the interview question on “Do you conduct audits of financial institutes using a risk-based approach according to the FATF

Recommendations”, the majority of respondents answered that related documents are already adopted; however, they have not started to use them in practice yet (see the notes from some respondents below).

- “With the aim of conducting audits in FIs according to the FATF Recommendations (specifically **using the risk-based approach**) **2 documents were adopted** including a “Risk Assessment Matrix for supervisory authorities” and a “Risk Assessment Process for reporting entities”. Moreover, the User Guide for these **documents is currently being drafted.** “
- All the necessary documents and instructions are ready and in the near future **we are planning to start** auditing FI’s according to the FATF Standards.
- The Republic of Tajikistan is **in the stage of improving** AML/CFT inspections. Regarding auditing using the ML/TF risks we prepared special documents and we are **going to start audits** in accordance with them.

Additionally, one of the key findings of the assessors is that “The supervisors do not apply a risk-based approach in the supervisory activity. Besides, the Ministry of Finance has no power to conduct on-site and off-site inspections of AML/CFT. No inspections on compliance with AML/CFT legislation of lawyers, independent legal professionals, and real estate dealers were conducted”. Therefore, they recommended that “Supervisors should intensify their work with ML/TF risks, including by raising reporting entities' awareness of their risks and applying a risk-based approach to supervision over their activities.”

Consequently, the point should be made that the rate of Recommendation 26 strictly depends on the implementation of the above-mentioned Core Principles

and due to gaps that existed in compliance with this principle in the Republic of Tajikistan, experts rated the implementation of this Recommendation as **partially compliant** (MER, 2018).

Another challenge for the supervisors is the absence of AML/CFT supervision instruction. In this regard, 35% of respondents agree that they are facing difficulties in conducting audits in FI's without having special guidelines on the instructions and 15% of respondents mentioned the lack of AML/CFT awareness among FI staff (see below for remarks from some of the interviews).

- “The main **challenge is** that there are **no Guidelines** for conducting AML/CFT inspections. However, with the aim of solving this problem nowadays the FIU of Tajikistan **prepared the Guidelines** for conducting inspections and they are **currently under consideration**. Also, the **Handbook** of the AML/CFT Inspection Manual for supervisory authorities **will be approved** at an early date”.
- “According to the part 8 of Article 12 of the AML/CFT Law FIU of Tajikistan, together with the supervisory authorities, conduct inspections of the reporting entities. However, it should be noted that the **Guidelines for** conducting the **inspections** are currently **under consideration** and they are scheduled to be approved in the first half of this year. Also, the **Handbook** on the AML/CFT Inspection Manual for supervisory authorities is **now being finalized**.”
- “The main **challenge is** the awareness of FATF Recommendations, AML/CFT legislation and related requirements among the FI's staff. Due to **the lack of knowledge of the system** and requirements we had some difficulties during the audits.”

According to the abovementioned remarks it is possible to argue that some serious weaknesses in AML/CFT supervision and regulation system remain for the country. In order to conduct mandatory financial monitoring in financial

institutions, supervisors must establish clear qualitative and quantitative criteria and for this there must be a regulatory framework such as instructions or guidelines on which the inspector can rely during his activities. The absence of this kind of regulatory framework may have a negative effect on the quantity and the quality of audits in FIs which can lead to weaknesses in the economic security of the country.

#### **5.4. Sanctions**

FATF standards require the adoption of effective, proportionate, dissuasive sanctions that can be used while working with financial institutions which are not compliant with the requirements of AML/CFT legislation. Moreover, a strong system of sanctions is essential to interrupt anti-money laundering/terrorist financing activities. However, the main purpose of applying sanctions is not to punish the financial institutions but to address deficiencies. Therefore, only the supervisor can determine whether corrective action is needed or not. Also, financial institutions should be aware that non-compliance with appropriate anti-money laundering/terrorist financing procedures may have a negative effect on their activities. Especially it may result in legal and financial liabilities that could damage their reputation and profitability.

The issue of sanctions is addressed in various FATF Recommendations, and they require that countries must provide criminal, civil, or administrative sanctions that are effective, adequate and dissuasive towards non-compliance with the requirements of anti-money laundering/terrorist financing. In this regard, according to the following requirement of FATF Standards, supervisory authorities should have the power to apply adequate administrative sanctions in cases where violation of anti-money laundering/terrorist financing requirements are identified. Because

of this, the implementation of the above-mentioned requirements can be evaluated not only by FATF or FSRBs but also the World Bank and International Monetary Fund in line with the Financial Sector Assessment Program.

In addition, besides their formal implementation, the full and proper effectiveness of the Standards is going to be evaluated. In this regard, not only the completeness of the scope of measures is going to be assessed but also the main indicators such as, for example, the number of sanctions applied to financial institutions, which indicate the effectiveness of the system.

In this regard, the evaluation of the AML/CFT system of the Republic of Tajikistan by experts in 2018 provided the following recommendations (see **Table 19**):

**Table 19. The results of MER related to sanctions (adapted from the Mutual Evaluation Report of the Republic of Tajikistan, 2018.)**

<b>Recommendation</b>	<b>Rating</b>	<b>Factor(s) underlying the rating</b>
3. Money laundering offence	Largely Compliant (LC)	Sanctions provided for legal entities are not fully proportionate and dissuasive
5. Terrorist financing offence	LC	Sanctions provided for legal entities are not fully proportionate and dissuasive.
24. Transparency and beneficial ownership of legal arrangements	LC	The sanctions against legal persons provided for by Tajik law cannot be considered effective or dissuasive;
27. Powers of supervisors	LC	Financial sector supervisors other than the NB lack the powers to impose sanctions for non-compliance with AML/CFT requirements
28. Regulation and supervision of DNFBPs	Partly Compliant (PC)	Supervisors are not authorized to apply sanctions against DNFBPs for failure to

		comply with the AML/CFT Law;
35. Sanctions	PC	A broad range of effective, proportionate and dissuasive sanctions against the senior management of FIs (except for credit institutions) and DNFBPs are absent.

**Table 19** shows that the rating of the implementation of the five FATF Recommendations is strictly dependent on the full realization of and compliance with the requirements of sanctions.

In addition to the results of MER provided above, Table 20 summarizes the findings from data collected via interviews, FIU annual reports and the MER of Tajikistan. This table includes data related to sanctions imposed on financial institutions (banks and micro deposit organizations) specifically:

- remedial instructions issued (i.e., decrees);
- applied disciplinary sanctions, including the issuance of reprimands, warnings, and dismissals of employees at credit institutions;
- the total amount of fines as a result of applied administrative sanctions in credit and micro deposit organizations and;
- the number of administrative offense reports (sanctions imposed by the National Bank of Tajikistan as a result of on-site and off-site audits by the Financial Monitoring Department).

In each table the left-most column shows the type of measure and the columns to the right show the number of measures by year from 2010 to 2020.

**Table 20. Sanctions applied to identified violations in financial institutions of the Republic of Tajikistan.**

Type of sanctions	YEARS										
	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020
<b>Disciplinary sanctions (reprimands, warnings, and dismissals of employees )</b>	0	0	0	0	0	8	13	18	40	7	0
<b>Number of Remedial Instructions</b>	0	0	0	35	0	4	42	15	23	22	
<b>Total amount of fines (in somoni)</b>	0	0	0	0	0	2 600 000	1 600 000	1 615 000	640 000	175 000	
<b>Number of administrative offence reports</b>	0	0	0	0	0	0	1	5	11	1	2

As the table shows the sanctions imposed on financial institutions began from 2013 and were applied only against credit and micro deposit organizations by the National Bank of Tajikistan as a result of on-site and off-site audits by the Financial Monitoring Department (FIU). Therefore, during the evaluation of the AML/CFT system of the country, the lack of sanctions or inadequate application of them can be viewed as an important reason for assessors to conclude that the country is not meeting international requirements. As a result, the country can be assigned a rating of “partly compliant” or “not compliant” with the implementation of recommendations related to the sanctions.

In this way, in the second Mutual Evaluation of the Republic of Tajikistan, evaluators rated Recommendation 35 as **partly compliant**. It is possible to argue, then, that due to the absence of applied sanctions in financial institutions other than credit and micro deposit organizations, it is impossible to rate the implementation of International Standards concerning the violation of AML/CFT requirements as effective. Therefore, it is also possible to observe a lack of supervisory power among the supervisory authorities other than National Bank of Tajikistan (including the FIU).



## **CHAPTER 6. CONCLUSION**

In conclusion, this chapter will now return to consider the research questions and hypotheses of this study, as set out in Chapter 1 (see p.17). With reference to the findings, it will offer answers to each of the research questions in turn, followed by an assessment of the hypotheses. The chapter will be organized broadly into three main sections, beginning with the objectives and hypotheses (as outlined above), followed by the practical implications of the results and how these might inform future policy directions in the Republic of Tajikistan and finally, it will offer some possible directions for future research in this area.

### **6.1. Conclusions on the research objectives**

Turning firstly to the aims of this study, the overall objective of this research was to examine the supervision and regulation of financial institutions in terms of AML/CFT in the Republic of Tajikistan, especially risk-based supervision of these institutions, and the measures employed to deal with violations of AML/CFT legislation in those institutions.

Considering the first research question (1), “To what extent is the mechanism of risk-based supervision for financial institutions established?”, the findings show that such mechanisms have not yet been established in the Republic of Tajikistan and that a lack of understanding of FATF Standards by supervisory authorities exists, especially regarding the risk-based approach. In the comparative study in Chapter 4, the same issue was identified in the Peoples Republic of China. Additionally, the related issue of the absence of implementation of fundamental

requirements regarding the risk-based supervision and approach was also observed. What this means, then, is that mechanisms for risk-based supervision of financial institutions are not yet established and the government of the Republic of Tajikistan needs to make further progress in this area.

In terms of the second research question (2), that is, “In what ways are the supervisors in Tajikistan intensifying their work with imposing sanctions for violations of AML/CFT legislation?”, the results show that sanctions are being applied on a limited scale to some organizations in Tajikistan but not others. For instance, AML/CFT audits have been regularly conducted on credit and micro deposit organizations and sanctions have also been applied to these organizations. Thus, more progress needs to be made in this area and supervisors need to expand their work to cover more organizations and financial institutions. Moreover, Tajikistan is prepared guidelines for conducting inspections according to the Handbook of the AML/CFT Inspection Manual for supervisory authorities, however, at the time interviews were conducted for this study, these documents were not adopted, therefore, it is impossible to assess their effectiveness at present.

As for the third research question (3), “To what extent is Tajikistan’s AML/CFT legislative and institutional capacity effective in regulating and supervising financial institutions?”, based on the findings of this research, it is possible to conclude that serious weaknesses related to the provision of effective AML/CFT regulation and supervision of financial institutions remain in the Republic of Tajikistan. Specifically, the main weakness is that the core principle of Recommendation 26 of FAFT Standards has not been implemented. Overall, then, it would appear that Tajikistan is making progress with implementing FAFT standards and AML/CFT policies, but more work lies ahead in terms of

strengthening supervisory and legislative mechanisms in relation to AML/CFT in the country.

## **6.2. Conclusions on the hypotheses**

Turning next to the research hypotheses, to what extent did the findings presented in Chapters 4 and 5 confirm the hypotheses proposed in Chapter 1 of this study (see 17) In terms of the first hypothesis, that is, " The mechanism of risk-based supervision is not established in the Republic of Tajikistan", the findings indicate that this hypothesis was proved correct. Based on the findings, Tajikistan is making progress with its efforts to establish risk-based supervision of financial institutions by adopting special instructions and establishing these requirements in legislation, however, major shortcomings for implementing them in practice can be observed.

For example, the National Bank of the Republic of Belarus started to conduct risk-based audits from 2014 and from 2018 after updating the requirements for conducting the risk-based supervision and established the risk-based mechanism in the national legislation of the country. Following this, other supervisory authorities also began to implement the requirements in the organizations under their control. Unlike Belarus, however, the Republic of Tajikistan did not establish a requirement for the risk-based supervision of financial institutions in national legislation and has not done so yet. Furthermore, the Republic of Belarus and the Russian Federation presented well-developed mechanisms for providing statistics regarding all types of AML/CFT activities which shows the effectiveness of the AML/CFT systems in these countries. Therefore, in case of the Republic of

Tajikistan, it is difficult to obtain an overview of the statistics generated with regard to AML/CFT activities.

The second hypothesis suggested that " The supervisory authorities have lack of power for applying sanctions for violation of AML/CFT legislation and they imposed only toward credit and micro deposit organizations" As the results showed, this hypothesis was also proved correct. For instance, according to the findings, only the National Bank of Tajikistan applied sanctions for non-compliance toward credit and micro-deposit organizations. Therefore, the lack of action with imposing sanctions and weak supervisory power remains an issue for supervisory authorities in the country.

### **6.3. Recommendations**

The results of this research demonstrates the importance of implementing FATF Standards in the countries reviewed, especially the risk-based supervision of financial institutions and the establishment of preventive measures for non-compliance with AML/CFT regulations in the organizations mentioned. Moreover, the presence of some gaps and shortcomings in the powers of supervisory authorities in the Republic of Tajikistan were observed. In light of these findings, three main recommendations are offered as follows.

Firstly, in the case of the implementation of a risk-based approach, the FATF adopted various documents and guidance materials for countries which allow the flexible application of a risk-based approach. The guidelines outlined the requirements of risk-based supervision and provided the mechanism with structure. By acting in accordance with them, it will be possible to allocate available resources

and direct efforts towards preventive measures in areas of high ML/TF risk. In this regard, this study recommends the Republic of Tajikistan implement the following FATF-adopted documents as a form of good practice with the aim of addressing the identified shortcomings:

- Guidance for applying a Risk-Based Approach to Supervision;
- Specific Risk Factors in the Laundering of Proceeds of Corruption;
- Guidance for a Risk-Based Approach: Prepaid Cards, Mobile Payments and Internet-Based Payment Services;
- Risk-Based Approach Guidance for the Banking Sector;
- Guidance for a Risk-Based Approach to Virtual Currencies;
- Guidance for a Risk-Based Approach for Money or Value Transfer Services;
- Guidance on Correspondent Banking Services.

Furthermore, based on the results of comparative analysis in Chapter 4, this study recommends that the Republic of Tajikistan use the established mechanisms of the Republic of Belarus and the Russian Federation as examples of good practice.

Secondly, in order to demonstrate effective regulation and supervision of financial institutions, it is important for all supervisory authorities to have a publicly accessible database to compile, store, and maintain statistics and other qualitative information on AML/CFT supervision including risk-based supervision and imposed sanctions for violation of AML/CFT legislation.

Risk-based supervision is a challenge for all supervisors and the main responsibility of supervisors is to be aware of related requirements and fully understand the FATF Standards. To increase the AML/CFT awareness of the

supervisory authorities and encourage them to fulfill their responsibilities, this study suggests that the Republic of Tajikistan provide mandatory and regular training on procedures to pass exams and assessments. This study recommends, for instance, that an FIU Training Center be established to strengthen cooperation with the FATF and EAG. The aim of this Center would be to foster the development of AML/CFT professionals and trainers who can provide courses in Tajikistan and to raise the level of AML/CFT knowledge among supervisory authorities.

Finally, these recommendations may provide some solutions to enhance the AML/CFT system and encourage the supervisory authorities to develop mechanisms and good practices and serve as a point of reference for other countries with similar shortcomings. Such recommendations can contribute to ensuring the economic security of countries and safeguard financial institutions from the risks of money laundering and terrorism financing. In addition, supervisors, through knowledge of the ML/TF risks in their sector, can mitigate and address them effectively, an important aspect in the effective regulation and supervision of financial institutions.

#### **6.4. Suggested directions for future research**

Considering the results of this research, the following topics suggest themselves as possible directions for future research in the area of AML/CFT.

Firstly, due to the lack of research in this field, it would be useful to explore Tajikistan's AML/CFT system more deeply. For instance, research could be conducted that examines the linkage between various organizations and institutions in their actual implementation of FATF Standards. This type of exploration could

involve examining financial institutions, cooperation between supervisory authorities and financial institutions and cooperation among the supervisory authorities.

A second avenue of research might include identifying the impact of the AML/CFT system and the implementation of FATF Standards with reference to different economic sectors and a larger dataset. This aim could be achieved by employing a combination of qualitative and quantitative methods. By such means, it may be possible to obtain a more detailed and up-to-the minute account of the implementation and effect of AML/CFT systems on the economic performance of various sectors or on the country as a whole. Additionally, by employing a larger dataset, it may be possible to offset some of the limitations faced in the present study, such as the effects of bias and short answers by interviewees. Some topics that suggest themselves in this regard are the influence of AML/CFT compliance on foreign direct investment, or the advantages and disadvantages imposed by implementation of FATF Standards on the economy of Tajikistan.

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# APPENDIX 1

## Research Questionnaire

### Commitment to Privacy and Confidentiality

All responses to this questionnaire will remain private and confidential and will only be viewed by the researcher and her supervisors at Ritsumeikan Asia Pacific University. Excerpts from the responses may be used in the researcher's thesis or related presentations, but any references to names and identities will be removed and anonymized to ensure privacy.

Interviewee:

Date:

1. In your opinion, how well is the AML/CFT system working in Tajikistan?
  - a. Very well
  - b. Somewhat well
  - c. Not so well
  - d. Poorly

Please explain your answer: [For example: *a. Very well, because....*]

2. Did you participate in the Republic of Tajikistan's AML/CFT mutual evaluation?
  - a. Yes [Go on to Q3 below]
  - a. No. [Go on to Q4 below]
3. [YES] Please explain your role in the mutual evaluation. [Type your answer here]

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4. [NO] What is your opinion about mutual evaluation? [Type your answer here]

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5. To what extent are the requirements of Recommendations 26-29 (see key below) implemented at the required level in the Republic of Tajikistan?
  - a. Very well
  - b. Somewhat well
  - c. Not so well
  - d. Poorly

Please explain your answer: [For example: *a. Very well, because....*]

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### Key to Recommendations:

26 (Regulation and supervision of financial institutes),

27 (Powers of supervision),

28 (Regulation and supervision of DNFBPs),  
29 (Financial Intelligence Unit)

6. What kinds of financial institutions have supervisory bodies?  
[Type your answer here]

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7. What challenges do you face in conducting inspections of financial institutions?  
[Type your answer here]

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8. Do you conduct audits of financial institutes using a risk-based approach according to the FATF Recommendations?

- a. Yes
- b. No

Please explain your answer: [For example: *a. Yes, ...*]

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9. Are sanctions imposed by supervisory authorities for violations of the AML/CFT Law?

- b. Yes
- c. No

If YES, please provide details:

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If NO, please comment on why sanctions are not imposed.

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10. Are all supervisory authorities empowered to apply sanctions when they identify violations of the AML/CFT Law?

- d. Yes
- e. No

If YES, please provide details:

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If NO, please comment on why they are not so empowered.

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## APPENDIX 2

Code	Description
<b>VW</b>	The AML/CFT system works very well
<b>LGFWK</b>	Legal Framework
<b>MECH IMP</b>	The country has a mechanism for implementing the AML/CFT
<b>ROB MECH</b>	The country created a robust AML/CFT mechanism
<b>FIU Staff</b>	Participated in Mutual Evaluation as Financial Intelligence Unit staff
<b>FATF OBJ</b>	Mutual evaluation is one of the main objectives of FATF
<b>CNTR ASSES</b>	Mutual evaluation is the AML/CFT country assessment
<b>FATF RESP</b>	Mutual evaluation is the responsibility of FATF
<b>ME RATING</b>	Rating of recommendations from Mutual Evaluation Report
<b>ALL FI's</b>	All of the Financial institutions have the supervisory bodies
<b>INSP GUIDE</b>	The main challenge is that there are no inspection guidelines on AML/CFT
<b>INSP INSTR</b>	The difficulty is conducting AML/CFT audit without Instructions
<b>RBA INSP</b>	The challenge is conducting audits using a risk-based approach
<b>AML/CFT AWNS</b>	The challenge is that not all FI's are aware of the AML/CFT requirements
<b>IN PROG</b>	FIU is going to start conducting audits using an AML/CFT risk-based approach
<b>IMPR PLCY</b>	FIU is improving its audit policy regarding RBA
<b>FIU DATA</b>	Data from the FIU annual report