

**Rethinking the Meaning of a Politically Exposed Person to Promote Substantive
Compliance of the Financial Action Task Force Standards**

By

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ABSTRACT

This dissertation explores whether there is a need for a broader definition of Politically Exposed Persons (PEPs). It aims to enhance understanding of PEPs to improve countries' abilities to substantially comply with the Financial Action Task Force (FATF) standards. The dissertation observes that the current PEP definition is deemed too narrow, thereby hindering substantial compliance with the FATF standards. It highlights the need to broaden the scope of PEPs beyond natural persons to encompass legal entities, similar to the EU model implemented in the UK.

The paper presents a brief comparative analysis of the Anti-Money Laundering, Counter-Terrorism Financing, and financing of proliferation of weapons of mass destruction (AML/CTF) regimes of the FATF, South Africa, the EU, and the UK concerning PEPs. It considers Recommendation 12 of the FATF, Mutual Evaluation Reports, domestic legislation of the respective jurisdictions, financial intelligence units' guidelines and international standard-setting bodies like Wolfsberg Group and Basel Committee on Banking Supervision and international instruments.

The comparison reveals that the fundamental element of a PEP being a natural person is too restrictive, and thus ineffective in combatting ML/TF and hinders national efforts by countries like South Africa to promote substantive compliance with the FATF standards. Therefore, this paper suggests ways to respond to this and other challenges. It suggests that a broader definition of PEPs be adopted by the FATF on an international level and by South Africa, incorporating legal entities in the definition of PEPs to better comply with FATF AML/CTF standards.

LIST OF ACRONYMS

AML:	Anti-Money Laundering
AML/CFT:	Anti Money Laundering/Counter-terrorism financing
CTF:	Counter Financing of terrorism
CDD:	Customer Due Diligence
ESAAMLG:	Eastern and Southern African Anti-Money Laundering Group
EDD:	Enhanced Due Diligence
EU:	European Union
FATF:	Financial Action Task Force
ML/TF:	Money Laundering/ Terrorism Financing
PEP:	Politically Exposed Person
PEE:	Politically Exposed Entities
PIP:	Prominent Influential Person
UK:	United Kingdom

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CHAPTER 1 INTRODUCTION

1.1. BACKGROUND TO THE STUDY

Following the 2001 terrorist attacks on the United States, there has been widespread acceptance and global consensus on the importance of the Financial Action Task Force (FATF) standards. To provide context, the FATF is an international organisation that functions independently to create and maintain regulations to safeguard the global financial system from money laundering, terrorism financing, and financing the proliferation of weapons of mass destruction (AML/CTF).¹ It was created in 1989 during the G-7 Summit in Paris.²

The FATF standards originated from a report the FATF issued at its inception that contained Forty Recommendations initially designed to combat money laundering (ML) from drug trafficking.³ They subsequently underwent various revisions over the years.⁴ To begin with, in 1996 there was a revision to broaden the FATF's mandate to go beyond ML. Thereafter, in 2001, post the US terrorist attacks, eight Special Recommendations were issued by the FATF on terrorist financing (TF), following which a ninth Special Resolution was added.⁵ Furthermore, there was another revision in 2003, which was aimed at keeping up with the evolution of the patterns and the new techniques in ML/TF.⁶ The FATF updated its recommendations after taking into account the necessity to identify Politically Exposed Persons (PEPs), given the clear relationship between corruption and ML.⁷ Finally, in 2012, the Recommendations, the interpretive notes and the

¹ Financial Action Task Force available at <https://www.fatf-gafi.org/en/the-fatf/who-we-are.html> accessed on 23.06.2023.

² Louis de Koker, Manet Bason, John Symington, et al *Money Laundering and Terror Financing: Law and Compliance in South Africa* (2023) 11.

³ K.E. Davis 'The financial war on terrorism' in V.V Ramraj et al *Global Anti-Terrorist Law & Policy* (2009) 179--198.

⁴ Louis de Koker, Manet Bason, John Symington et al op cit note 2 at 11--12.

⁵ Ibid at 11.

⁶ FATF on Money Laundering 2003 Recommendations available at <https://www.fatf-gafi.org/content/dam/fatf-gafi/recommendations/FATF%20Recommendations%202003.pdf> accessed on 26.11.2023 (FATF Recommendation, 2003).

⁷ Jackie Johnson 'Little enthusiasm for enhanced CDD of the politically connected' (2008) 11 *JMLC* 291 at 292.

glossary made by the FATF were legislated into a single code known as ‘Forty Recommendations’.⁸ Thus, the Forty Recommendations, also known as the ‘FATF standards’ consist of interpretive notes, a glossary, and recommendations.⁹ PEP regulation is contained in Recommendation 12 therein.¹⁰

The FATF urge countries who have membership to create policies to combat ML/TF and most countries have committed to establishing their AML/CTF policies,¹¹ as well as implementing the same in their national legal systems.¹² In this regard, the FATF standards function as a model law for countries to adopt within their domestic jurisdictions to create policies to combat ML/TF, which includes regulation on how to identify and monitor PEPs.¹³ The identification and monitoring of PEPs play a significant role in the prevention of ML. This is based on the understanding that PEPs, due to their influential public positions, can be more susceptible to corruption and may have direct involvement in illicit ML activities.¹⁴ On this account, Recommendation 12 of the FATF mandates financial institutions to identify PEP customers since they are more prone to conduct financial crimes.¹⁵ Thus, PEP customers should undergo Enhanced Due Diligence (EDD).¹⁶

⁸ FATF Recommendations ‘international standards on combating money laundering and the financing of terrorism & proliferation’ available at <https://www.fatf-gafi.org/content/dam/fatf-gafi/recommendations/FATF%20Recommendations%202012.pdf.coredownload.inline.pdf> accessed on 12.06.2023 (FATF Recommendations, 2012).

⁹ Ibid.

¹⁰ Recommendation 12 of the FATF Recommendations, 2012 at 16.

¹¹ Michael Pisa ‘Does the Financial Action Task Force (FATF) Help or Hinder Financial Inclusion? A Study of FATF Mutual Evaluation Reports’ available at *Does the Financial Action Task Force (FATF) Help or Hinder Financial Inclusion? A Study of FATF Mutual Evaluation Reports (cgdev.org)* accessed on 04.05.2023.

¹² Nicholas W. Turner ‘The Financial Action Task Force: International Regulatory Convergence Through Soft Law’ (2015) 59 *New York Law School Law Review* 547 at 548.

¹³ Joel Harry Clavero Suntura, Piedad Maribel Rosero, Gloria Esperanza Aragon Cuamacas ‘Challenges of identifying and monitoring politically exposed persons (PEPs) in Latin America (2021) 24 *JMLC* 268 at 268.

¹⁴ Ibid at 268.

¹⁵ FATF Guidance ‘Politically Exposed Persons (Recommendations 12 and 22)’ available at <https://www.fatf-gafi.org/en/publications/Fatfrecommendations/Peps-r12-r22.html> accessed on 12.06.2023. (FATF Guidance).

¹⁶ Recommendation 12 of the FATF Recommendations, 2012 at 16.

Regarding whom is considered a PEP, it is individuals with prominent public functions, their known close associates and their family members are regarded as PEPs.¹⁷ Importantly, there exists a universal consensus that a PEP is a natural person, although PEPs are defined differently by several international standard-makers and international agencies.¹⁸ For instance, the FATF defines PEPs in the following manner:

‘*Foreign PEPs* are individuals who are or have been entrusted with prominent public functions by a foreign country, for example,

- Heads of State or government,
- senior politicians, senior government,
- judicial or military officials,
- senior executives of state-owned corporations, and
- high-ranked political party officials.

Domestic PEPs are individuals who are or have been entrusted domestically with prominent public functions.’¹⁹

The examples remain consistent with those provided earlier for domestic PEPs, and a third category of PEPs is delineated below:

‘Persons who are or have been entrusted with a prominent function by an *international organisation* refers to members of senior management, i.e.

- directors, deputy directors and members of the board or equivalent functions.’²⁰

The FATF establishes 3 categories of PEPs: foreign, domestic, and international PEPs.²¹ Notably, it designates PEPs as individuals, thereby implicitly referring to natural persons.²²

¹⁷ Jackie Johnson op cit note 7 at 292.

¹⁸ Ramandeep Kaur Chhina ‘Implementation of the concept of politically exposed persons (PEPs) in India’ (2017) 20 *JMLC* 89 at 91--93; Ibid at 292.

¹⁹ Terms and definitions of the 2012 FATF Recommendations available at <https://www.fatf-gafi.org/content/dam/fatf-gafi/recommendations/FATF%20Recommendations%202012.pdf.coredownload.inline.pdf> accessed on 14/07/2024 at 133.

²⁰ Ibid.

²¹ Ibid.

²² FATF Guidance.

The European Union (EU)'s Third Anti-Money Laundering Directive (AMLD)²³ defines a PEP as follows:

“Politically exposed persons’ means natural persons who are or have been entrusted with prominent public functions and immediate family members, or persons known to be close associates, of such persons”.²⁴

This definition was adopted in the 2006 Joint Money Laundering Steering Group (JMLSG) guidance and examples include:

- ‘heads of state,
- senior politicians, senior government,
- judicial or military officials,
- senior executives of state-owned enterprises, and
- high-ranked political party officials.’²⁵

Additionally, according to the Wolfsberg Group,²⁶ which is an industry regulatory body responsible for developing AML/CTF standards for the private banking industry, examples of specific functions that would likely give rise to PEP status include:

- ‘Heads of State, heads of government and ministers,
- Senior judicial officials who sit on bodies whose decisions are not subject to further appeal,
- Heads and other high-ranking officers holding senior positions in the armed forces,
- Members of ruling royal families with governing responsibilities,
- Senior executives of state-owned enterprises, where the state-owned enterprise has genuine economic or political importance, and
- Senior officials of major political parties.’²⁷

The prevailing international consensus is that PEPs primarily refer to natural persons. This aligns with the Wolfsberg Group’s reaffirmation that a fundamental element for defining a PEP is

²³ EU Directive 2005/60/EC of the European Parliament and of the council (26/10/2005) (hereinafter EU Third AMLD)

²⁴ Article 3(8) of the EU Third AMLD.

²⁵ Section 5.6.12 Joint Money Laundering Steering Group, 2006.

²⁶ Refer to 1.8.2.4 for a thorough discussion of the Wolfsberg Group.

²⁷ The Wolfsberg Group ‘Wolfsberg guidance on Politically Exposed Person(“PEP”)’ available at *Wolfsberg Frequently Asked Questions (“FAQ’s”) on (wolfsberg-principles.com)*, accessed on 05/03/2023.

its status as a natural person.²⁸ This is particularly evident from the examples of listed roles that are likely to result in PEP status. However, the EU has adopted a different approach. The EU expanded the definition of PEPs in its Third AMLD to include, among other things, any legal entity whose beneficial owner is a PEP's family member. It maintained the same PEP scope in its Fourth AMLD.²⁹ It is for this reason that the EU's definition of a PEP is regarded as the best-established definition of a PEP.³⁰

Though it has left the EU, the United Kingdom's (UK) framework for PEPs was developed while it was still bound to the EU's AMLDs and while it was still a member of the EU, the UK implemented these AMLDs through its Money Laundering Regulations (MLRs).³¹ The MLRs, 2007 defined a PEP as 'an individual who holds or has held a prominent position in the previous 12 months in a country other than the UK'.³² The listed examples of PEPs are contained in a separate Schedule 2 to the MLRs and contrary to the EU, the definition does not encompass legal entities. This position changed with the introduction of the MLRs, 2017 revision, which was passed to implement the Fourth AMLD, whose PEP provision encompasses legal entities.

A similar approach is necessary in countries such as South Africa, where corruption is prevalent,³³ and the societal influence of business and politics tends to be relatively similar. The Guidance for Banks on Customer Identification and Verification and Related Matters (FIC Guidance Note 3)³⁴ whose applicability is restricted to banks, defines PEPs under Section 25 as

²⁸ Ibid.

²⁹ EU Directive 2015/849 of the European Parliament and the Council (20 May 2015) (Fourth AMLD).

³⁰ Christelle Ahlers *The South African Anti-Money Laundering Regulatory Frameworks Relevant to Politically Exposed Persons* (unpublished MPhil thesis, University of Pretoria, 2013) 78.

³¹ Money Laundering Regulations 2007 and Money Laundering, Terrorist Financing and Transfer of Funds (information on the payer) Regulations 2017 available at <https://www.legislation.gov.uk/ukxi/2007/2157/regulation/14/made> accessed on 21.11.2023 and *The Money Laundering, Terrorist Financing and Transfer of Funds (Information on the Payer) Regulations 2017* ([legislation.gov.uk](https://www.legislation.gov.uk)) accessed on 19.11.2023.

³² Regulation 14(5)(b) -(c) and paragraph 4 of Schedule 2 of MLRs, 2007

³³ Corruption Watch 'NBI Addressing Corporate Corruption in South Africa-The EOH Experience' available at https://www.corruptionwatch.org.za/wp-content/uploads/2023/08/NBI-Addressing-Corporate-Corruption-in-South-Africa-The-EOH-Experience_29-Aug-2023.pdf accessed on 13.01.2024.

³⁴ Guidance for Banks on Customer Identification and Verification and Related Matters (GN 715 in GG 27803 of 18 July 2005). (hereinafter FIC Guidance Note 3).

‘an individual who is or has been entrusted with prominent public functions in a particular country’.³⁵ The standards established by the Wolfsberg Group serve as important guidelines for financial institutions in the implementation of AML/CTF measures.³⁶ Its classification of PEPs serves as a valuable reference point for South Africa in identifying and managing the risks associated with PEPs. Same Wolfsberg Group which reaffirms that a fundamental element for defining a PEP is its status as a natural person.³⁷ The regulation of PEPs in South Africa is integrated into the Financial Intelligence Centre Act 38 OF 2001 (FICA). FICA essentially aligns with the international approach and provides a definition of PEPs that closely resembles the guidelines set by the FATF. However, as of 2022, FICA as amended, introduced a new category of PEPs referred to as Prominent Influential Persons (PIPs) in Schedule 3C. The following is considered a PIP:

‘Any person who currently holds, or has held within the last 12 months, the position of chief financial officer, head of the committee on Audit, chairperson of the governing body, executive officer, head of a company, or head of an international organisation with headquarters in the Republic.’³⁸

Particularly, if the company supplies goods or services to a government entity and the yearly transactional worth of those supplies, commodities, or both, surpasses a threshold set by the Minister announced in the Government Gazette. The amendment resulted from the need to address the AML/CTF deficiencies in South Africa, the General Laws (Anti-Money Laundering and Combating Terrorism Financing) Amendment Act 22 of 2022 (the 2022 Amendment)³⁹ was enacted in order to, *inter alia*, strengthen the country’s beneficial ownership regulation and address the particular deficiencies highlighted in its 2021 Mutual Evaluation Report (MER,2021).⁴⁰ It was

³⁵ Section 25 of FIC Guidance Note 3.

³⁶ Christelle Ahlers op cit note 30 at 78.

³⁷ Ibid.

³⁸ Schedule 3C of the FICA.

³⁹ The Act amends the Companies Act and gives the mandate to the Companies and Intellectual Property Commission to collect beneficial ownership information.

⁴⁰ Companies and Intellectual Property Commission ‘Implementation of the Beneficial Ownership Regime by the Companies and Intellectual Property Commission (CIPC)’ available at https://www.cipc.co.za/wp-content/uploads/2023/03/General-Beneficial-Ownership-Notice_01-March-2023-Final.pdf accessed on 13.01.2024.

responding to its placement on the FATF grey list, which partially resulted from its failure to regulate legal entities and implement beneficial ownership measures.⁴¹

Some scholars advocate for a broader expansion of the PEP scope.⁴² To ensure a more comprehensive and effective approach to PEP identification and risk management, it is crucial for financial institutions to also consider legal entities in their due diligence processes.⁴³ The scholarly argument is that the focus on PEPs should extend to legal entities in the private sector.⁴⁴ However, that is already addressed by Recommendation 24⁴⁵ on beneficial ownership. Notably, the beneficial ownership regulation under Recommendation 24 remains limited as it continues to support the idea that the association with a PEP who is a natural person should be the primary focus.⁴⁶ Meanwhile, the EU-UK approach is thought to be the most comprehensive,⁴⁷ the monitoring of beneficial ownership alone leaves out a wide class of legal entities that are not associated with PEPs but are just as susceptible to ML/TF, such as those that conduct business with the government, through state institutions. On the other hand, FICA recognises that PEP-related risks extend beyond individual public officials. It acknowledges the role of influential individuals in the private sector who may have the ability to facilitate ML or illicit transactions by exploiting their connections to the state. However, despite being a positive step towards moving away from the narrow definition set by the FATF, South Africa's expansion of the scope of PEPs remains limited, as it continues to focus exclusively on natural persons.

Thus, this dissertation aims to show the need to expand the scope of PEPs beyond natural persons. The rationale for widening the scope to include legal entities lies in the understanding that illicit financial flows can occur through various channels, not limited to public officials alone who

⁴¹ FATF 'black and grey lists' available at "*Black and grey" lists (fatf-gafi.org)* accessed on 30/03/2023.

⁴² Kim-Kwang Raymond Choo 'Politically exposed persons (PEPs): risks and mitigation' (2008) 11 *JMLC* 371 at 383; emphasises that individuals in high-ranking positions within the private sector should also be subjected to PEP monitoring as these individuals are equally susceptible to corruption and may pose similar risks as their counterparts in the public sector.

⁴³ Daniele Canestri 'Politically exposed entities: how to tailor PEP requirements to PEP owned legal entities' (2019) 22 *JMLC* 359 at 360.

⁴⁴ Kim-Kwang Raymond Choo op cit note 42 at 383.

⁴⁵ Recommendation 24 of the FATF Recommendations, 2012.

⁴⁶ Daniele Canestri op cit note 43 at 363.

⁴⁷ Christelle Ahlers op cit note 30 at 78.

are natural persons or legal entities with a well-defined connection with a natural person. It must encompass especially a PEP who serves as a beneficial owner of a legal entity that engages in transactions with organs of state.

1.2. RESEARCH PURPOSE

The dissertation will answer the question whether the present definition of PEPs under the FATF, UK and South Africa's AML/CTF regime is effective in combating ML/TF. The analysis draws on insights from South Africa's Mutual Evaluation reports issued by the FATF and the Eastern and Southern African Anti-Money Laundering Group (ESAAMLG), which identified deficiencies in the adequacy of PEP regulation within South Africa's AML/CTF regulatory framework.⁴⁸ To provide a comparative perspective, the dissertation examines the AML/CTF regimes of both South Africa and the UK. These countries were chosen due to their shared characteristics in terms of legal and financial systems, as well as their mutual commitment to combating corruption and ML/TF.⁴⁹ By studying the well-developed AML/CTF regime of the UK⁵⁰ alongside the South African context, the research aims to highlight potential areas for improvement in PEP regulation and contribute to strengthening the effectiveness of AML/CTF efforts in South Africa.

⁴⁸ FATF Mutual evaluation report: Anti-money laundering and counter-terrorist financing measures – South Africa (2021) available at *Mutual-Evaluation-Report-South-Africa.pdf* accessed on 04.05.2023; FATF/ ESAAMLG Mutual evaluation report: Anti-money laundering and counter-terrorist financing measures – South Africa (2009) available at <https://www.fatf-gafi.org/contentdam/fatf-gafi/mer/MER%20South%20Africa%20full.pdf.coredownload.pdf> accessed on 15.11.2023 at pages 103,104; The 2021 report concluded that South Africa's PEP regulation was non-compliant with FATF standards, indicating the need for improvement in combatting money laundering and the financing of terrorism within the country.

⁴⁹ HM Treasury 'Review of the UK's AML/CFT regulatory and supervisory regime' June 2022 available at https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/1085407/MLRs_Review_Report_-_2.5_for_publication.pdf accessed on 08.06.2023.

⁵⁰ UK will be examined in this dissertation. Though it has left the European Union, its framework for PEPs was developed while it was still bound to the European Union directives.

1.3. RESEARCH OBJECTIVES AND RESEARCH QUESTIONS

This dissertation will analyse and evaluate the adequacy of PEP regulation under the international AML/CTF regulatory framework. It will comparatively analyse the regulatory framework for PEPs set by the FATF, the EU, the UK and South Africa, with particular regard to the definition of PEPs. The dissertation inquires whether PEPs are regulated sufficiently in order to combat ML/TF effectively in South Africa. The EU will be used as an example of well-developed PEP regulation while the UK will be used as an example of a jurisdiction in which PEP regulations were applied efficiently. The question then arises, how effective is the present definition of PEPs in combatting ML/TF? This dissertation is structured around the following three sub-questions:

- (1) Does the exclusion of legal entities as PEPs make the PEP regulatory framework ineffective in combatting ML/TF in South Africa?
- (2) Can the expansion of the scope of PEPs to encompass legal entities enhance the effectiveness of PEP regulation in combating ML/TF in South Africa?
- (3) Whether an improved PEP regulation is required for AML/CFT efforts in South Africa?

The goal of this dissertation is to ascertain whether the inclusion of legal entities in the definition of PEPs, regardless of their association with PEPs who are natural persons, will promote substantive compliance with FATF Recommendation 12 on PEPs.

1.4. SIGNIFICANCE OF THIS STUDY

The relevance of this dissertation lies in the fact that some international standard setters reiterate that the basic element of a PEP is that a PEP is a natural person;⁵¹ thereby acknowledging that legal entities are excluded as PEPs. The EU contradicts this stance and has expanded its definition of PEPs to include, among other things, any legal entity whose beneficial owner is a PEP or a PEP's family member.⁵² The EU's definition of a PEP is regarded as the best-established definition of a PEP for this reason.⁵³ One limiting factor of the EU's PEP definition, however, is that it has a

⁵¹ The Wolfsberg Group 'Wolfsberg guidance on Politically Exposed Person("PEP")' available at *Wolfsberg Frequently Asked Questions ("FAQ's") on (wolfsberg-principles.com)*, accessed on 05/03/2023.

⁵² Article 3(11) of the Fourth AMLD.

⁵³ Christelle Ahlers op cit note 30 at 78.

narrow focus on natural persons and a strict requirement for a clear relationship between the legal entity and a natural person PEP. This prerequisite excludes legal entities that lack a well-defined connection with a natural person PEP who serves as a beneficial owner, even if they engage in transactions with organs of state. Consequently, these legal entities, despite being equally susceptible to corruption and ML/TF, get excluded from being classified as PEPs. The anticipated outcome of this dissertation suggests that the exclusion of certain legal entities from the definition of a PEP has a detrimental impact on the effectiveness of PEP regulation in combating ML/TF. This finding could catalyse the FATF, other international standard-setting bodies, and domestic jurisdictions to revise their PEP definitions. Particularly, it can provide valuable guidance to South Africa in making necessary improvements to its AML/CTF regime, by improving its PEP regulation in alignment with AML/CTF efforts. This would be an appropriate response to its grey-listing status. Furthermore, this dissertation's findings can offer insights into the potential for sharing PEP regulations and practices between South Africa, the EU and the UK.

1.5. RESEARCH METHODOLOGY

This dissertation relies on desktop research as the primary methodology for gathering information and data. It involves a comprehensive investigation of laws and standards on PEPs at both international and domestic levels. The author will conduct a thorough review of relevant materials, including model laws, legislation, regulations, policy documents, court decisions, and scholarly literature. The literature review will reflect on the present knowledge connected to how we can enhance the protection of the integrity of the financial system. This review includes secondary sources such as scholarly writings as well as legal instruments. This literature encompasses digital books, journals, articles, reports, and information obtained from reliable websites.

1.6. RESEARCH LIMITATION

The comparison of PEP regulation between South Africa and the UK includes an examination of international standard setters such as the FATF, EU, Wolfsberg Group, Basel Committee on Banking Supervision, and United Nations Convention Against Corruption (UNCAC). It should be noted that there is no globally accepted definition of a PEP, and different jurisdictions have adopted varying PEP regulatory frameworks modelled after the FATF standards. The scope of this

dissertation was limited to analysing PEP regulation in South Africa, the EU, and the UK. The primary focus of the dissertation was on evaluating compliance with FATF Recommendation 12; however, Designated Non-Financial Businesses and Professions (DNFBPs) concerning PEP regulation were not addressed. This dissertation focuses on the implications for financial institutions, even if the FATF standards are applied to a broad range of businesses. Furthermore, the dissertation did not encompass the issue of compliance with the newly adopted regulations for Prominently Influential Persons (PIPs) in South Africa, but it will still consider the legislative requirements regarding PIPs.

1.7. CHAPTER OUTLINE

The dissertation is structured into several chapters to address the research issues systematically. This first introductory chapter introduces the subject matter, the research objectives, the research question, the purpose, the significance of the study, and the research methodology used to achieve the research objectives and concludes with the precepts of PEPs.

Chapter Two focuses on introducing and discussing the frameworks for PEPs. This chapter lays the groundwork for understanding the existing international PEPs regulatory framework.

Chapter Three will focus on UK's AML/CTF regulatory framework.

Chapter Four will discuss the South Africa's AML/CTF regulatory framework.

Chapter Five provides a critical assessment of the PEP frameworks. Through an in-depth analysis, it evaluates the strengths, weaknesses, and areas requiring improvement within these frameworks. A comparative study is conducted using legal justifications. The aim is to determine the extent to which an expansion of the definition of PEPs is necessary. The dissertation examines various PEP regulations to evaluate whether the existing definition should be broadened.

Finally, the dissertation concludes in Chapter Six, where the findings are summarised and discussed in light of the research objectives. This chapter serves as a conclusive summary of the critical assessment, comparative analysis, and legal justifications explored throughout the preceding chapters.

1.8. THE PRECEPTS OF PEPs.

This section aims to enhance the understanding of PEPs by examining their origins and the diverse definitions provided by various international standard-setting bodies.⁵⁴ By delving into the underlying principles that inform these definitions, one can gain valuable insights into the factors shaping their respective approaches.

1.8.1. THE ORIGINS OF POLITICALLY EXPOSED PERSONS

To present a concise historical overview of PEPs, the concept of PEP emerged in the early 2000s.⁵⁵ The Durban Declaration of 1999 highlighted the role of the international banking industry in potentially enabling corruption by facilitating the transfer and concealment of funds acquired unlawfully by corrupt leaders from developing countries.⁵⁶ In response, the Declaration sought assistance from the international community to combat corruption effectively.⁵⁷ To prevent and detect corruption and the associated ML activities, the banking industry was urged to develop internationally recognised norms that would mandate transaction recording and establish enforceable standards.⁵⁸ Addressing similar concerns, the United States issued guidance to its financial institutions regarding financial transactions involving a specific group designated as senior Foreign Political Figures. In the guidance provided by the United States, senior foreign political figures encompassed the following roles:

- “a current or former senior official of a foreign government or a major foreign political party;
- a current or former senior executive of a foreign government-owned commercial enterprise;

⁵⁴ Ramandeep Kaur Chhina op cit note 18 at 91-93.

⁵⁵ Nasir Sultan & Norazida Mohamed ‘Challenges faced by the financial institute before onboarding politically exposed person in undocumented eastern economies: a case study of Pakistan’ (2023) 26 *JMLC* 488 at 489; Mario Menz ‘Show me the money – managing politically exposed persons (PEPs) risks in UK financial services’ (2021) 28 *JFC* 968 at 969.

⁵⁶ Jackie Johnson op cit note 7 at 291.

⁵⁷ *Ibid* at 291.

⁵⁸ *Ibid*.

- a corporation, business, or other entity that has been formed by, or for the benefit of, any such individual;
- the immediate family members of any such individual; and
- the widely and publicly, or actually, known close associates of any such individual.”⁵⁹

The guidance explicitly defines any company, enterprise, or other organisation founded by or for the advantage of a prominent foreign political figure. Similar to the EU, the US follows international best practices by incorporating legal entities into its PEP regulation. The guidance provides instructions and recommendations on how financial institutions should navigate and manage such transactions involving Foreign Political Figures.⁶⁰

The term Foreign Political Figures was ultimately replaced by the term PEP. The concept of PEP was officially introduced in 2001 by the Basel Committee on Banking Supervision, it replaced the United States’ concept of Foreign Political Figures, which had been employed by international instruments as an alternative designation.⁶¹ While the Basel Committee on Banking Supervision guided how banks should approach customer due diligence (CDD) concerning PEPs, and the UK expressed its intention to address this matter, no other country promptly responded. The implementation of the Basel Committee’s recommendations would typically be the responsibility of banking authorities in each respective jurisdiction instead of governments.⁶² Similar to the UK, South Africa made it the responsibility of banking authorities to implement PEP regulations. Prior to the 2022 Amendment, despite having ratified UNCAC, South Africa was not in compliance with the FATF PEP requirements. PEP was regulated by the Guidance for Banks on Customer Identification and Verification and Related Matters (FIC Guidance Note 3) which is intended only for banks.⁶³

On an international scale, the FATF had to acknowledge the significance of identifying PEPs due to the clear connection between corruption and ML.⁶⁴ In 2003, it revised its AML

⁵⁹ FIN-2008-G005 available at *fin 2008 g005 (fincen.gov)* accessed on 15.07.2024.

⁶⁰ Jackie Johnson op cit note 7 at 291.

⁶¹ Nasir Sultan & Norazida Mohamed op cit note 55 at 489.

⁶² Jackie Johnson op cit note 7 at 291.

⁶³ Christelle Ahlers op cit note 30 at 101.

⁶⁴ Norman Mugarura ‘The effect of corruption factor in harnessing global anti-money laundering regimes’ (2010) 13 *JMLC* 272 at 273.

recommendations to include guidelines for regulating PEPs.⁶⁵ The FATF presented an updated collection of its “Forty Recommendations” about AML efforts and one of the specific additions in the revised recommendations was Recommendation 6⁶⁶, which focused on the relationship between financial institutions (such as banks) and PEPs.⁶⁷ Although its Recommendations are not legally binding, the FATF standards are recognised as an international standard for AML/CTF.⁶⁸ In light of both the UNCAC and the FATF standards, both South Africa and the UK were obligated to integrate regulations on PEPs into their domestic laws. South Africa remained non-compliant until 2022 as the non-compliance was remedied by the 2022 Amendment. Post-2023, the FATF began to raise public awareness regarding the vulnerability of high-ranking government officials, including heads of state, to bribery and corruption.⁶⁹

1.8.2. DEFINING POLITICALLY EXPOSED PERSONS⁷⁰

Several international standard-setting bodies define PEPs differently, and this arguably leads to inconsistency in many jurisdictions and such inconsistencies impair the efficiency of the implementation of the PEP regulation.⁷¹ Theodore et al believe that not having a widely accepted definition of a PEP makes it more difficult to enforce compliance with PEP regulations.⁷² On the contrary, Choo points out that avoiding developing a prescriptive definition of PEPs would be preferable.⁷³ Instead, financial institutions and regulators should adopt a risk-based approach to determine which forms of AML strategies are most likely to be effective in reducing the long-term

⁶⁵ FATF Recommendations, 2003.

⁶⁶ Recommendation 6 of the FATF Recommendations, 2012.

⁶⁷ Nasir Sultan & Norazida Mohamed op cit note 55 at 489.

⁶⁸ Nicholas W. Turner op cit note 12 at 548.

⁶⁹ Ibid at 490.

⁷⁰ Kim-Kwang Raymond Choo ‘Challenges in dealing with politically exposed persons’ (2010) 386 Trends and issues in crime and criminal justice 1 at 2; Jackie Johnson op cit note 7 at 292; Joel Harry Clavero Suntura, Piedad Maribel Rosero, Gloria Esperanza Aragon Cuamacas op cite note 13 at 268; Kim-Kwang Raymond Choo op cit note 42 at 373; Mario Menz op cit note 55 at 969.

⁷¹ Ramandeep Kaur Chhina op cit note 18 at 91-93.

⁷² Theodore S. Greenberg & Larissa Gray & Delphine Schantz et al ‘*Politically Exposed Persons Preventive Measures for the Banking Sector*’ (2010) 25.

⁷³ Kim-Kwang Raymond Choo op cit note 70 at 2.

ML risks that PEPs present. In a risk-based approach, jurisdictions' risks of ML/TF are identified, evaluated, and understood. Appropriate mitigation measures that are appropriate to the risk level are also implemented. Many regulatory frameworks favour the risk-based approach as a measure of compliance with the regulations and the laws, particularly in the financial sector, where it is believed that financial institutions may be more qualified than regulators to effectively identify and reduce the particular ML risks they come across.⁷⁴ Same was adopted by the FATF in 2012 when the FATF AML/CTF regulatory framework was revised. The risk-based approach was adopted under Recommendation 1.⁷⁵ However, despite the FATF having adopted a risk-based approach, the rule-based approach remains relevant in that, firstly, financial institutions are still bound by the prescribed rules that get legislated domestically – which must be adhered to else jurisdictions get grey-listed by the FATF for failing to meet its standard. Secondly, rules are important because regulations enhance behavioural and legal certainty, in that financial institutions are made fully aware of the extent of their obligations and the consequences of not adhering to these in advance.⁷⁶ On this account, the FATF has made significant progress in standardising the legal and regulatory frameworks of various jurisdictions.⁷⁷ Therefore, considering the above, this dissertation favours the view that a prescriptive definition of a PEP is necessary.

1.8.2.1. The Financial Action Task Force

Initially, the FATF issued mandatory requirements covering foreign PEPs, their family members, and close associates under Recommendation 6 of the 2003 FATF AML/CTF standards.⁷⁸ The 2003 PEP definition provided by the FATF encompassed individuals who currently or formerly held prominent public functions in foreign countries. Such individuals included ‘heads of State, heads of government, senior politicians, high-ranking government officials, senior judicial or military officers, and

⁷⁴ Ibid at 2.

⁷⁵ Recommendation 1 of the FATF Recommendations, 2012.

⁷⁶ Asim Jusic ‘Kuwait’s Administrative Risk-based Model for the Prevention of Money Laundering: Costs and Benefits of Compliance with the Financial Action Task Force (FATF) Standards’ (2017) 31 Arab Law Quarterly 101 at 111-112.

⁷⁷ Nicholas W. Turner op cit note 12 at 548.

⁷⁸ FATF Recommendations, 2003.

senior executives of state-owned corporations...'.⁷⁹ With the 2012 revision, mandatory requirements for PEPs were revised to cover domestic PEPs and PEPs of international organisations.⁸⁰ The goal of this revision was to align the FATF standards with the UNCAC which does not differentiate between domestic and foreign PEPs.⁸¹ Considering that there remains no widely agreed-upon definition of a PEP,⁸² different jurisdictions adopt varying PEP regulatory frameworks. The FATF aims to achieve consistent PEP regulation across various standard-setting bodies,⁸³ by creating benchmarks and recommending how AML/CTF may be implemented.⁸⁴ Therefore, how the FATF defines a PEP is important as it informs the approaches across various standard-setting bodies.

1.8.2.2. European Union

The EU Member States strongly favour a unified EU implementation of the FATF guidelines over fragmented approaches, guaranteeing fair competition in the financial sector. It is important to ensure that the EU's AML/CTF measures are in line with those taken by the FATF.⁸⁵ To achieve harmonisation of AML/CTF regulations within Europe, the EU has integrated the principles set forth by the FATF into several AMLDs. The Third AMLD previously set out the framework for combating ML/TF within the EU. As discussed above, according to Article 3(8) of the Third AMLD, PEP refers to:

“... natural persons who are or have been entrusted with prominent public functions and immediate family members, or persons known to be close associates, of such persons”.⁸⁶

⁷⁹ Recommendation 6 of the FATF Recommendations, 2003; Ibid at 14.

⁸⁰ Sungyong Kang ‘Rethinking the global Anti-Money Laundering Regulations to deter corruption’ (2018) 67 ICLQ 695 at 695-698.

⁸¹ Ibid at 695-698.

⁸² Kim-Kwang Raymond Choo op cit note 70 at 2.; Jackie Johnson op cit note 7 at 292; Joel Harry Clavero Suntura, Piedad Maribel Rosero, Gloria Esperanza Aragon Cuamacas op cite note 13 at 268; Kim-Kwang Raymond Choo op cit note 42 at 373; Mario Menz op cit note 55 at 969.

⁸³ FATF Guidance: Politically Exposed Persons (Recommendation 12 and 22) available at FATF Guidance: Politically Exposed Persons (Recommendations 12 and 22) (fatf-gafi.org).

⁸⁴ Theodore S. Greenberg & Larissa Gray & Delphine Schantz et al op cit note 72 at 25.

⁸⁵ Mariano Fernández Salas ‘The third anti-money laundering directive and the legal profession’ presented at European Association of Lawyers conference (27.05.2005).

⁸⁶ Article 3(8) of the Third AMLD.

The EU expanded the definition of PEPs in its Third AMLD to include, among other things, any legal entity whose beneficial owner is a PEP's family member. It maintained the same PEP scope in its Fourth AMLD.⁸⁷ It is for this reason that how the EU defines a PEP is considered to be the most comprehensive.⁸⁸

1.8.2.3. Basel Committee on Banking Supervision

In 1974, governors of eleven central banks worldwide came together to form the Basel Committee on Banking Supervision.⁸⁹ It was created to enhance financial stability and promote sound banking practices globally. While the Basel Committee does not possess legal or administrative authority, its role is to formulate and disseminate best practice principles, as well as develop supervisory standards and guidelines for the banking industry.⁹⁰ The Basel Committee first introduced the concept of PEP in 2001.⁹¹ Referring to PEPs as individuals known as potentates, such as foreign heads of state, ministers, powerful public figures, judges, and military leaders.⁹² It is important to note that the list of examples is suggestive rather than exhaustive. The underlying concept is that PEPs can abuse their public positions for personal gain through the taking of bribes, and embezzlement, especially in nations where corruption is widespread.

1.8.2.4. Wolfsberg Group

Established in 2000, the Wolfsberg Group has a specific objective of developing AML/CTF standards for the private banking industry.⁹³ Comprising 11 prominent financial institutions, the group collaboratively establishes industry standards and AML/CTF procedures. Its primary focus

⁸⁷ Article 3(11) of the Fourth AMLD.

⁸⁸ Christelle Ahlers op cit note 30 at 78.

⁸⁹ Basel Committee on Banking Supervision 'Consultative Document Customer due diligence for banks' available at <https://www.bis.org/publ/bcbs77.pdf> accessed on 22.06.2023; The current member countries of the Basel Committee comprise the following countries: South Africa, Singapore, Switzerland, Brazil, China, Russia, Japan, Korea, United States, and United Kingdom.

⁹⁰ Christelle Ahlers op cit note 30 at 78.

⁹¹ Nasir Sultan & Norazida Mohamed op cit note 55 at 489.

⁹² Basel Committee on Banking Supervision 'Consultative Document Customer due diligence for banks' available at <https://www.bis.org/publ/bcbs77.pdf> accessed on 22.06.2023.

⁹³ The Wolfsberg Group 'Wolfsberg guidance on Politically Exposed Person("PEP")' available at *Wolfsberg Frequently Asked Questions ("FAQ's") on (wolfsberg-principles.com)*, accessed on 05/03/2023.

is to combat corruption and advance global AML/CTF initiatives.⁹⁴ According to the Group, the fact that a PEP is a natural person is a fundamental component of the PEP definition. Moreover, it holds that it might not be necessary to classify a legal entity as a PEP. However, in practice, the involvement of a PEP in the administration of an entity could heighten the risks associated with creating or maintaining a relationship with such a legal entity.⁹⁵ Furthermore, it holds that the primary focus of the process for identifying and managing PEPs should be on detecting instances of grand corruption in the political sphere.⁹⁶ Its exclusive focus is corruption within the public sector. Finally, it advocates for the application of a risk-based approach to all PEPs, regardless of whether they are foreign or domestic. This can be contrasted with the FATF 2003 Recommendations, which suggested automatically categorising all foreign PEPs as high risk, although the position has since changed. The Wolfsberg Group guidance took into account the criteria outlined by globally recognised organisations, with an emphasis that while all individuals holding public office are susceptible to the possibility of corruption to some extent, those in senior, prominent, or influential positions with significant control over government operations, policies, or resource allocation carry a higher level of influence and pose greater risks for financial institutions.⁹⁷ This reiteration concerning PEPs emphasises that PEPs pertain to natural persons, meaning individuals rather than legal entities. This fundamental component ensures that the focus remains on assessing the risks associated with individuals who hold influential positions and have the potential to abuse their power for illicit activities.⁹⁸

1.9 CONCLUSION

The FATF was established during the Paris G7 summit in 1989⁹⁹ with the primary objective of developing AML/CTF policies and procedures at both the national and international levels. Its mandate also includes providing guidance and assistance to member countries in implementing

⁹⁴ Ibid.

⁹⁵ The Wolfsberg Group ‘Wolfsberg guidance on Politically Exposed Person(“PEP”)’ available at *Wolfsberg Frequently Asked Questions (“FAQ’s”) on (wolfsberg-principles.com)*, accessed on 05/03/2023.

⁹⁶ Ibid.

⁹⁷ Ibid.

⁹⁸ Ibid.

⁹⁹ The G7 countries present were Japan, the United Kingdom, the United States of America, Italy, France, Canada, and Germany.

the policies and procedures effectively. Although in purely legal terms, the FATF Standards are not legally binding, members of the FATF committed to incorporating international standards into their domestic laws.¹⁰⁰ Since its inception, the FATF has emerged as the leading international organisation responsible for setting standards and promoting strategies to protect the integrity of the world financial system. It serves as a benchmark for other international standard-setting bodies like the EU, the Basel Committee on Banking Supervision, the Wolfsberg Group, and the Joint Money Laundering Steering Committee. It is essential to the coordination of international measures to prevent ML/TF and other financial crimes.¹⁰¹ The FATF established three categories of PEPs. First, Foreign and Domestic PEPs are those who currently hold or have held prominent public positions domestically and in another country, for example, heads of state or government, significant figures in political parties, senior military or judicial members, and top executives of state-owned enterprises.¹⁰² In addition, International PEPs are those who are or have been entrusted with a prominent function by an international organisation, referring to senior management personnel, such as directors, deputy directors, board members, and those performing related roles.¹⁰³ The list of examples is suggestive rather than exhaustive.

¹⁰⁰ Nicholas W. Turner op cit note 12 at 548.

¹⁰¹ Ibid at 548.

¹⁰² FATF Recommendations 2012 ‘international standards on combating money laundering and the financing of terrorism & proliferation’ available at <https://www.fatf-gafi.org/content/dam/fatf-gafi/recommendations/FATF%20Recommendations%202012.pdf.coredownload.inline.pdf> accessed on 12.06.2023.

¹⁰³ FATF Recommendations, 2012.

CHAPTER 2 INTERNATIONAL AML/CTF STANDARDS ON POLITICALLY EXPOSED PERSONS

2.1. INTRODUCTION

While this study focuses on the AML/CTF frameworks of South Africa and the UK, it commences with an examination of foreign and international AML/CTF frameworks.

In most developing countries like South Africa, the association between ML and corruption is inextricable. Corruption serves as both a causative factor and a predicate offence in ML cases. It manifests in two ways: first, the laundered assets often stem from corrupt activities; and secondly, the act of laundering itself is facilitated by corrupting law enforcement agencies or officials within financial institutions. This enables the illicit proceeds to be seamlessly integrated into the financial system. As a consequence, the FATF was forced to integrate PEP-related standards as a result of the increased importance attached to the connection between ML and corruption.

In the 2003 Recommendations, the FATF introduced PEPs as ‘individuals who are or have been entrusted with prominent public functions in a foreign country’.¹⁰⁴ PEP regulation was contained under Recommendation 6 and excluded domestic PEPs within its scope. The 2003 PEP definition was too narrow in that it excluded domestic PEPs and has been superseded by subsequent revisions, notably the 2012 Recommendations. In addition, different formulations in other regulatory frameworks such as the UNCAC, the African Union Convention on Preventing and Combatting Corruption (AUPCC), and the Fourth AMLD, have expanded the narrow scope to include in addition to foreign PEPs, domestic PEPs. Recognising the challenges associated with identifying foreign PEPs alone, these instruments acknowledge the importance of identifying domestic PEPs.

Additionally, UNCAC, being a significant global initiative addressing corruption and its connection to ML imposes an obligation on State Parties to conduct enhanced scrutiny of accounts held by or on behalf of individuals who hold or have held prominent public positions, in addition to their close associates and family members.¹⁰⁵ Given the foregoing, the FATF expanded the

¹⁰⁴ Recommendation 6 of the FATF Recommendations, 2003.

¹⁰⁵ Article 52 of United Nations Convention Against Corruption (hereinafter UNCAC).

mandatory requirements for domestic PEPs and those of international organisations in 2012.¹⁰⁶ To further align with the objectives of Article 52 of the UNCAC. Recommendation 12 of the 2012 Recommendation establishes comprehensive guidelines for addressing the treatment of PEPs within the framework of AML/CTF. According to Recommendation 12, jurisdictions must ensure that financial institutions implement strategies to prevent PEPs from abusing the financial system and to identify possible abuse when it happens. The primary objective of this Recommendation is to the EDD process for PEPs, considering their elevated risk profile due to their prominent public positions or associations.

Furthermore, the African Union (AU) has a convention aimed at combatting corruption at a regional level, and whose general objectives have had a direct impact on the effectiveness of AML measures, the African Union Convention on Preventing and Combatting Corruption (AUCPCC). The AUCPCC seeks to promote and enhance the establishment of mechanisms that prevent, detect, punish, and eliminate corruption and related offences in both the public and private sectors. It introduced the concept of Public Official which is the equivalent of a PEP in terms of the FATF standards. A Public Official is defined broadly to encompass various positions and roles within the public sector. It includes individuals who hold legislative, executive, administrative, or judicial offices in a State Party, regardless of their appointment or election status, duration of service, or remuneration. The definition also extends to individuals who perform public functions, work for public agencies or public enterprises, or provide public services as defined by the domestic law of the State Party. The scope of the said Public Official is limited to domestic officials and excludes foreign officials.

2.2. THE AML/CTF FRAMEWORK UNDER INTERNATIONAL INSTRUMENTS

The International AML/CTF framework is primarily based on the FATF standards. In addition, it incorporates the provisions outlined in international Conventions which will be elaborated upon subsequently. For instance, many countries criminalise ML based on Conventions. This is according to the mandate under Recommendation 3 of the FATF:

¹⁰⁶ FATF Guidance: Politically Exposed Persons (Recommendation 12 and 22) available at FATF Guidance: Politically Exposed Persons (Recommendations 12 and 22) (fatf-gafi.org).

‘Countries should criminalise money laundering on the basis of the Vienna Convention and the Palermo Convention. Countries should apply the crime of money laundering to all serious offences, with a view to including the widest range of predicate offences.’¹⁰⁷

The scope of the criminal offence of ML is based on the formulation of the United Nations Convention Against Transnational Organized Crime (Palermo Convention).¹⁰⁸ A convention that South Africa ratified in 2012. Although South Africa is not a party to the Vienna Convention on the Law of Treaty, it is bound by the provisions of the Treaty. On the other hand, The UK is a party to both the Vienna and the Palermo Conventions. The UK signed Palermo in December 2000.

Additionally, the ML framework also finds its basis on best practices recommended by self-regulatory bodies within the financial sector, such as the Basel Committee on Banking Supervision and the Wolfsberg Group which have been incorporated to further enhance the effectiveness of the framework etc. Thus, by combining the sources of guidance and expertise, a comprehensive and robust approach to combating ML is established. In this context, the Vienna Convention describes ML as:

‘the conversion or transfer of property, knowing that such property is derived from any offense(s), for the purpose of concealing or disguising the illicit origin of the property or of assisting any person who is involved in such offense(s) to evade the legal consequences of his actions’.¹⁰⁹

Put simply, ML is the attempt to hide the source, ownership, control, or flow of funds that have been obtained illegally.¹¹⁰ The three phases of ML are integration, layering, and placement. Placement is the term used to describe the first-time cash obtained through illicit operations that are then used in a legal money transfer. Layering is the process of creating a sequence of transactions to conceal the initial transaction. Integration is the process of allocating cash to

¹⁰⁷ Recommendation 3 of the FATF Recommendations, 2012 at 12.

¹⁰⁸ Article 7 of the United Nations Convention Against Transnational Organized Crime (hereinafter Palermo Convention).

¹⁰⁹ Article 3.1 of the United Nations Convention Against Illicit Traffic in Narcotic Drugs and Psychotropic Substances, 1988 (hereinafter Vienna Convention).

¹¹⁰ Goredema, C. and Madzima, J. ‘An assessment of the links between corruption and the implementation of anti-money laundering strategies and measures in the ESAAMLG region’ available at https://www.esaamlg.org/reports/Corruption_and_AML_Systems..pdf accessed on 06.12.2023 at 15-16.

legal activities.¹¹¹ Instances of ML may involve any of these stages and all three are not necessarily present in every instance of ML.¹¹²

The Palermo Convention includes specific provisions aimed at combating ML in Articles 6, 7, 12, 13, and 14. Furthermore, the UNCAC Convention addresses measures to combat money laundering in Articles 14, 23, 24, 31, 51, and 59.

When it comes to the criminalisation of TF, as alluded previously, after the US terrorist attacks in 2001, the FATF issued eight Special Recommendations on TF, followed by a ninth Special Resolution urging jurisdictions to criminalise TF.¹¹³ According to the International Convention for the Suppression of the Financing of Terrorism (Terrorism Convention), TF is described as:

‘the distribution of financial resources to strengthen the capacity of an organisation or individual engaged in terrorism or associated activities to carry out an act that is considered a terrorist act.’¹¹⁴

The financial resources (funds) may be raised from legitimate sources, such as personal donations and profits from businesses and charitable organisations, as well as from criminal sources, such as the drug trade, the smuggling of weapons and other goods, fraud, kidnapping and extortion.¹¹⁵

Notably, notwithstanding the separate conventions regulating ML/TF, the FATF identified a nexus between ML/TF due to their inherent interconnectedness, thereby regulating them jointly and severally. Importantly, given that the financial sector is a rapidly evolving domain, it necessitates the continuous adaptation of AML/CTF standards to keep pace with evolving ML/TF techniques. The FATF maintains a commitment to updating its standards to address emerging risks

¹¹¹ Land and Agricultural Development Bank Of South Africa ‘Anti-Money Laundering (AML) & Combating The Financing Of Terrorism (CFT) And Sanctions Risk Management And Compliance Program’ available at https://Landbank.Co.Za/About-Us/Corporate%20governance%20documents/Anti-Money%20laundering%20aml_Cft.Pdf Accessed On 26.06.2023.

¹¹² Louis de Koker, Manet Bason, John Symington et al op cit note 2 at 5.

¹¹³ K.E. Davis op cit note 3 at 179-198.

¹¹⁴ Article 2(1) of the International Convention for the Suppression of the Financing of Terrorism, 2000 (hereinafter Terrorism Convention).

¹¹⁵ K.E. Davis op cit note 3 at 179-198.

and challenges in AML/CTF efforts.¹¹⁶ Further, it encourages FATF member countries to continually evaluate and strengthen their AML/CTF frameworks, including provisions related to PEPs, to ensure their efficacy in combating ML/TF.¹¹⁷ Given the foregoing, one area of concern has been the limited effectiveness of provisions on PEPs under Recommendation 12 of the FATF standards in combatting ML/TF, largely due to the narrow scope of the PEP definition.

2.3. POLITICALLY EXPOSED PERSON REGULATION UNDER UNITED NATIONS CONVENTION AGAINST CORRUPTION (UNCAC)

As mentioned above, the UNCAC is an important international initiative adopted in 2003 to eliminate corruption and its relationship to ML.¹¹⁸ It acknowledges that ML activities have a clear link to offences of corruption.¹¹⁹ The UK ratified the UNCAC in 2006 after signing it in 2003,¹²⁰ and South Africa ratified it in 2004.¹²¹ Article 52 of the UNCAC imposes an obligation on financial institutions in State Parties to conduct EDD of accounts held by or on behalf of individuals who hold or have held prominent public positions, as well as their family members and close associates.¹²² There is no distinction between a foreign and a domestic PEP under the UNCAC. The FATF established three kinds of PEPs, domestic, foreign, and international organisations in

¹¹⁶ FATF ‘FATF methodology for assessing compliance with the FATF recommendation and the Effectiveness of AML/CFT systems’ available at *FATF Methodology for assessing compliance with the FATF Recommendations and the effectiveness of AML/CFT systems (fatf-gafi.org)* accessed on 29/03/2023

¹¹⁷ Nicholas W. Turner op cit note 12 at 548.

¹¹⁸ UNCAC; Sungyong Kang op cit note 80 at 695.

¹¹⁹ FATF ‘FATF methodology for assessing compliance with the FATF recommendation and the Effectiveness of AML/CFT systems’ available at *FATF Methodology for assessing compliance with the FATF Recommendations and the effectiveness of AML/CFT systems (fatf-gafi.org)* accessed on 29/03/2023.

¹²⁰ UNCAC Coalition available at <https://uncaccoalition.org/files/cso-review-reports/year2-uk-report.pdf> accessed on 12.08.2023.

¹²¹ Justice and constitutional development available https://www.justice.gov.za/m_statements/2019/20191219-UNCAC.html#:~:text=South%20Africa%20ratified%20the%20United,been%20made%20in%20this%20regard. accessed on 12.08.2023.

¹²² Article 52 of the UNCAC.

order to align with the UNCAC.¹²³ The FATF initially issued mandatory requirements covering foreign PEPs, their family members, and close associates in June 2003, however, to comply with the objectives of UNCAC, which defines a PEP that encompasses both domestic and foreign PEPs, the FATF updated its standards for PEPs in its 2012 revision in line with Article 52 of UNCAC. Both South Africa and the UK adhere to the principles outlined in the UNCAC and the FATF, treating all PEPs uniformly, regardless of their categorisation as domestic, foreign, or international PEPs. This alignment stems from the FATF's 2012 revision, which aimed to harmonise the FATF with UNCAC.¹²⁴ Prior to this revision, differentiating between domestic and foreign PEPs was a possibility for jurisdictions, with the UK being one of those jurisdictions.¹²⁵ In South Africa, given that UNCAC has stricter guidelines regarding PEP Regulation than the FATF, and it remained non-compliant with PEP regulation for the longest time, it was even more non-compliant with UNCAC.¹²⁶

2.4. INTERNATIONAL AML/CTF STANDARDS

The FATF is entrusted with the responsibility of developing international standards and policies to combat ML/TF.¹²⁷ Through its ministerial mandate, the FATF has established a unified framework for AML/CTF efforts globally. Numerous jurisdictions have become members of the FATF or similar regional bodies that follow FATF standards.¹²⁸ These jurisdictions have committed to adopt and implement the FATF standards and undergo assessments of their

¹²³ FATF Glossary available at '*Glossary of the FATF Recommendations*' accessed on 21/03/2023; FATF 'FATF methodology for assessing compliance with the FATF recommendation and the Effectiveness of AML/CFT systems' available at *FATF Methodology for assessing compliance with the FATF Recommendations and the effectiveness of AML/CFT systems (fatf-gafi.org)* accessed on 29/03/2023.

¹²⁴ Sungyong Kang op cit note 80 at 695-698.

¹²⁵ Jackie Johnson op cit note 7 at 291.

¹²⁶ FATF/ ESAAMLG Mutual evaluation report: Anti-money laundering and counter-terrorist financing measures – South Africa (2009) available at <https://www.fatf-gafi.org/content/dam/fatf-gafi/mer/MER%20South%20Africa%20full.pdf.coredownload.pdf> accessed on 15.11.2023. at 103.

¹²⁷ Louis de Koker, Manet Bason, John Symington et al op cit note 2 at 11.

¹²⁸ Financial Action Task Force available at <https://www.fatf-gafi.org/en/the-fatf/who-we-are.html> accessed on 23.06.2023.

AML/CTF systems.¹²⁹ South Africa became a member of the FATF in June 2003 and is currently the only African FATF member. South Africa is also part of the Eastern and Southern Africa Anti-Money Laundering Group (ESAAMLG), which is one of the groups that was established within the African region to function as a regional body, adhering to the FATF model.¹³⁰ Through a peer review process of mutual evaluations, the FATF evaluates members' adherence to the FATF standards. It also undertakes typologies studies of ML/TF methods, and trends, and encourages the adoption and implementation of international measures to combat ML/TF.¹³¹ The FATF has successfully harmonised national legal and regulatory frameworks without having official, explicit jurisdiction under international law.¹³² Its Standards are globally accepted benchmarks for putting into practice efficient AML/CTF. They make the financial system more transparent and make it possible for jurisdictions to properly combat ML/TF.¹³³ As quoted above, Recommendation 3 mandates jurisdictions to criminalise ML according to the Vienna and Palermo Conventions. Most countries have implemented this provision domestically as discussed in the subsequent chapters. Furthermore, Recommendation 5 states that:

‘Countries should criminalise financing the travel of individuals who travel to a state other than their states of residence or nationality for the purpose of perpetrating, planning, or participating in terrorist acts or providing or receiving terrorist training.’¹³⁴

Similar to ML, this provision is also implemented by some countries. South Africa’s implementation is discussed under chapter 4 herein. Beyond criminalisation, other Recommendations that regulate TF. Recommendation 1 on Assessing Risks and Applying a Risk-Based Approach mandates countries to “... identify, assess, and understand the money laundering and terrorist financing risks they face. They should take appropriate measures to mitigate these risks.”¹³⁵ Further, Recommendation 6 on Targeted Financial Sanctions Related to Terrorism and Terrorist 3 Financing states that:

¹²⁹ Nicholas W. Turner op cit note 12 at 548.

¹³⁰ ESAAMLG available at <https://www.esaamlg.org/index.php/about> accessed on 27.11.2023.

¹³¹ Nicholas W. Turner op cit note 12 at 548.

¹³² Ibid at 548.

¹³³ Ibid.

¹³⁴ Recommendation 5 of the FATF Recommendations, 2012.

¹³⁵ Recommendation 1 ibid.

‘Countries should implement targeted financial sanctions against individuals and entities associated with terrorism. Financial institutions should freeze assets and prevent transactions related to designated terrorists and their supporters.’¹³⁶

Moreover, under Recommendation 7 on Targeted Financial Sanctions Related to Proliferation Financing the mandate is for countries to, ‘... implement targeted financial sanctions to prevent the financing of weapons of mass destruction proliferation.’¹³⁷ Despite being non-financial institutions, Recommendation 8 mandates countries to regulate Non-Profit Organizations to ‘... prevent abuse for terrorist financing purposes.’¹³⁸ Lastly, under Recommendation 16 on Wire Transfers, ‘Countries should ensure transparency and traceability of cross-border wire transfers to prevent terrorist financing.’¹³⁹

As above mentioned, the implementation of these is discussed below. Both the UK and South Africa have incorporated these provisions in their respective domestic legislation.

2.5. CONCLUSION

The FATF has developed international standards, and these standards are internationally endorsed global standards for implementing effective AML/CTF.¹⁴⁰ Several jurisdictions that are members of the FATF or similar regional bodies have committed to adopt and implement the international standards.¹⁴¹ Thereby strengthening their AML/CTF measures. However, one area of concern remains the limited effectiveness of provisions on PEPs in combatting ML/TF, largely due to the narrow scope of the PEP definition. Various revisions of the FATF standards and domestic AML/CTF regimes have attempted to address this however, it remains limited. To address this challenge, it is suggested that the PEP scope be widened to encompass legal entities, understanding that illicit financial flows can occur through various channels, not limited to public officials alone.¹⁴² Further, regulations must incorporate domestic PEPs.

¹³⁶ Recommendation 6 *ibid*.

¹³⁷ Recommendation 7 *ibid*.

¹³⁸ Recommendation 8 *ibid*.

¹³⁹ Recommendation 16 *ibid*.

¹⁴⁰ Nicholas W. Turner *op cit* note 12 at 548.

¹⁴¹ *Ibid* at 548.

¹⁴² Daniele Canestri *op cit* note 43 at 360.

CHAPTER 3 EUROPEAN UNION AND UNITED KINGDOM'S ANTI-MONEY LAUNDERING AND COUNTER-TERRORIST FINANCING LEGAL FRAMEWORK

3.1. INTRODUCTION

The previous chapter provided an overview of international ML/TF regulations. This section will concentrate on the AML/CTF framework, with a particular emphasis on PEPs in the UK.

Being among the world's oldest financial hubs, the UK is eager to be seen as the lead in the worldwide campaign to combat corruption and ML/TF. Firstly, it mandates its financial intelligence unit, the Financial Conduct Authority (FCA),¹⁴³ to issue guidance on how financial institutions can comply with the ML/TF regulations in the UK.¹⁴⁴ The guidance specifies who should and should not be considered a PEP.¹⁴⁵

Secondly, the UK's AML/CTF regime included the Money Laundering Regulations 2007 (MLRs, 2007). This became operative on 15 December 2007. The MLRs, 2007 defined a PEP as a person who holds or has held a prominent position in the previous 12 months in a country apart from the UK.¹⁴⁶ Including their immediate family members¹⁴⁷ and close associates.¹⁴⁸ Notably, the UK had no established definition for PEPs prior to the MLRs.¹⁴⁹ In addition, on 26 June 2017, the

¹⁴³ The Financial Conduct Authority is the UK's Financial Intelligence Unit.

¹⁴⁴ Section 138G of the Financial Services and Markets Act, 2000.

¹⁴⁵ Financial Conduct Authority *Guidance on the treatment of PEPs under the Money Laundering, Terrorist Financing and Transfer of Funds (Information on the Payer) Regulations 2017* available at <https://www.fca.org.uk/publication/guidance-consultation/gc17-02.pdf> accessed on 07.08.2023.

¹⁴⁶ Regulation 14(5)(a) and paragraph 4 of Schedule 2 of the MLRs, 2007 available at <https://www.legislation.gov.uk/uksi/2007/2157/regulation/14/made> accessed on 21.11.2023 (hereinafter MLRs, 2007).

¹⁴⁷ Family members of a PEP are defined in this regulation as the PEP's parents, children and their partners, and PEP's partner; A person is categorised as a known close associate if they have a close relationship with a PEP and take part in beneficial co-ownership, the creation of a corporate structures that are in the PEP's best interest.

¹⁴⁸ Regulation 14(5)(b) -(c) and paragraph 4 of Schedule 2 of MLRs, 2007.

¹⁴⁹ Money Laundering Regulations 2007 and Money Laundering, Terrorist Financing and Transfer of Funds (information on the payer) Regulations 2017 available at <https://www.legislation.gov.uk/uksi/2007/2157/regulation/14/made> accessed on 21.11.2023 and *The Money Laundering, Terrorist Financing and Transfer of Funds (Information on the Payer) Regulations 2017* ([legislation.gov.uk](https://www.legislation.gov.uk)) accessed on 19.11.2023.

Money Laundering, Terrorist Financing and Transfer of Funds (Information on the Payer) Regulations 2017 (MLRs, 2017) was introduced, which replaced and repealed the MLRs, 2007. The MLRs, 2017 defines PEPs in a similar way to the MLRs, 2007, except that it removes the specified period of 12 months.¹⁵⁰ Lastly, in 2022, a further revision was introduced, the Money Laundering, Terrorist Financing and Transfer of Funds (Information on the Payer) Amendment Regulation, 2023 (MLRs, 2023) but it did not address PEP provisions.¹⁵¹

Thus, this section provides an overview of the UK PEP framework, with an emphasis on the connection between the UK and the EU, to determine whether the MLRs adequately and effectively address ML/TF. Further, it reviews PEP provisions under the EU's AMLD, POCA, 2007 and MLRs,2017 and the FCA guidelines. In particular, this section focuses on the recently published MLRs, 2023, which modified MLRs, 2017. Specifically, how according to this Regulation, the UK reverts to its MLRs, 2007 stance of creating a distinction between domestic and non-domestic PEPs.¹⁵²

3.1.1. DEVELOPMENT OF AML/CTF REGULATION LEGAL FRAMEWORK IN THE UNITED KINGDOM

In the UK, ML has been made illegal by the Proceeds of Crime Act, 2002.¹⁵³ The Money Laundering Regulations (MLRs) provide additional regulation of ML.¹⁵⁴ The UK has had laws in place to prevent ML for over thirty years. The MLRs have changed throughout time to comply with various European Union Anti Money Laundering Directive (AMLDs) and international

¹⁵⁰ Regulation 35(12) of Money Laundering, Terrorist Financing and Transfer of Funds (Information on the Payer) Amendment Regulation, 2017 (hereinafter MLRs, 2017).

¹⁵¹ Money Laundering, Terrorist Financing and Transfer of Funds (Information on the Payer) Amendment Regulation, 2023 (hereinafter MLRs, 2023) available at <https://www.legislation.gov.uk/uksi/2023/1371/made> accessed on 20.01.2023; MLRs, 2023 amended Regulations 35(3) and 35(12) of MLRs, 2017.

¹⁵² Money Laundering and Terrorist Financing (Amendment) Regulations 2023 (hereinafter MLRs, 2023).

¹⁵³ Part 7 of the Proceeds of Crime Act, 2002.

¹⁵⁴ Money Laundering Regulations 2007 and Money Laundering, Terrorist Financing and Transfer of Funds (information on the payer) Regulations 2017 available at <https://www.legislation.gov.uk/uksi/2007/2157/regulation/14/made> accessed on 21.11.2023 and *The Money Laundering, Terrorist Financing and Transfer of Funds (Information on the Payer) Regulations 2017* ([legislation.gov.uk](https://www.legislation.gov.uk)) accessed on 19.11.2023.

standards. The EU Fourth AMLD, which was transposed in 2017 and was greatly influenced by a significant revision of the FATF standards in 2012, was the most significant recent revision.¹⁵⁵ A further revision to the MLRs was the implementation of the Fifth AMLD in January 2020.¹⁵⁶ ML regulation in the UK is quite efficient as ML crimes are successfully prosecuted. For instance, in the case of *SFO v Glencore Energy Limited UK*¹⁵⁷, a UK Court rendered a guilty verdict against Glencore and imposed a monetary fine as a penalty for contravening its AML principles.¹⁵⁸ The most attractive feature of the UK ML regulation is its extraterritorial effect.

TF was made illegal by the Counter-Terrorism Act, 2008.¹⁵⁹ The primary goal of the UK's AML/CTF regime is to guarantee the security of the financial systems and the economy as a whole from the threats of ML/TF, therefore enhancing the integrity of the financial sector and advancing its safety and security.¹⁶⁰ The AML/CTF regime in the UK was initially influenced by EU legislation, which aimed to incorporate the standards set by the FATF into EU law. However, with the occurrence of Brexit, the UK government introduced and enacted the Sanctions and Anti Money Laundering Act of 2008.¹⁶¹ Part 2 of this Act grants the authority to create secondary legislation for implementing FATF standards as they evolve.¹⁶² This allows the UK to potentially deviate considerably from the regulatory framework of the EU in the future.

¹⁵⁵ Zaiton Hamin, Wan Rosalili Wan Rosli, Normah Omar, Awang Armadajaya Pengiran Awang Mahmud 'Configuring criminal proceeds in money laundering cases in the UK' (2014) 17 *JMLC* 374 at 376-377.

¹⁵⁶ HM Treasury 'Review of the UK's AML/CFT regulatory and supervisory regime' June 2022 available at https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/1085407/MLRs_Review_Report_-_2.5_for_publication.pdf accessed on 08.06.2023.

¹⁵⁷ *Serious Fraud Office v Glencore* [2022] EWCR 1.

¹⁵⁸ *Ibid.*

¹⁵⁹ Section 1(1)(c) of the Terrorist Act, 2000; Section 93 of the Counter-Terrorism Act, 2008.

¹⁶⁰ HM Treasury 'Review of the UK's AML/CFT regulatory and supervisory regime' June 2022 available at https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/1085407/MLRs_Review_Report_-_2.5_for_publication.pdf accessed on 08.06.2023.

¹⁶¹ *Ibid.*

¹⁶² Part 2 of the Counter-Terrorism Act, 2008.

3.2. PEP REGULATION UNDER THE EU'S AMLDs AND ITS ADOPTION IN THE UK

PEP regulation has undergone multiple revisions in the EU over the years to conform to the FATF standards. The EU community acknowledges that PEPs are susceptible to abusing the financial system and laundering the money obtained from these abuses.¹⁶³ PEPs, as well as their family members and close associates, are subjected to EDD measures by financial institutions that serve as the financial system's gatekeepers.¹⁶⁴ To maintain uniform AML/CTF regulation across Europe, the EU has embraced the FATF Recommendations in the form of multiple AMLDs.

In June 2003, the FATF released the first set of required regulations on foreign PEPs, their immediate family members, and close associates which did not include the regulation of domestic PEPs.¹⁶⁵ These mandatory requirements were updated in 2012 to include both domestic, foreign, and international PEPs.¹⁶⁶ Similarly, the EU adopted the same approach. Prior to the Fourth AMLD, the EU treated domestic PEPs differently from foreign PEPs.¹⁶⁷

The FATF standards have been adopted by the EU through the AMLDs, which have been applied in the UK through secondary legislation.¹⁶⁸ Though the UK has left the European Union, its framework for PEPs was developed while it was still bound to the European Union directives. The MLRs, 2007, which were influenced by the Third AMLD, were the pertinent law in the UK prior to the MLRs, 2017. Both the Third AMLD and the MLRs, 2007 permitted financial institutions to treat domestic PEPs differently from foreign PEPs. At present, financial institutions

¹⁶³ Ali Shalchi 'Politically Exposed Persons Regime' *Commons Library Research Briefing* 16 February 2022 available at <https://commonslibrary.parliament.uk/research-briefings/cbp-7376/> accessed on 31.05.2023.

¹⁶⁴ Ibid.

¹⁶⁵ FATF on Money Laundering 2003 Recommendations available at <https://www.fatf-gafi.org/content/dam/fatf-gafi/recommendations/FATF%20Recommendations%202003.pdf> accessed on 26.11.2023.

¹⁶⁶ FATF Recommendations 'international standards on combating money laundering and the financing of terrorism & proliferation' available at <https://www.fatf-gafi.org/content/dam/fatf-gafi/recommendations/FATF%20Recommendations%202012.pdf.coredownload.inline.pdf> accessed on 12.06.2023.

¹⁶⁷ HM Treasury 'Review of the UK's AML/CFT regulatory and supervisory regime' June 2022 available at https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/1085407/MLRs_Review_Report_-_2.5_for_publication.pdf accessed on 08.06.2023.

¹⁶⁸ HM Treasury 'Review of the UK's AML/CFT regulatory and supervisory regime' June 2022 available at https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/1085407/MLRs_Review_Report_-_2.5_for_publication.pdf accessed on 08.06.2023 at 4.

are no longer permitted to treat PEPs differently when implementing EDD measures to take into consideration the dangers posed by foreign PEPs but not by domestic PEPs. This is according to the MLRs, 2017, and the Fourth AMLD.¹⁶⁹ The EU's strategy remains to carry out the same level of monitoring for both domestic and foreign PEPs.¹⁷⁰ Contrarily, in the UK, starting on 10 January 2024, domestic PEPs will be considered differently from foreign PEPs because domestic PEPs are regarded to pose a lower risk than foreign PEPs.¹⁷¹

Generally, PEPs are individuals who are or have been entrusted with prominent public functions as well as their immediate family members and close associates. The Third AMLD defined a PEP as a natural person who is or has held a position of prominence in the public sphere as well as that person's immediate family members and known close associates.¹⁷² The Third AMLD does not provide listed examples of PEPs within the definition. In contrast, in the Fourth AMLD, individuals in prominent positions, such as heads of state or the definition of PEPs included the following examples: senior government officials, senior politicians, judicial or military authorities, senior CEOs of state-owned companies, and significant political party officials.¹⁷³

Considering the potential ML and corruption risks connected with PEPs,¹⁷⁴ the required EDD measures were designed to make sure that the financial institutions covered by the Fourth AMLD had the proper protections in place when dealing with them.¹⁷⁵ Internationally, there exists a universal consensus that a PEP is a natural person, however, the EU PEP scope encompasses legal entities.¹⁷⁶ Unlike its counterpart - South Africa, the EU's PEP regulation incorporates beneficial ownership, thus simultaneously addressing natural persons and legal entities. Contrarily, in South Africa, FICA does not define 'Known close associate', only identifying family members

¹⁶⁹ Ibid at 16.

¹⁷⁰ It creates no distinction between domestic and foreign PEPs.

¹⁷¹ Regulation 3A of MLRs, 2017.

¹⁷² Article 3(8) of the Third AMLD.

¹⁷³ Article 3(9) of the Fourth AMLD; Section 5.6.14 Joint Money Laundering Steering Group guidance, 2006.

¹⁷⁴ Norman Mugarura op cit note 64 at 273.

¹⁷⁵ Article 20 of the Fourth AMLD

¹⁷⁶ Article 3(11) *ibid*.

of a PEP and not legal entities.¹⁷⁷ On this account, unlike in the EU, PEP regulation in South Africa does not extend to legal entities.

The UK's AML/CTF framework was expanded by the POCA.¹⁷⁸ MLRs are secondary to POCA, the former of which clarifies the AML obligations on businesses in greater detail and has undergone several revisions.¹⁷⁹ As alluded to above, while it was still a member of the EU, the UK implemented these AMLDs through its MLRs.¹⁸⁰ To provide a summary, of the evolution of PEP evolution in the UK. The MLRs, 2007 defined a PEP as 'an individual who holds or has held a prominent position in the previous 12 months in a country other than the UK'.¹⁸¹ Included are the PEP's immediate family and close associates.¹⁸² The listed examples of PEPs are contained in a separate Schedule 2 to the MLRs and contrary to the EU, the definition does not encompass legal entities. This position changed with the introduction of the MLRs, 2017 revision, which was passed to implement the Fourth AMLD, whose PEP provision encompasses legal entities. Further, the MLRs, 2017 required EDD to be applied to PEPs, family members and known close associates.¹⁸³ Lastly, the MLRs, 2023 was passed to amend PEP regulation in MLRs, 2017, and by defining and assessing domestic and non-domestic PEPs differently, domestic and non-domestic PEPs are now distinguished under the MLRs, 2023.¹⁸⁴

¹⁷⁷ Section 21H of FICA.

¹⁷⁸ Proceeds of Crime Act, 2002 (hereinafter POCA); POCA criminalised ML Offences under Part 7 of POCA which established three separate principal offences of ML Section 340(11)(a) defines ML as an act set out in sections 327, 328 and 329.

¹⁷⁹ Sabrina Fiona Preller 'Comparing AML legislation of the UK, Switzerland and Germany' (2008) 11 JMLC 234 at 245.

¹⁸⁰ Money Laundering Regulations 2007 and Money Laundering, Terrorist Financing and Transfer of Funds (information on the payer) Regulations 2017 available at <https://www.legislation.gov.uk/uksi/2007/2157/regulation/14/made> accessed on 21.11.2023 and *The Money Laundering, Terrorist Financing and Transfer of Funds (Information on the Payer) Regulations 2017 (legislation.gov.uk)* accessed on 19.11.2023.

¹⁸¹ Regulation 14(5) of the MLRs, 2007 available at <https://www.legislation.gov.uk/uksi/2007/2157/regulation/14/made> accessed on 21.11.2023.

¹⁸² Ibid at 16-17

¹⁸³ Regulation 35(1) of MLRs, 2017.

¹⁸⁴ Regulation 35(3A) (a), (b); 35(12) (d), (e), (f) *ibid*.

Notably, although the list of examples of PEPs as contained in a separate Schedule 2 to the MLRs is more suggestive than exhaustive, it seems to encompass individuals who, except for middle-level or lower-level officials, are trusted with prominent public functions.¹⁸⁵ In addition, unlike the MLRs, 2007 PEP definition, the MLRs, 2017 PEP definition is not time-specific. Importantly, although MLRs, 2017 defines a known close associate of a PEP as inter alia an individual who has sole beneficial ownership of a legal entity or a legal arrangement which is known to have been set up for the benefit of a PEP,¹⁸⁶ which definition encompasses legal entities, it remains limited as it still only focuses on the individuals who are behind the legal entities rather than the actual legal entity.

3.2.1. PEP REGULATION IMPLEMENTATION IN THE UK

The POCA, as amended by the Serious Organized Crime and Police Act 2005, the MLRs, 2017, the Terrorism Act 2000, and the Anti-Terrorism, Crime, and Security Act 2001 comprise the extensive AML/CFT legal framework in the UK.¹⁸⁷ The first AML law passed in the UK, was to prevent drug money from being laundered and to recover illegal proceeds.¹⁸⁸ Subsequently, several other legislative revisions were implemented that resulted in minor changes to the law. For example, the Criminal Justice Act of 1988 allowed for the seizure of assets valued at £10,000 following a conviction for specific summary offences and other crimes that were subject to an indictment.¹⁸⁹

The MLRs, which govern this sector at present, mandate the FCA to provide guidance on the EDD requirements for PEPs.¹⁹⁰ Regulation 48 of the MLRs imposes this obligation on the FCA.¹⁹¹

¹⁸⁵ Regulation 35(12)(a) *ibid*.

¹⁸⁶ Regulation 35(12)(c) *ibid*.

¹⁸⁷ Zaiton Hamin, Wan Rosalili Wan Rosli, Normah Omar et al op cit note 155 at 376-377; The Joint Money Laundering Steering Group Guidance and other pertinent guidelines from industry advisory groups and the government are included in the regulatory system.

¹⁸⁸ Drug Trafficking Offences Act 1986

¹⁸⁹ Zaiton Hamin, Wan Rosalili Wan Rosli, Normah Omar et al op cit note 155 at 376-377.

¹⁹⁰ Regulation 33–35 of the MLRs, 2007 available at <https://www.legislation.gov.uk/uksi/2007/2157/regulation/14/made> accessed on 21.11.2023.

¹⁹¹ Regulation 48 of MLRs, 2017 available at *The Money Laundering, Terrorist Financing and Transfer of Funds (Information on the Payer) Regulations 2017 (legislation.gov.uk)* accessed on 19.11.2023.

Prior to the introduction of the MLRs, 2017 that incorporate the EU's Fourth AMLD, the FICA was required by Section 333U of the Financial Services and Markets Act to publish guidelines regarding PEPs.¹⁹² This obligation is also covered by regulation 48(1) of MLRs, 2017, under which, the UK is obliged to issue guidance for PEP-specific EDD requirements.¹⁹³ The MLRs, 2017 further state that if the FCA has already provided guidance in accordance with the MLRs, the responsibility to provide guidance under section 333U is not applicable. Therefore, the guidance was released in accordance with Regulations 48(1), and it was assumed that by doing so, the FCA has fulfilled its obligation under section 333U once it takes effect.¹⁹⁴ Financial institutions are given clear instructions in the published guidelines on how to apply PEP definitions within the UK's MLRs.¹⁹⁵ Accordingly, although the definitions for domestic PEPs and foreign PEPs previously were different, the FCA recommended that domestic PEPs undergo EDD when it appears that they constitute a high risk for ML. In 2023, the UK passed an amendment to the MLRs, in 2017 to revert to this stance.¹⁹⁶ A PEP is defined in the FCA Guidance the same as MLRs, 2017 in Regulation 35(12)(a). This regulation defines a PEP as an individual holding a high-profile public position, excluding middle-level or junior officials.¹⁹⁷ The following categories are included in the definition but not exclusively:

- i. 'Heads of state, heads of government, ministers, deputy ministers; members of parliament or similar legislative bodies;
- ii. members of political party governing bodies;
- iii. members of supreme courts, constitutional courts, or other high-level judicial bodies where decisions are final except in extraordinary circumstances;
- iv. members of boards of central banks;

¹⁹² Section 333U of the Financial Services and Markets Act 2000.

¹⁹³ Regulation 48(1) of MLRs, 2017 available at *The Money Laundering, Terrorist Financing and Transfer of Funds (Information on the Payer) Regulations 2017 (legislation.gov.uk)* accessed on 19.11.2023.

¹⁹⁴ Financial Conduct Authority *Guidance on the treatment of politically exposed persons (PEPs) under the Money Laundering, Terrorist Financing and Transfer of Funds (Information on the Payer) Regulations 2017* available at <https://www.fca.org.uk/publication/guidance-consultation/gc17-02.pdf> accessed on 07.08.2023.

¹⁹⁵ Ibid.

¹⁹⁶ MLRs, 2023.

¹⁹⁷ Financial Conduct Authority, FG 17/6 available at *FG17/6: The treatment of politically exposed persons for anti-money laundering purposes (fca.org.uk)* accessed on 05/03/2023 at 6-8.

- v. members of the administration, managerial, or supervisory bodies of state-owned enterprises;
- vi. ambassadors, chargés d'affaires, and senior military officials; directors, deputy directors, and board members; and
- vii. those performing a similar position for an international organisation.¹⁹⁸

It is important to note that this definition applies to individuals holding such positions both in the UK and abroad, and it is not an exhaustive list. Additionally, the definition of family members regarding a PEP is similar to MLRs, 2017 in Regulation 35(12)(c). Family members of a PEP are defined in this regulation as the PEP's parents, the PEP's partner, and the PEP's children and their partners.¹⁹⁹ The provisions of Regulation 35(9), which mandate that a PEP be treated as such even after leaving office, do not apply to family members, as stated in Regulation 35(11).²⁰⁰ Family members should instead be considered like regular customers unless there are obvious other risks.²⁰¹

Following the UK's 2018 Mutual Evaluation Report (MER,2018),²⁰² the UK was given priority actions by the FATF. These actions specifically focused on areas such as improving the quality of financial intelligence accessible to UK law enforcement agencies. In addition, the FATF also highlighted some specific weaknesses in the regulated sector's understanding of risk and the effectiveness of the preventative measures implemented.²⁰³ PEP regulation is a major part of risk management, and thus crucial to the UK's strengthening of its AML/CTF regime.

3.2.2. POLITICALLY EXPOSED PERSONS UNDER JOINT MONEY LAUNDERING STEERING GROUP (JMLSG)

Presently in the UK, there are three statutory supervisors. The Financial Conduct Authority (FCA) supervises banks and other financial and credit institutions. His Majesty's Revenue and Customs

¹⁹⁸ Regulation 35(12) of the MLRs, 2017; Ibid at 6.

¹⁹⁹ Ibid at 7-8; Regulation 35(12)(c) of the MLRs, 2017.

²⁰⁰ Regulations 35(9) and 35(11) of the MLRs, 2017.

²⁰¹ Ibid at 8; Regulation 35(11) of the MLRs, 2017.

²⁰² AML/CTF United Kingdom Mutual Evaluation Report, 2018 available at <https://www.fatf-gafi.org/content/dam/fatf-gafi/mer/MER-United-Kingdom-2018.pdf.coredownload.pdf> accessed on 27.11.2023.

²⁰³ Ibid.

(HMRC) oversees money service businesses, high-value dealers, estate agents, letting agents and art market participants, amongst others. The Gambling Commission deals with betting firms and casinos. The POCA enabled specific LEAs that deal with organised crime to recover the proceeds of “criminally derived” property.

The Joint Money Laundering Steering Group (JMLSG) is a self-regulatory industry body consisting of major UK Trade Associations in the financial services industry. It is in charge of creating guidelines to help companies in the financial sector fulfil their legal and regulatory duties under UK AML/CTF regulation.²⁰⁴ HM Treasury granted the guidance approval, meaning that the UK government recognises and supports JMLSG guidelines even though it is not a legally enforceable instrument.²⁰⁵ According to the JMLSG Guidelines, PEPs are individuals who either presently hold or have previously held a prominent political position or public office.²⁰⁶ The JMLSG holds that due to their influential positions, PEPs present an elevated risk of ML for financial institutions, as they may be susceptible to corruption.²⁰⁷ This risk also applies to their immediate family members and close associates.²⁰⁸ This definition is in line with the guidelines of the MLRs, 2017²⁰⁹ and thus also the Fourth AMLD.²¹⁰

3.3. CONCLUSION

The PEP regulatory framework within the UK was shaped by the AMLDs. Domestically, AML/CTF was incorporated through POCA, which made it illegal for anyone in the UK to possess proceeds of crime, as well as to make efforts to do so.²¹¹ Several MLRs have imposed legal obligations on financial institutions since the early 1990s. Financial institutions must look for the

²⁰⁴ Joint Money Laundering Steering Group ‘Prevention of money laundering/ combating terrorist financing’ available at <https://www.jmlsg.org.uk/guidance/current-guidance/> accessed on 22.06.2023.

²⁰⁵²⁰⁵ HM Treasury ‘Review of the UK’s AML/CFT regulatory and supervisory regime’ June 2022 available at https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/1085407/MLRs_Review_Report_-_2.5_for_publication.pdf accessed on 08.06.2023.

²⁰⁶ Section 5.6.12 Joint Money Laundering Steering Group, 2006.

²⁰⁷ Ibid at 90.

²⁰⁸ Ibid.

²⁰⁹ Regulation 35(12)(a) of the MLRs, 2017.

²¹⁰ Article 3(9) of the Fourth AMLD.

²¹¹ Sections 327, 328 and 329 of POCA.

proceeds of all financially motivated crimes, perform ongoing customer due diligence and take a risk-based approach to applying AML duties.²¹²

The PEP provisions are contained in the MLRs. Due to their positions of power and influence within the government, PEPs are susceptible to risks including corruption and ML. The UK understands that it is crucial to regulate PEPs because financial institutions that are exploited by PEPs are exposed to reputational risk, financial instability, diminished public confidence, threats to safety and soundness, and direct losses. Accordingly, the FCA is mandated by Section 333U of the Financial Services and Markets Act and Regulation 48(1) of MLRs, 2017 to publish guidelines regarding PEPs, to assist financial institutions in their business with PEPs. The JMLSG also issues guidelines to help financial institutions in applying PEP regulation. Considering the PEP regulatory framework in the UK, PEPs are properly regulated. Notwithstanding the differentiation of foreign and domestic PEPs, as well as its limited ability to regulate legal entities that engage with organs of state independent of the natural persons behind them, the UK has largely adopted Recommendation 12 of the FATF on PEPs.

²¹² Section 330 of the POCA

CHAPTER 4 ANTI-MONEY LAUNDERING AND COUNTER-TERRORIST FINANCING REGIME IN SOUTH AFRICA

4.1.INTRODUCTION

In the preceding chapters, we examined international and foreign AML/CTF frameworks. This section will now delve into the AML/CTF frameworks specific to South Africa.

Many countries over the years, including South Africa, established legislation to combat ML/TF since the 1990s. Initially focusing on the proceeds of drug-related activities.²¹³ South Africa expanded its laws' initial focus on the proceeds of drug-related activities to include the proceeds of any criminal activity.²¹⁴ Moreover, it expanded its legal framework further when the FATF AML/CTF standards were revised in 2003, mandating client identification, record-keeping, and reporting of suspicious transactions not only for financial institutions but also for non-financial businesses that could be exploited by money launderers and terrorist financiers.²¹⁵ In 2001, the Financial Intelligence Centre Act 38 of 2001 (FICA) was introduced to further strengthen South Africa's AML framework.²¹⁶ Following this, the international community came to an agreement that a similar approach should be employed to prevent TF as global concerns over cross-border TF increased in the early 2000s. South Africa only introduced the Protection of Constitutional Democracy Against Terrorist and Related Activities Act²¹⁷ in 2004, extending its AML policies to include combating financing of terrorism activity.²¹⁸ The FATF standards inform key elements of the South African AML/CTF law and policy. The most recent legislative development in this regard is the enactment of the 2022 Amendment which addresses, inter alia, the non-compliance

²¹³ Drugs and Drug Trafficking Act 140 of 1992.

²¹⁴ Louis de Koker, Manet Bason, John Symington et al op cit note 2 at 18-19; Proceeds of Crimes Act 76 of 1996.

²¹⁵ Prevention of Organised Crime Act 121 of 1998 (hereinafter POCA).

²¹⁶ Financial Intelligence Centre Act 38 of 2001.

²¹⁷ Protection of Constitutional Democracy Against Terrorist and Related Activities Act 33 of 2004 (hereinafter POCDATARA).

²¹⁸ Louis de Koker, Manet Bason, John Symington et al op cit note 2 at 25-27.

of South Africa with Recommendation 12 of the FATF as highlighted in its 2021 MER.²¹⁹ The Act among others, introduces the concept of PIP, which is central to this discussion.²²⁰

4.2.THE EVOLUTION OF THE AML/CTF LEGAL FRAMEWORK IN SOUTH AFRICA

The development of the AML/CTF regime in South Africa can be traced back to 1992 with the enactment of the Drug and Drug Trafficking Act 140 of 1992.²²¹ This was the initial legislation primarily focused on addressing ML related to drug-related crimes and ML is criminalised under section 14 of this Act.²²² Eventually, this Act became less effective due to its limited scope.²²³ On this account, the Proceeds of Crimes Act 76 of 1996 was introduced, to further strengthen the AML framework in the country.²²⁴ Generally, this Act expanded the scope of ML regulations in South Africa to include the proceeds of all types of crimes,²²⁵ and it introduced provisions for the confiscation of such proceeds upon conviction.²²⁶ In 1998, the South African government took decisive action against organised crime by enacting the Prevention of Organised Crime Act 121 of 1998 (POCA).²²⁷ POCA replaced the Proceeds of Crimes Act and aimed to combat organised criminal activities more effectively.²²⁸ For instance, by inter alia broadening the ‘proceeds of unlawful activities’ definition and providing explicitly that ML offence could be committed negligently, and imposing general obligations on businesses to report suspicious transactions.²²⁹ These reporting requirements were later amended and eventually repealed with the introduction of a broader duty to report suspicious and unusual transactions under the Financial Intelligence Centre

²¹⁹ Ibid at 33-35; Cayle Lupton ‘A comparative analysis of the targeted financial sanctions regulatory framework of the European Union and United Kingdom: Lessons for South Africa’ (2023) 86 *Journal of contemporary Roman-Dutch law* 40 at 43.

²²⁰ Schedule 3C of FICA.

²²¹ Louis de Koker, Manet Bason, John Symington et al op cit note 2 at 18.

²²² Section 14 of the Drugs and Drug Trafficking Act 140 of 1992.

²²³ Louis de Koker, Manet Bason, John Symington et al op cit note 2 at 19.

²²⁴ Proceeds of Crimes Act 76 of 1996.

²²⁵ Section 4 ibid.

²²⁶ Section 8, 16 and 18 ibid; Louis de Koker, Manet Bason, John Symington et al op cit note 2 at 19.

²²⁷ Prevention of Organised Crime Act 121 of 1998 (hereinafter POCA).

²²⁸ Louis de Koker, Manet Bason, John Symington et al op cit note 2 at 20.

²²⁹ Sections 4,5 and 6 of the Prevention of Organised Crime Act 121 of 1998.

Act 38 of 2001 (FICA).²³⁰ FICA further strengthened South Africa's AML/CTF framework and established the Financial Intelligence Centre (FIC) as the regulatory authority responsible for overseeing compliance with AML/CTF obligations in the country,²³¹ the Counter-Money Laundering Advisory Council,²³² and enabled the drafting of regulations under the Act.²³³ When the Financial Intelligence Centre Amendment Act 11 of 2008 was passed in 2008, significant changes to FICA were made.²³⁴ This Amendment provides that it will take precedence over any Act on matters covered by FICA in the case of a conflict.²³⁵ The Financial Intelligence Centre Amendment Act 1 of 2017 was introduced in 2017 to align South Africa's AML/CTF law and policy with the FATF's standards.²³⁶ The Amendment introduces improved due diligence measures relating to beneficial ownership, ongoing due diligence and foreign and domestic prominent influential persons and dissolves the Counter-Money Laundering Advisory Council.²³⁷ The Prevention and Combatting of Corrupt Activities Act 12 of 2004 (PRECCA) is important because the offence of ML overlaps with the offence of corruption.²³⁸ The Act addresses ML in the context of corrupt activities. While the Act itself is comprehensive and covers a wide range of corrupt activities, it does not contain a section specifically dealing with ML. Similarly, the Protection of Constitutional Democracy Against Terrorist and Related Activities Act 33 of 2004 (POCDATARA) covers inter alia targeted financial sanctions, freezing orders,²³⁹ and penalties for terrorist financing offences.²⁴⁰ This legislation is exhaustive and encompasses an extensive range of activities related to the financing of terrorism, wherein ML is consequently associated. The Act addresses ML in the context of financing of terrorism. Finally, in 2022, South Africa committed

²³⁰ Section 29 of FICA.

²³¹ Section 2 *ibid*.

²³² Section 17 *ibid*.

²³³ Section 77 *ibid*; Louis de Koker, Manet Bason, John Symington et al op cit note 2 at 22-24.

²³⁴ Key objectives of the FICA; *ibid* at 23.

²³⁵ Section 1A *ibid*.

²³⁶ Louis de Koker, Manet Bason, John Symington et al op cit note 2 at 23.

²³⁷ Section 21B of the Financial Intelligence Centre Amendment Act 11 of 2008; *ibid* at 23.

²³⁸ Prevention and Combatting of Corrupt Activities Act 12 of 2004; refer to 2.3 for a thorough discussion of the link between ML and corruption.

²³⁹ Sections 22-24 of the POCDATARA.

²⁴⁰ Chapters 3 and 4 *ibid*; Louis de Koker, Manet Bason, John Symington et al op cit note 2 at 26-27.

to strengthening its AML/CTF regime by passing the 2022 Amendment which inter alia amended FICA.²⁴¹

4.3. PEPs UNDER THE FINANCIAL INTELLIGENCE CENTRE ACT 38 OF 2001 (AS AMENDED) (FICA)

FICA provides for the issuing of Guideline Notes to help financial institutions in the practical implementation of the Act. In this regard, the Financial Intelligence Centre (FIC) is tasked with the responsibility of monitoring and providing guidance to accountable institutions, supervisory bodies, and other individuals under FICA, although, such Guideline Notes do not replace FICA or its Regulations.²⁴² Accordingly, FIC issued the Guidance for Banks on Customer Identification and Verification and Related Matters (FIC Guidance Note 3).²⁴³ PEPs are defined in Section 25 of the FIC Guidance Note 3, along with the EDD that applies to them.²⁴⁴ Importantly, the FIC Guidance Note 3 was only intended for banks. Although, the guidance note addressed PEP regulation; however, its applicability is restricted to banks.²⁴⁵ Section 25 of the FIC Guidance Note 3 classifies a PEP as ‘an individual who is or has been entrusted with prominent public functions in a particular country’.²⁴⁶ This definition encompasses individuals holding significant positions of authority and influence, particularly, in the public sector.

This classification of PEPs, as defined by the FIC Guidance Note 3 holds a significant importance in South Africa. The guidance note references the principles issued by the Wolfsberg Group.²⁴⁷ The Wolfsberg Group contributes to the development of effective AML/CTF frameworks that help prevent financial crimes such as ML/TF.²⁴⁸ The standards and procedures

²⁴¹ General Laws (Anti-Money Laundering and Combating Terrorism Financing) Amendment Act 22 of 2022 (hereinafter the 2022 Amendment); *ibid* at 33-34.

²⁴² Section 4(c) of the FICA.

²⁴³ Guidance for Banks on Customer Identification and Verification and Related Matters (GN 715 in GG 27803 of 18 July 2005). (hereinafter FIC Guidance Note 3).

²⁴⁴ Section 25 of FIC Guidance Note 3.

²⁴⁵ Christelle Ahlers *op cit* note 30 at 101.

²⁴⁶ Section 25 of FIC Guidance Note 3.

²⁴⁷ Section 24 *ibid*.

²⁴⁸ Refer to 1.8.2.4 for a thorough discussion of the Wolfsberg Group

established by the Wolfsberg Group serve as important guidelines for financial institutions, promoting a common understanding and implementation of AML/CTF measures.²⁴⁹ Its classification of PEPs serves as a valuable reference point for South Africa in identifying and managing the risks associated with PEPs. The Wolfsberg Group has issued principles that provide guidance on best banking practices related to PEPs.²⁵⁰ These principles apply to PEPs who are foreign as well as domestic ones, emphasising the importance of implementing extra safeguards when dealing with individuals in prominent public positions. At present, PEP regulation is incorporated into FICA. However, before the 2022 Amendment, South Africa had no PEP regulation despite having the FIC Guidance Note 3 because it was exclusively applicable to banks.

As above mentioned, there are specific classifications for PEPs. FICA distinguishes between Domestic Politically Exposed Persons (DPEPs) and Foreign Politically Exposed Persons (FPEPS). A DPEP is an individual who holds or has held a prominent public function in South Africa, including acting positions lasting more than six months.²⁵¹ This includes a broad range of positions, including those held by the President, ministers of government, executives of state-owned enterprises, and judiciary members.²⁵² On the other hand, an FPEP is an individual who holds or has held a prominent public function in a foreign country, including acting positions exceeding six months.²⁵³ For example, a head of State; a member of the royal family; a minister in government or the head of a political party; a senior executive in a state-owned enterprise; a senior judge; or a high-ranking military officer in a foreign state.²⁵⁴ While there is no universally agreed-upon definition for PEPs²⁵⁵, the list of examples although suggestive as opposed to exhaustive helps provide clarity.²⁵⁶

²⁴⁹ Christelle Ahlers op cit note 30 at 78.

²⁵⁰ The Wolfsberg group ‘Wolfsberg guidance on Politically Exposed Person (“PEP”)’ available at *Wolfsberg Frequently Asked Questions (“FAQ’s”) on (wolfsberg-principles.com)*, accessed on 23/03/2023.

²⁵¹ Section 18(e) of the 2022 Amendment; Schedule 3A and 3B of FICA.

²⁵² Schedule 3A of FICA

²⁵³ Section 18(f) of the 2022 Amendment; Schedule 3A and 3B of the FICA.

²⁵⁴ Schedule 3B of FICA

²⁵⁵ Kim-Kwang Raymond Choo op cit note 42 at 387.

²⁵⁵ Daniele Canestri op cit note 43 at 372.

²⁵⁶ Schedule 3A and 3B of FICA.

FICA recognises the importance for banks to extend their scrutiny beyond the PEPs themselves and also pay attention to their family members and known close associates.²⁵⁷ The term family members encompasses those immediate family members, such as spouses, children, parents, siblings, other blood relatives and relatives through marriage.²⁵⁸ Furthermore, according to FIC Guidance Note 3, close associates comprise individuals who have business relations with the PEP and may encompass individuals who benefit significantly from their proximity to the PEP, either financially or in terms of influence or reputation.²⁵⁹ Given their positions of power and influence, it is widely acknowledged that PEPs have the potential to exploit their roles for illicit activities, such as ML, corruption, and involvement in activities related to TF.²⁶⁰ The elevated risk associated with these individuals arises from their ability to misuse their authority and access to resources, making them attractive targets for illicit financial schemes.²⁶¹ The funds generated through such activities can be hidden or disguised through complex transactions, making it crucial for regulatory bodies to strengthen their AML/CTF measures to detect such behaviour.²⁶² Thus, the wider the category, the better.

4.3.1. THE GENERAL LAWS (ANTI-MONEY LAUNDERING AND COMBATING TERRORISM FINANCING) AMENDMENT ACT 22 OF 2022

The South African legislature passed the 2022 Amendment, in response to its placement on the FATF grey list. This was an important turning point in South Africa's efforts to combat ML/TF effectively and was a pivotal development in response to the deficiencies exposed during the state capture era.²⁶³ This legislative revision which inter alia amended FICA was aimed at enhancing the effectiveness of AML/CTF measures, ensuring that the financial system is better protected from abuse and facilitating the country's compliance with international standards, although

²⁵⁷ Section 21H (1) of FICA.

²⁵⁸ Section 21H (2) of FICA.

²⁵⁹ Section 25 of FIC Guidance Note 3.

²⁶⁰ Christelle Ahlers op cit note 30 at 97-98.

²⁶¹ Ibid at 97-98.

²⁶² Ibid at 98.

²⁶³ Cayle Lupton op cit 219 at 43.

ultimately, the reinforcement of its AML/CTF measures is also part of its efforts to get removed from the FATF grey list.

Accordingly, FICA as amended, introduced a new category of PEPs referred to as Prominent Influential Persons (PIPs) in Schedule 3C.²⁶⁴ Any person who currently holds, or has held within the last 12 months, the position of chief financial officer, head of the committee on Audit, chairperson of the governing body, executive officer, head of a company, or head of an international organisation with headquarters in the Republic is considered a PIP. Particularly, if the company supplies goods or services to a government entity and the yearly transactional worth of those supplies, commodities, or both, surpasses a threshold set by the Minister announced in the Government Gazette.²⁶⁵

Notably, one of the key areas of focus in the DPEP and FPEP was the absence of explicit requirements for the role of influential individuals, including those in the private sector, who have the ability to facilitate ML or illicit transactions by exploiting their connections to the state. Thus, the introduction of the concept of PIPs represents a substantial expansion in this regard, as it broadened the scope of PEPs beyond natural persons in the public sector. Overall, PIPs encompass individuals involved in the governance and management of companies engaged in transactions with organs of the state, particularly those legal entities benefiting from state contracts.²⁶⁶ By including governance and management personnel of companies involved in dealings with organs of state and beneficiaries of state contracts, FICA, recognises that PEP-related risks extend beyond individual public officials. It acknowledges the role of influential individuals in the private sector who may have the ability to facilitate ML or illicit transactions by exploiting their connections to the state. However, despite being a positive step towards moving away from the narrow definition set by the FATF, South Africa's expansion of the scope of PEPs remains limited, as it continues to focus exclusively on natural persons.

²⁶⁴ Schedule 3C of the FICA.

²⁶⁵ Ibid.

²⁶⁶ Schedule 3C of the FICA.

4.4. THE GREYLISTING OF SOUTH AFRICA BY THE FATF

Every eight to ten years, assessors examine every jurisdiction in the world, and the FATF publishes a report detailing the evaluation's findings. We refer to this report as the Mutual Evaluation Report (MER). The last MER for South Africa was released in 2021 (MER,2021).²⁶⁷ Mutual evaluations evaluate members based on two criteria: technical compliance and effectiveness. technical compliance evaluates whether members have followed the recommendations, and effectiveness evaluates the overall efficacy of the AML/CTF regime in that jurisdiction.²⁶⁸ The FATF methodology acknowledges that jurisdictions must have appropriate, proportionate, and dissuasive sanctions for non-compliance with AML/CTF regulations.²⁶⁹

South Africa's 2021 MER highlighted key findings that although some ML risks in South Africa are being mitigated, significant risks remain unaddressed.²⁷⁰ For instance, MER,2021 revealed that the country has not adequately addressed the risks related to TF.²⁷¹ Moreover, the sustained period of state capture in South Africa has contributed to the generation of substantial proceeds from corruption and has undermined key agencies responsible for combating ML/TF.²⁷² Corruption was identified as the primary activity through which ML proceeds were generated.²⁷³

Following this, South Africa was placed on the FATF grey list in February 2023, subjecting the country to close monitoring of its AML regulations.²⁷⁴ Additionally, the State Capture Commission investigated several multinational and local companies for their suspected

²⁶⁷ FATF Mutual evaluation report: Anti-money laundering and counter-terrorist financing measures – South Africa (2021) available at *Mutual-Evaluation-Report-South-Africa.pdf* accessed on 04.05.2023.

²⁶⁸ HM Treasury 'Review of the UK's AML/CFT regulatory and supervisory regime' June 2022 available at https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/1085407/MLRs_Review_Report_-_2.5_for_publication.pdf accessed on 08.06.2023.

²⁶⁹ Ibid at 43.

²⁷⁰ FATF Mutual evaluation report: Anti-money laundering and counter-terrorist financing measures – South Africa (2021) available at *Mutual-Evaluation-Report-South-Africa.pdf* accessed on 04.05.2023.

²⁷¹ Ibid.

²⁷² Ibid at 5.

²⁷³ Christelle Ahlers op cit note 30 at 29.

²⁷⁴ FATF 'black and grey lists' available at "*Black and grey" lists (fatf-gafi.org)* accessed on 30/03/2023.

involvement in state capture and the exploitation of governmental institutions.²⁷⁵ Examples include consulting firms like Bosasa, Glencore, McKinsey and Bain, as well as legal entities involved in the Free State asbestos project, which were implicated in dishonest practices.²⁷⁶ The report from the State Capture Commission revealed that certain businesses, linked to politically connected enterprises such as the Gupta family, benefited from access to lucrative state contracts.²⁷⁷ However, the findings against private companies involved in state capture projects were relatively limited in the commission's report.²⁷⁸ This is a clear illustration that the narrow focus of only natural persons as PEPs in South Africa's AML/CTF regime hinders its ability to address these illicit activities comprehensively. By broadening the scope of PEPs to include legal entities, South Africa can strengthen its efforts in combatting ML/TF and mitigate the risks associated with corruption in ML practices and state capture.

In South Africa, PEP regulation is incorporated into FICA.²⁷⁹ However, before the 2022 amendment, South Africa had no PEP regulation despite having the FIC Guidance Note 3, which was exclusively applicable to banks.²⁸⁰ The amendment follows the State Capture Commission's exposure of PEPs being linked to corruption, involving inter alia legal entities.²⁸¹ Overall, the 2022 Amendment amended South Africa's AML/CTF regime. Despite the consensus that a PEP is a natural person,²⁸² the exclusion of legal entities has a major negative impact in South Africa, as it

²⁷⁵ Volume 3 of the State Capture report available at *Judicial Commission of Enquiry into State Capture report - part 1 | South African Government (www.gov.za)* accessed on 25/3/2023

²⁷⁶ Volume 3 of the Commission of Inquiry into State Capture report available at *Court Judgments - Commission of Inquiry into Allegations of State Capture*, accessed on 13/03/2023.

²⁷⁷ Ibid; Corruption news 'private sector needed at the state capture solution table' *Corruption Watch* 29 June 2022 available at <https://www.corruptionwatch.org.za/private-sector-needed-at-the-state-capture-solutions-table/> accessed on 15/05/2023.

²⁷⁸ Ibid.

²⁷⁹ Section 42 of FICA; Schedule 3A and 3B of FICA; Section 39 of the 2022 Amendment.

²⁸⁰ FATF/ ESAAMLG Mutual evaluation report: Anti-money laundering and counter-terrorist financing measures – South Africa (2009) available at <https://www.fatf-gafi.org/content/dam/fatf-gafi/mer/MER%20South%20Africa%20full.pdf.coredownload.pdf> accessed on 15.11.2023. at 103.

²⁸¹ Commission of Inquiry into State Capture report available at *Court Judgments - Commission of Inquiry into Allegations of State Capture*, accessed on 13/03/2023.

²⁸² The Wolfsberg Group 'Wolfsberg guidance on Politically Exposed Person("PEP")' available at *Wolfsberg Frequently Asked Questions ("FAQ's") on (wolfsberg-principles.com)*, accessed on 05/03/2023.

hinders its ability to substantively comply with FATF standards, which results in placement in the FATF grey list.²⁸³ South Africa has since addressed the technical compliance deficiencies found in MER,2021 with substantial progress. The FATF has published its most recent report, which details South Africa's attempts to strengthen its AML/CTF measures.²⁸⁴ Recommendation 12 on PEP has changed from being non-compliant to largely compliant, according to the report's key findings.²⁸⁵ South Africa has made progress in strengthening AML/CFT measures.

4.5. CONCLUSION

In South Africa, ML has been criminalised by the Prevention of Organised Crime Act, of 1998.²⁸⁶ The development of ML regulation in South Africa can be traced back to 1992 with the enactment of the Drug and Drug Trafficking Act 140 of 1992. South Africa has had regulations to prevent ML for over thirty years. This initial legislation primarily focused on addressing ML related to drug-related crimes.²⁸⁷ Subsequently, in 1996, the Proceeds of Crimes Act was introduced to further strengthen the ML regulation in the country. The Proceeds of Crimes Act²⁸⁸ expanded the scope of ML regulations in South Africa to include the proceeds from all kinds of crimes.²⁸⁹ On the other hand, TF in South Africa is criminalised by the Protection of Constitutional Democracy Against Terrorist and Related Activities Act 33 of 2004. Finally, in 2001, the Financial Intelligence Centre Act²⁹⁰ was established to further strengthen the framework for AML/CTF in South Africa and jointly regulate ML/TF.

Despite South Africa's longstanding commitment to combatting ML/TF, the effectiveness of its AML/CTF enforcement remains limited. The 2022 Amendment introduced the concept of

²⁸³ FATF 'black and grey lists' available at "*Black and grey*" lists ([fatf-gafi.org](https://www.fatf-gafi.org)) accessed on 30/03/2023.

²⁸⁴ FATF (2023), Anti-money laundering and counter-terrorist financing measures – South Africa, 2nd Enhanced Follow-up Report, FATF, Paris available at <https://www.fatf-gafi.org/content/dam/fatf-gafi/fur/South-Africa-FUR-2023.pdf.coredownload.inline.pdf> accessed on 04.12.2023.

²⁸⁵ Ibid.

²⁸⁶ Section 4 of the Prevention of Organised Crime Act, 1998.

²⁸⁷ Ibid at 18.

²⁸⁸ Proceeds of Crimes Act 76 of 1996.

²⁸⁹ Ibid.

²⁹⁰ Financial Intelligence Centre Act 38 of 2001.

PIPs, which expands the scope of PEPs beyond the FATF scope.²⁹¹ South Africa's PIP concept encompasses a broader category of individuals who may have significant influence or control over legal entities within both the private and the public sectors.²⁹² While PEPs are generally associated with public officials, South Africa's PIPs include individuals from the private sectors, such as corporate executives and governance. The introduction of PIPs reflects a recognition that individuals outside the realm of public office can also play a crucial role in illicit financial activities. The rationale for widening the scope to include PIPs lies in the understanding that illicit financial flows can occur through various channels, not limited to public officials alone. For South Africa to get removed from the FATF grey list, the FATF first needs to be convinced that South Africa's efforts are effective in combatting ML/TF.

²⁹¹ The 2022 Amendment.

²⁹² Schedule 3C of FICA.

CHAPTER 5 AN ANALYSIS OF THE POLITICALLY EXPOSED PERSON REGULATORY FRAMEWORK

5.1. INTRODUCTION

In the preceding chapters, we explored the international, foreign and South African regulation of ML/TF through a combination of international and regional instruments, as well as domestic legislation adopted by South Africa and the UK within their respective jurisdictions. This dissertation primarily investigates how these regulatory frameworks were incorporated into the legal systems of South Africa and the UK. A central focus lies in addressing the common challenge faced by both countries: the limited effectiveness of provisions related to PEPs in combating ML and TF. This limitation often stems from the narrow scope of the PEP definition. Notably, the EU's definition of PEPs stands out due to its recognition of legal entities associated with PEPs and their family members as falling within this category. It is thought to be the best-established definition.²⁹³ It's important to note that the UK also benefits from a similar approach. Thus, this section will compare and contrast the PEP regulations in South Africa, the EU and the UK, with the suggestion that, in order to be effective, South Africa needs to broaden its PEP scope and potentially adopt other desirable features from the EU and the UK. Conversely, the suggestion is that the UK could benefit from incorporating certain features from South Africa. Furthermore, the section looks at the South African AML/CTF regime on PEP and its connection to the Wolfsberg Group, as well as the UK AML/CTF regime on PEPs and its relationship to the AMLDs. Ultimately, the focus is on advocating for further revisions in PEP regulation, emphasising the inclusion of legal entities within the scope.

5.2. COMPARATIVE OVERVIEW

Under the Third AMLD regime, institutions were able to treat domestic PEPs differently from foreign PEPs. The UK is examined in this dissertation. Though it has left the European Union, its framework for PEPs was developed while it was still bound to the European Union directives. Consequently, the UK allowed for the treatment of domestic PEPs to be distinct from that of

²⁹³ Christelle Ahlers op cit note 30 at 78.

foreign PEPs prior to the Fourth AMLD.²⁹⁴ However, the PEP scope was extended to include domestic PEPs under the EU's Fourth AMLD.²⁹⁵ Furthermore, the FATF Mutual Assessment Guidelines of countries' AML regimes did not stipulate that PEP regulations must be widened to encompass domestic PEPs.²⁹⁶ In the UK, financial institutions were only required to include EDD with foreign PEPs as implied by the PEP definition. This position had since changed and for the longest time, the strategy in the UK was not to differentiate domestic and foreign PEPs.²⁹⁷ Until 2023, when the country reverted to differentiating between domestic and foreign PEPs.

PEP regulation in the UK, is done through the MLRs, which are secondary to POCA²⁹⁸ and were used to implement the AMLDs in the UK while it was still a member of the EU.²⁹⁹ At present, the PEP definition is contained in the MLRs, 2017, which inter alia sets out the EDD that PEPs need to comply with.³⁰⁰ Prior to the MLRs, PEPs in the UK had no established definition.³⁰¹ The UK has incorporated PEP regulation in its domestic law since 2007.

As a consequence of South Africa's ratification of the UNCAC, the country undertook the obligation to incorporate regulations related to PEPs. UNCAC mandates its member states to provide guidelines on when to apply EDD domestically to combat corruption, and financial

²⁹⁴ HM Treasury 'Review of the UK's AML/CFT regulatory and supervisory regime' June 2022 available at https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/1085407/MLRs_Review_Report_-_2.5_for_publication.pdf accessed on 08.06.2023.

²⁹⁵ Article 52 of the UNCAC.

²⁹⁶ Jackie Johnson op cit note 7 at 291.

²⁹⁷ Section 3(9) of the Fourth AMLD. It creates no distinction between domestic and foreign PEPs.

²⁹⁸ Proceeds of Crime Act 2002.

²⁹⁹ Money Laundering Regulations 2007 and Money Laundering, Terrorist Financing and Transfer of Funds (information on the payer) Regulations 2017 available at <https://www.legislation.gov.uk/ukxi/2007/2157/regulation/14/made> accessed on 21.11.2023 and *The Money Laundering, Terrorist Financing and Transfer of Funds (Information on the Payer) Regulations 2017* (legislation.gov.uk) accessed on 19.11.2023.

³⁰⁰ Regulation 35(12) of the MLRs, 2017 available at *The Money Laundering, Terrorist Financing and Transfer of Funds (Information on the Payer) Regulations 2017* (legislation.gov.uk) accessed on 19.11.2023.

³⁰¹ HM Treasury 'Review of the UK's AML/CFT regulatory and supervisory regime' June 2022 available at https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/1085407/MLRs_Review_Report_-_2.5_for_publication.pdf accessed on 08.06.2023.

institutions must always apply EDD on PEPs.³⁰² There was no legislative or regulatory mandate in FICA prior to 2022 that was expressly directed at PEPs.³⁰³ Therefore no legal obligation existed under FICA requiring the identification of PEPs or the application of EDD to PEPs since FIC Guidance Note 3 does not qualify as a regulation or ‘... other enforceable means’.³⁰⁴ Most recently, following the amendment, FICA now incorporates PEP regulation.³⁰⁵ Given that UNCAC has stricter guidelines than the FATF regarding PEPs, which South Africa was not in compliance with, that is prior to the 2022 Amendment.³⁰⁶ South Africa was even more non-compliant with UNCAC. South Africa had no PEP regulation until recently. Contrarily, as above stated, the UK has incorporated PEP regulation in its domestic law since 2007.

South Africa ratified the UNCAC, which mandates its member states to provide guidelines on when to apply EDD domestically to combat corruption and that financial institutions must always apply EDD on PEPs.³⁰⁷ Given that UNCAC has stricter guidelines than the FATF regarding PEPs, South Africa was not in compliance with it,³⁰⁸ before the 2022 Amendment, when it was not in compliance with the FATF PEP requirements.³⁰⁹ Thus, despite the 2003 FATF Recommendations excluding domestic PEPs, South Africa had an obligation to regulate domestic PEPs under the AUCPCC. At present, it is no longer necessary for South Africa to rely on AUCPCC because the 2012 FATF Recommendations now aligns with UNCAC, particularly, the extension of the FATF's PEP scope to include domestic, foreign, and international PEPs. Presently, PEP regulation is governed by FICA. The 2022 Amendment,³¹⁰ follows the State Capture Commission's exposure

³⁰² Article 52 of the UNCAC.

³⁰³ FATF/ ESAAMLG Mutual evaluation report: Anti-money laundering and counter-terrorist financing measures – South Africa (2009) available at <https://www.fatf-gafi.org/content/dam/fatf-gafi/mer/MER%20South%20Africa%20full.pdf.coredownload.pdf> accessed on 15.11.2023. page 103.

³⁰⁴ FATF/ ESAAMLG Mutual evaluation report: Anti-money laundering and counter-terrorist financing measures – South Africa (2009) available at <https://www.fatf-gafi.org/content/dam/fatf-gafi/mer/MER%20South%20Africa%20full.pdf.coredownload.pdf> accessed on 15.11.2023. (pages 103,104)

³⁰⁵ Section 42 of FICA; Schedule 3A and 3B of FICA; Section 39 of the 2022 Amendment.

³⁰⁶ Christelle Ahlers op cit note 30 at 101.

³⁰⁷ Article 52 of the UNCAC.

³⁰⁸ Christelle Ahlers op cit note 30 at 101.

³⁰⁹ The 2022 Amendment amended South Africa's AML/CTF regime.

³¹⁰ Ibid.

of PEPs being linked to corruption, involving, inter alia, legal entities.³¹¹ Despite the consensus that a PEP is a natural person,³¹² the exclusion of legal entities has a major negative impact on countries like South Africa, as it hinders the ability to comply substantively with FATF standards and has resulted in its placement in the FATF grey list in 2023.³¹³ However, there has been some substantial progress in this area, as South Africa has since addressed the technical compliance deficiencies found in its Mutual Evaluation Report from 2021.³¹⁴ In the FATF's most recently published Follow-Up Report, which details South Africa's attempts to strengthen its AML/CTF measures,³¹⁵ the report's key findings reveal that Recommendation 12 on PEP has changed from being non-compliant to largely compliant.³¹⁶ Unfortunately, South Africa is still on the grey list even after making efforts to improve its AML/CFT standards. Therefore, in order to guarantee adequate AML/CTF measures, a more stringent PEP regulation that encompasses legal entities is required.

The FATF standards are non-binding.³¹⁷ Contrarily, the AMLDs unlike the FATF Standards are binding as it includes binding legal commitments that supersede national legislative frameworks in each member state and are enforceable by the EU.³¹⁸ Despite its non-binding nature, the FATF effectively enforces its standards through a system of name and shame. Countries failing to comply with these standards find themselves on the FATF black or grey list. This inclusion signals weak AML/CTF regimes, posing a threat to global security. Additionally, the FATF standards, although not legally binding, gain practical enforceability through periodic peer

³¹¹ Commission of Inquiry into State Capture report available at *Court Judgments - Commission of Inquiry into Allegations of State Capture*, accessed on 13/03/2023.

³¹² The Wolfsberg Group 'Wolfsberg guidance on Politically Exposed Person("PEP")' available at *Wolfsberg Frequently Asked Questions ("FAQ's") on (wolfsberg-principles.com)*, accessed on 05/03/2023.

³¹³ FATF 'black and grey lists' available at "*Black and grey" lists (fatf-gafi.org)* accessed on 30/03/2023.

³¹⁴ FATF (2023), Anti-money laundering and counter-terrorist financing measures – South Africa, 2nd Enhanced Follow-up Report, FATF, Paris available at <https://www.fatf-gafi.org/content/dam/fatf-gafi/fur/South-Africa-FUR-2023.pdf.coredownload.inline.pdf> accessed on 04.12.2023.

³¹⁵ Ibid.

³¹⁶ Ibid.

³¹⁷ Nicholas W. Turner op cit note 12 at 548.

³¹⁸ Umut Turksen, Ismail Ufuk Misirlioglu and Osman Yukselturk 'Anti-money laundering law of Turkey and the EU: an example of convergence?' 14 *JMLC* 279 at 281.

reviews. These reviews assess the strengths and weaknesses of AML/CTF frameworks in various countries. PEP regulation is contained in Recommendation 12 of the FATF Standards,³¹⁹ and beneficial ownership³²⁰ is regulated separately by Recommendation 24.³²¹ In South Africa, PEP regulation is covered by s21F, s21G and s21H as well as Schedules A, B and C of FICA, and similar to the FATF, beneficial ownership is regulated separately by s21B of FICA as well as the Companies Act 71 of 2008³²² and other Acts. In the EU, however, PEP's definition incorporates beneficial ownership. Thus PEP regulation in the EU addresses natural persons and legal entities simultaneously.³²³ The PEP definition encompasses immediate family members and known close associates, and in the Fourth AMLD, known close associates of a PEP are natural persons who either have sole beneficial ownership of a legal entity or arrangement that is known to have been established for the de facto benefit of a PEP, or who are believed to have beneficial ownership of these entities with a PEP jointly.³²⁴ Similarly, in the UK, PEP regulation also incorporates beneficial ownership.³²⁵ This is because the MLRs were enacted as national legislative frameworks in order to implement the EU AMLDs.³²⁶ The UK also reproduced the EU's definition of 'known close associates' in its MLRs 2017.³²⁷ FICA, on the other hand, does not define 'known close associates', only identifying family members of a PEP.³²⁸

³¹⁹Recommendation 12 of the FATF Recommendations, 2012.

³²⁰ Beneficial regulations regulate the individuals behind the legal entity by taking into account their beneficial interests therein.

³²¹ Recommendation 24 of the FATF Recommendations available at <https://www.fatf-gafi.org/content/dam/fatf-gafi/guidance/Guidance-Beneficial-Ownership-Legal-Persons.pdf.coredownload.pdf> accessed on 11.12.2023.

³²² Sections 33(1) (Aa) – addresses the security register; 56(7) (aA) – addresses the registration of beneficial interest in a legal entity; 56(14) – addresses the filing of beneficial ownership register with CIPC; 214 – addresses criminal sanctions.

³²³ The Fourth AMLD available at <https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=celex%3A32015L0849> accessed on 19.11.2023.

³²⁴ Article 3(11) *ibid*.

³²⁵ Regulation 35(12) of the MLRs, 2017.

³²⁶ HM Treasury 'Review of the UK's AML/CFT regulatory and supervisory regime' June 2022 available at https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/1085407/MLRs_Review_Report_-_2.5_for_publication.pdf accessed on 08.06.2023.

³²⁷ Regulation 35(12)(c) *ibid*; Article 3(11) of the Fourth AMLD.

³²⁸ Section 21H of FICA.

Unlike its counterparts in the EU and the UK, the PEP definition in South Africa does not incorporate beneficial ownership regulation and ultimately excludes legal entities. However, it is important to note that, despite the incorporation of beneficial ownership within the PEP definition, the effectiveness of the regulation of PEPs through the partial regulation of legal entities, remains limited as it still only focuses on the individuals who are behind the legal entities rather than the actual legal entity.

5.3. THE SCOPE OF A POLITICALLY EXPOSED PERSON

The PEP definition within the framework of AML/CTF as set out by the FATF focuses exclusively on natural persons.³²⁹ This limitation was alluded to by the Wolfsberg Group, which asserts that the fundamental aspect of the PEP definition is that it applies to natural persons.³³⁰ The FATF definition pertains to individuals, which is consistent with the Wolfsberg Group’s reiterations.³³¹ The identification and customer due diligence processes for PEPs are also primarily centred around natural persons.³³² Within this context, the requirements for financial institutions and supervisory authorities were developed based on a model that emphasises personal links to natural persons with political influence.³³³ Consequently, even the application of EDD measures primarily revolves around establishing a direct connection between natural persons by financial institutions.

It is pivotal for legal entities to be encompassed within the scope of PEPs, to address the need for equal scrutiny applied to legal entities as is done with natural persons,³³⁴ as failure to scrutinise legal entities, financial institutions, and regulators may inadvertently facilitate ML/TF activities.³³⁵ The experience within the ESAAMLG has highlighted the importance of not only

³²⁹ Daniele Canestri op cit note 43 at 360; Jackie Johnson op cit note 7 at 292.

³³⁰ The Wolfsberg Group ‘Wolfsberg guidance on Politically Exposed Person(“PEP”)’ available at *Wolfsberg Frequently Asked Questions (“FAQ’s”) on (wolfsberg-principles.com)*, accessed on 05/03/2023.

³³¹ Ibid.

³³² Daniele Canestri op cit note 43 at 360.

³³³ Ibid at 363.

³³⁴ Daniele Canestri op cit note 43 at 360.

³³⁵ Goredema, C. and Madzima, J. ‘An assessment of the links between corruption and the implementation of anti-money laundering strategies and measures in the ESAAMLG region’ available at https://www.esaamlg.org/reports/Corruption_and_AML_Systems..pdf accessed on 06.12.2023 at 15-16.

profiling PEPs but also examining the institutions involved in corrupt activities.³³⁶ Thus moving away from the natural person-centred approach. The observation is that while measures are in place to scrutinise individuals holding prominent public positions, there was a gap in addressing the potential risks posed by legal entities.³³⁷ On this account, the EU expanded the definition of PEPs in its AMLDs.³³⁸

The EU expanded the definition of PEPs in its Third AMLD, published in November 2005, to include, among other things, any legal entity whose beneficial owner is a PEP's family member.³³⁹ This is reflected in Article 3 of the Fourth AMLD, thus, expanding the scope of PEPs beyond natural persons.³⁴⁰ Despite the expansion, however, the EU PEP definition is still limited because it excludes legal entities that lack a well-defined connection with an individual PEP who serves as a beneficial owner, even if they engage in transactions or interactions with state organs.³⁴¹ The concerns were also addressed by FATF in a separate recommendation under Recommendation 24 on beneficial ownership which stipulates that jurisdictions must take steps to prohibit the use of legal entities for ML/TF.³⁴²

In March 2022, the FATF reached a consensus on more stringent global standards concerning beneficial ownership through Recommendation 24, which necessitates jurisdictions to guarantee that relevant agencies possess sufficient, precise, and up-to-date information regarding the beneficial owners of legal entities.³⁴³ This Recommendation requires all financial institutions to perform EDD on legal entities associated with PEPs.

While international reform regarding PEPs is essential, South Africa has taken strides to broaden the scope of PEPs by introducing the PIP category, which includes certain office bearers

³³⁶ Ibid at 16-17.

³³⁷ Daniele Canestri op cit note 43 at 359.

³³⁸ Christelle Ahlers op cit note 30 at 78.

³³⁹ Ibid at 78.

³⁴⁰ Article 3(8) of the Third AMLD.

³⁴¹ Article 3(9) of the Fourth AMLD.

³⁴² FATF (2023) Guidance on beneficial ownership for legal persons' available on <https://www.fatf-gafi.org/en/publications/Fatfrecommendations/Guidance-Beneficial-Ownership-Legal-Persons.html#:~:text=It%20aims%20to%20assist%20policy,links%20to%20crime%20or%20terrorism>. accessed on 28.05.2023.

³⁴³ Ibid.

within legal entities, expanding beyond the traditional focus on public officials.³⁴⁴ Under the new PIP regulation, the evaluation focuses on the proximity and association with the government as a legal entity, however, only the natural persons managing the legal entity are regarded as PEP.³⁴⁵

It is important to acknowledge that this expansion remains limited, as it primarily revolves around natural persons. Despite the limitation, however, the consideration of the potential risks and vulnerabilities that may arise from conducting financial transactions or engaging in business relationships with the government in the South African PIP regulation is a great feature. Furthermore, the South African Companies Act has been amended to permit the Companies and Intellectual Property Commission (CIPC), which is responsible for the registration and maintenance of companies, co-operatives, intellectual property rights, and disclosure of information on its business registers, to collect beneficial ownership of legal entities within its register.³⁴⁶ Understanding that failure to regulate legal entities, financial institutions, and regulators may inadvertently facilitate ML/TF activities.³⁴⁷ This demonstrates progress on the part of South Africa in preventing the abuse of corporate bodies to facilitate ML/TF. The implementation of a beneficial ownership register partially addresses the issues addressed in this dissertation.

5.3.1. *GLENCORE ENERGY LIMITED*

The exclusion of legal entities from the scope of PEPs has been demonstrated to present significant risks to the global financial system, as illustrated by the Glencore Energy Limited UK (Glencore UK) scandal.³⁴⁸ In the Glencore UK case, prosecutors alleged that Glencore UK's employees and agents utilised private jets to transfer cash to pay bribes in several African countries, thereby

³⁴⁴ Schedule 3C of the FICA.

³⁴⁵ Ibid.

³⁴⁶ Ibid.

³⁴⁷ Goredema, C. and Madzima, J. 'An assessment of the links between corruption and the implementation of anti-money laundering strategies and measures in the ESAAMLG region' available at https://www.esaamlg.org/reports/Corruption_and_AML_Systems..pdf accessed on 06.12.2023 at 15-16.

³⁴⁸ Glencore Energy Limited is discussed further in para 5.3.1. Serious Fraud Office 'Glencore to pay £280 million for highly corrosive and endemic corruption' available at <https://www.sfo.gov.uk/2022/11/03/glencore-energy-uk-ltd-will-pay-280965092-95-million-over-400-million-usd-after-an-sfo-investigation-revealed-it-paid-us-29-million-in-bribes-to-gain-preferential-access-to-oil-in-africa/> accessed on 29.06.2023.

violating AML principles. Glencore pleaded guilty to bribery offences exceeding US\$100 million in the Democratic Republic of Congo, Cameroon, Côte d'Ivoire, Equatorial Guinea, Nigeria, and South Sudan, both in a US court in late May 2022 and a UK court in June 2022.³⁴⁹ In addition, the company admitted guilt to other bribery offences in Brazil and Venezuela, as well as market manipulation in the US. This UK-incorporated company effectively corrupted governments all over the world. Not only that, it enabled ML. In South Africa, Legislator Phiwaba Madokwe expressed concerns about Glencore's corrupt reputation and questioned whether South Africa should allow such a company to operate within its borders, especially considering the nation's strong stance against corruption.³⁵⁰ The pervasive corruption and ML activities within Glencore serve as a clear indication of the necessity for a comprehensive approach to combat financial crimes. It highlights the importance of implementing effective measures to deter and prevent illicit activities associated with corrupt legal entities.³⁵¹

Further, it was suggested that the South African government, in collaboration with relevant institutions such as the National Prosecuting Authority and the Special Investigating Unit should conduct a thorough investigation into all of Glencore's activities within the country. Unfortunately, no investigations were conducted against Glencore South Africa despite concerns raised regarding its involvement in corrupt activities.³⁵² On this point, Corruption Watch³⁵³ suggested that the State Capture Commission's Report lacked thorough findings against private companies, including

³⁴⁹ *Serious Fraud Office v Glencore* [2022] EWCR 1.

³⁵⁰ Anathi Madubela 'Parliament to shine spotlight on Glencore operations' *Mail & Guardian* 23/08.2022 available at <https://mg.co.za/business/2022-08-23-parliament-to-shine-spotlight-on-glencore-operations/> accessed on 16/05/2023.

³⁵¹ Parliament of the Republic of South Africa 'Committee on mineral resources to determine a way forward on assessment of Glencore's activities at a later stage' available at <https://www.parliament.gov.za/press-releases/media-statement-committee-mineral-resources-determine-way-forward-assessment-glencores-activities-later-meeting> accessed on 16/05/2023.

³⁵² Paddy Harper 'Brian Molefe calls for investigation of Glencore's South African operations' *Mail & Guardian* 01.06.2022 available at <https://mg.co.za/politics/2022-06-01-brian-molefe-calls-for-investigation-of-glencores-south-african-operations/> accessed on 16/05/2023.

³⁵³ Corruption Watch is a Transparency International chapter, a global movement that seeks to stop corruption and promote transparency.

Glencore, that participated in projects associated with corruption.³⁵⁴ This highlights the dangers posed by the exclusion of legal entities from the scope of PEPs, to be subjected to EDD and ongoing monitoring.

5.3.2. AFRICAN GLOBAL OPERATIONS (FORMERLY BOSASA OPERATIONS)

In addition to the concerns surrounding Glencore, the State Capture Commission revealed Bosasa's involvement in the extensive corruption and ML activities in South Africa.³⁵⁵ Bosasa Operations was a controversial South African company that gained notoriety due to its involvement in corruption scandals. Its activities were closely scrutinised during the state capture investigations. Whistleblower testimonies indicated that Bosasa was awarded lucrative state contracts worth R2.3 billion after paying bribes totalling R75 million to government officials.³⁵⁶ Large sums of cash were stored in bundles and boxes at Bosasa offices to facilitate bribery payments. Evidence presented during the state capture commission revealed that between R2 million and R6.5 million in cash was held on the property.³⁵⁷ Notwithstanding the cash threshold requirement, these amounts were not reported.³⁵⁸ To combat ML/TF activity, the Amendment of Money Laundering and Terrorist Financing Control Regulations required various institutions to report transactions involving any dealing in cash of more than R24.999 to the Financial Intelligence Centre (FIC),³⁵⁹ even if they did not appear suspicious.³⁶⁰ The State Capture Commission's findings emphasised that Bosasa's corrupt practices significantly heightened the

³⁵⁴ Parliament of the Republic of South Africa 'Mineral Resources committee agrees on an approach to Glencore and alleged misuse of rehabilitation funds' available at <https://www.parliament.gov.za/press-releases/media-statement-mineral-resources-committee-agrees-approach-glencore-and-alleged-misuse-mining-rehabilitation-funds> accessed on 16/05/2023.

³⁵⁵ Volume 3 of the Commission of Inquiry into State Capture report available at *Court Judgments - Commission of Inquiry into Allegations of State Capture*, accessed on 13/03/2023.

³⁵⁶ Volume 3, Part 3 *ibid*.

³⁵⁷ Volume 3, Part 1 and 4 *ibid*.

³⁵⁸ Section 28 of the FICA.

³⁵⁹ As of 14 November 2022, the prescribed threshold changed from R24 999.99 to R49 999.99.

³⁶⁰ Amendment Of Money Laundering and Terrorist Financing Control Regulations (GN R867 in GG 33596 of 01 October 2010).

risks of ML/TF.³⁶¹ Bosasa further highlights the dangers posed by the exclusion of legal entities from the scope of PEPs.

5.3.3. NEDBANK

The findings of the State Capture Commission have raised serious concerns regarding the potential involvement of financial institutions in questionable activities. In addition to Glencore and Bosasa concerns, Nedbank's involvement with Regiment Capital, a company associated with the Gupta family came under scrutiny during the State Capture investigations.³⁶² The State Capture Report highlighted potential criminal activities involving Nedbank, allegedly having an arrangement with Regiments.³⁶³ The revelations concerning Nedbank's interactions with Regiment Capital and ACSA highlight the importance of scrutinising legal entities because they end up tainting financial institutions and this could have a dire effect on the integrity of the global financial system. The state capture highlights the deficiencies within South Africa's AML/CTF legal framework. This situation is particularly concerning because it involves financial institutions that bear the responsibility of implementing these regulations.

In contrast, the UK safeguards its AML/CTF regime more efficiently and it has PEP regulation that encompasses legal entities. The UK seem to be more advanced in addressing corruption in both public and private sectors, particularly in the private sector.³⁶⁴ As opposed to South Africa, which has a grey-list status and a state-capture commission of inquiry, the UK's private sector is not deeply compromised. This could be because it adopted the legal entity-encompassing EU PEP

³⁶¹ Volume 3, Part 4 of the Commission of Inquiry into State Capture report available at *Court Judgments - Commission of Inquiry into Allegations of State Capture*, accessed on 13/03/2023.

³⁶² FATF Mutual evaluation report: Anti-money laundering and counter-terrorist financing measures – South Africa (2021) available at *Mutual-Evaluation-Report-South-Africa.pdf* accessed on 04.05.2023.

³⁶³ Sarah Smit 'Nedbank features negatively in state capture report; Standard Bank defends itself' *Mail & Guardian* 18.01.2022 available <https://mg.co.za/business/2022-01-18-nedbank-features-negatively-in-state-capture-report-standard-bank-defends-itself/> accessed on 16.05.2023; Due to time constraints, the state capture commission did not hear Nedbank's response to these allegations.

³⁶⁴ HM Treasury 'Review of the UK's AML/CFT regulatory and supervisory regime' June 2022 available at https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/1085407/MLRs_Review_Report_-_2.5_for_publication.pdf accessed on 08.06.2023.

model, despite its limitation of only focusing on the individuals who are behind the legal entities rather than the actual legal entity.

5.4. PREVALENT ISSUES RELATING TO POLITICALLY EXPOSED PERSONS

As stated earlier, the FATF has developed international standards, and these standards are internationally endorsed global standards for implementing effective AML/CTF.³⁶⁵ Even without clear, legal sanction under international law, the FATF has had significant success harmonising national legal and regulatory frameworks. It has done so by assessing its members' compliance with the FATF standards through a peer review process of mutual evaluations.³⁶⁶

According to the UK's 2018 Mutual Evaluation Report, the country demonstrated a great degree of compliance with the technical standards of the FATF, positioning it among the top-performing nations in the world.³⁶⁷ However, to improve its AML efficacy, the UK was given priority actions by the FATF. These actions specifically focused on areas such as improving the quality of financial intelligence accessible to UK law enforcement agencies. The FATF also highlighted some specific weaknesses in the regulated sector's understanding of risk and the effectiveness of the preventative measures implemented.³⁶⁸

In South Africa, following the release of the 2021 Mutual Evaluation Report,³⁶⁹ South Africa was placed on the FATF grey list in February 2023, subjecting the country to rigorous scrutiny of its AML/CTF regulations.³⁷⁰ The nation is currently working towards reinstatement by demonstrating its commitment to adopting and effectively implementing FATF standards. In response to the extensive ML harms perpetrated by corrupt legal entities during the state capture era, South Africa has embarked on regulatory reforms to counter such illicit activities.³⁷¹ By implementing EDD measures on legal entities, financial institutions can better mitigate the risks

³⁶⁵ Nicholas W. Turner op cit note 12 at 548.

³⁶⁶ Ibid at 548.

³⁶⁷ AML/CTF United Kingdom Mutual Evaluation Report, 2018 available at <https://www.fatf-gafi.org/content/dam/fatf-gafi/mer/MER-United-Kingdom-2018.pdf.coredownload.pdf> accessed on 27.11.2023.

³⁶⁸ Ibid.

³⁶⁹ FATF Mutual evaluation report: Anti-money laundering and counter-terrorist financing measures – South Africa (2021) available at [Mutual-Evaluation-Report-South-Africa.pdf](#) accessed on 04.05.2023.

³⁷⁰ FATF 'black and grey lists' available at "[Black and grey](#)" lists ([fatf-gafi.org](https://www.fatf-gafi.org)) accessed on 30/03/2023.

³⁷¹ Cayle Lupton op cit 219 at 43.

associated with PEP-related illicit financial activities. South Africa has clear trends of corruption in both the public and the private sectors.³⁷² On this account, the State Capture Report has implicated two prominent banks in South Africa, and this has exposed deficiencies within South Africa's AML/CTF legal framework.³⁷³ This situation is particularly concerning because it involves financial institutions, which is a sector that bears the responsibility of implementing these regulations. This sheds light on vulnerabilities in the South African AML/CTF framework, particularly considering South Africa's grey-listing status.³⁷⁴ South Africa's AML/CTF evaluation in its 2021 MER highlighted these deficiencies. The absence of rigorous explicit requirements for legal entities that despite not being closely connected to a natural person PEP can facilitate ML by exploiting their connections to the state is addressed in this section. Recognising the significance of expanding the scope of PEPs to include legal entities, countries like South Africa can strengthen their AML/CTF legal frameworks and help them evade the grey list status.

5.5. LIMITATIONS UNDER THE PRESENT SCOPE

Meanwhile, in the EU, the Fourth AMLD's definition of a PEP is thought to be the most comprehensive definition,³⁷⁵ and the same has been adopted by the UK. Although the EU-UK approach is better than the South African approach at present, it also remains limited in that it excludes legal entities that lack a well-defined connection with a natural person PEP who serves as a beneficial owner, even if the entity engages in transactions or interactions with state organs.

In South Africa, the newly amended Schedule 3C of the FICA³⁷⁶ which lists as examples of PIPs is a move in the right direction, as it recognises that PEP-related risks extend beyond

³⁷² Corruption Watch 'NBI Addressing Corporate Corruption in South Africa-The EOH Experience' available at https://www.corruptionwatch.org.za/wp-content/uploads/2023/08/NBI-Addressing-Corporate-Corruption-in-South-Africa-The-EOH-Experience_29-Aug-2023.pdf accessed on 13.01.2024.

³⁷³ Sarah Smit 'Nedbank features negatively in state capture report; Standard Bank defends itself' *Mail & Guardian* 18.01.2022 available <https://mg.co.za/business/2022-01-18-nedbank-features-negatively-in-state-capture-report-standard-bank-defends-itself/> accessed on 16.05.2023.

³⁷⁴ FATF Mutual evaluation report: Anti-money laundering and counter-terrorist financing measures – South Africa (2021) available at *Mutual-Evaluation-Report-South-Africa.pdf* accessed on 04.05.2023.

³⁷⁵ Christelle Ahlers op cit note 30 at 78.

³⁷⁶ Schedule 3C of FICA.

individual public officials. Despite this being a positive step towards moving away from the narrow definition set by the FATF, South Africa's expansion of the scope of PEPs remains limited, as it continues to focus exclusively on natural persons.³⁷⁷ The provided list of examples although suggestive and not exhaustive, gives the impression that the overarching element of the definition of PEPs is that a PEP is a natural person. In addition, the FIC Guidance Note 3, which was issued particularly for banks,³⁷⁸ references the Wolfsberg Group's principles³⁷⁹ which serves as the foundation for the definition of PEP in South Africa.³⁸⁰ The Wolfsberg Group reiterates that a basic element of the PEP definition is that a PEP is a natural person.³⁸¹ The founding idea of PEP regulation in South Africa is that a PEP is exclusively a natural person.

As above stated, the traditional classification of PEPs primarily focuses on government officials and individuals in public office but given how closely politics and corporations are intertwined in countries like South Africa, a broader scope is necessary.³⁸² On this account, scholars advocate for a broader expansion of the PEP scope. Individuals in high-ranking positions within the private sector, including CEOs of publicly listed companies, should also be subjected to PEP monitoring as these individuals are equally susceptible to corruption and may pose similar risks as their counterparts in the public sector.³⁸³ To improve the EU-UK approach, lessons should be drawn from the South African PIP concept,³⁸⁴ which shifted from the traditional classification which primarily focuses on government officials and individuals in public office.³⁸⁵ To extend the focus on PEPs to the private sector, the central assessment should be whether or not a legal entity

³⁷⁷ Section 18 of the 2022 Amendment; Schedule 3C of FICA.

³⁷⁸ FIC Guidance Note 3.

³⁷⁹ The principles are a resource for practical advice on PEP-related issues.

³⁸⁰ FIC Guidance Note 3.

³⁸¹ The Wolfsberg Group 'Wolfsberg guidance on Politically Exposed Person("PEP")' available at *Wolfsberg Frequently Asked Questions ("FAQ's") on (wolfsberg-principles.com)*, accessed on 05/03/2023.

³⁸² Kim-Kwang Raymond Choo op cit note 42.at 383.

³⁸³ Ibid at 383.

³⁸⁴ Schedule 3A and 3B of FICA; this schedule provides examples of PEPs as inter alia, the position of chairperson of the board of directors, the chairperson of the audit committee, the executive officer; or chief financial officer, of a company (if the company provides goods or services to an organ of state and the annual transactional value of the goods or services or both exceeds an amount determined by the Minister by notice in the Gazette).

³⁸⁵ Section 18 of the 2022 Amendment.

engages in business with a state organ, regardless of its proximity to an individual PEP.³⁸⁶ Furthermore, to ensure a more comprehensive and effective approach to PEP classification in South Africa, it is recognised that it would be crucial for the scope to encompass legal entities.³⁸⁷ Although South Africa has already begun implementing the beneficial ownership regulation, it is suggested that beneficial ownership be incorporated into the PEP definition in addition to being regulated by s21B of FICA, the Companies Act 71 of 2008,³⁸⁸ and other legislation. In this instance, the EU and the UK stand out by recognising legal entities as PEPs.

One of the observations in this dissertation is the observation that legal entities are excluded from the scope of PEPs, despite having the ability to facilitate ML by exploiting its connections to governments. The observation is that while measures are in place to scrutinise individuals holding prominent public positions, there is a gap in addressing the potential risks posed by legal entities conducting business with the state.³⁸⁹ This gap means that the same level of rigorous due diligence applied to PEPs needs to be extended to the category of legal entities.

Recognising the importance of addressing this gap, South Africa's legislature introduced the concept of PIPs which broadened the scope of PEPs beyond the public sector and encompasses individuals involved in the governance and management of companies engaged in transactions with organs of state, particularly those legal entities benefiting from state contracts.³⁹⁰ The revised FICA introduced the PIP category, which includes governance and management personnel of companies involved in dealings with organs of state and beneficiaries of state contracts, thus recognising that PEP-related risks extend beyond individual public officials. However, despite this being a positive step towards moving away from the narrow definition set by the FATF, South Africa's expansion of the scope of PEPs remains limited, as it continues to focus exclusively on natural persons. The scope is still limited so far as it excludes legal entities.

³⁸⁶ Ibid at 383

³⁸⁷ Daniele Canestri op cit note 43 at 360.

³⁸⁸ Sections 33(1) (Aa) – addresses the security register; 56(7) (aA) – addresses the registration of beneficial interest in a legal entity; 56(14) – addresses the filing of a beneficial ownership register with CIPC; 214 – addresses criminal sanctions.

³⁸⁹ Daniele Canestri op cit note 43 at 360.

³⁹⁰ Schedule 3A and 3B of FICA; Section 18 of the 2022 Amendment.

Although at present, South Africa has already begun implementing the beneficial ownership regulation to regulate legal entities, it is suggested that beneficial ownership be incorporated in the PEP definition in addition to being regulated by s21B of FICA, the Companies Act 71 of 2008;³⁹¹ and other legislation. The retention of the natural person element of a PEP in South Africa is seen as a limitation because the justification for expanding the definition of a PEP to include legal entities lies in the understanding that illicit financial flows can occur through various channels thus South Africa should avoid ignoring the risks associated with legal entities independent from their natural person PEP actors.

5.6. CONCLUSION

Although South Africa has moved away from the exclusive focus on the public sector concerning PEP scope and has shifted from primarily focusing on the political sphere to incorporating the private sector,³⁹² its approach is still limiting as it continues to be natural person-centred and does not recognise legal entities separately as PEPs without linkage with a PEP of a natural person. To strengthen its AML/CTF regime further, South Africa should adopt the EU-UK strategy of encompassing legal entities within the PEP scope. Conversely, the suggestion is that the UK could benefit from incorporating certain features from South Africa like the PIP concept. To improve the EU-UK approach, lessons may be drawn from the South African PIP concept,³⁹³ which shifted from the traditional classification which primarily focuses on government officials and individuals in public office.³⁹⁴ To extend the focus on PEPs to the private sector, the central

³⁹¹ Sections 33(1) (Aa) – addresses the security register; 56(7) (aA) – addresses the registration of beneficial interest in a legal entity; 56(14) – addresses the filing of beneficial ownership register with CIPC; 214 – addresses criminal sanctions.

³⁹² Schedule 3C of FICA; the positions of chairperson of the board of directors, the chairperson of the audit committee, the executive officer; or chief financial officer, of a company (if the company provides goods or services to an organ of state and the annual transactional value of the goods or services or both exceeds an amount determined by the Minister by notice in the Gazette) are listed as examples of a PIP.

³⁹³ Schedule 3A and 3B of FICA; It provides examples of PEPs as inter alia, the position of chairperson of the board of directors, the chairperson of the audit committee, the executive officer; or chief financial officer, of a company (if the company provides goods or services to an organ of state and the annual transactional value of the goods or services or both exceeds an amount determined by the Minister by notice in the Gazette).

³⁹⁴ Section 18 of the 2022 Amendment.

assessment should be whether or not a legal entity engages in business with a state organ, regardless of its proximity to an individual PEP.³⁹⁵

However, although the EU, the UK and recently South Africa acknowledge that it is crucial to monitor PEPs' known close associates, and immediate family members, especially those who are beneficial owners of legal entities to mitigate ML and corruption, they still do not understand how the monitoring of beneficial ownership alone leaves out a wide class of legal entities that are not associated with PEPs but are just as susceptible to ML and TF, such as those that conduct business with the government, through state institutions. The rationale for widening the scope to include legal entities lies in the understanding that illicit financial flows can occur through various channels, not limited to public officials alone who are natural persons. Applying EDD directly to legal entities aligns with the notion that legal entities, as separate entities distinct from their natural person actors, can be conduits for ML, corruption, and other illicit financial activities.³⁹⁶

Thus, this dissertation submits that although South Africa, the EU and the UK have already slightly moved away from the FATF's narrow scope, their respective positions are still limiting because they exclude legal entities that are not closely connected with a natural person's PEP. Therefore, there is a need to expand the scope of a PEP beyond natural persons to include legal entities irrespective of their relationship with PEPs, encompassing legal entities whose transactional activities involve governments. With a broader PEP scope, jurisdictions can enhance the effectiveness of their AML/CFT efforts and substantive compliance will follow.

³⁹⁵ Ibid at 383

³⁹⁶ Daniele Canestri op cit note 43 at 359.

CHAPTER 6 FINDINGS AND RECOMMENDATIONS

6.1. INTRODUCTION

From the FATF's perspective, by effectively implementing FATF Standards, countries can secure a more transparent and stable financial system that is more attractive to foreign investors as corrupt and opaque financial systems are inherently unstable.³⁹⁷ The FATF Standards build the capacity for jurisdictions to fight ML/TF. Thus, this research focused on PEP regulation, to ascertain whether the definition of PEPs is effective in combatting ML/TF.

To begin with, in this dissertation, it has been argued that South Africa's PEP definition, which is based on the FATF model, is inadequate since it excludes legal entities. In addition, through examination of the research question, it was ascertained whether the exclusion of legal entities from the category of PEPs renders the PEP regulatory framework ineffective in addressing ML/TF in South Africa. Lastly, whether the UK PEP regulation is sufficient within the international AML/CTF regulatory framework, or does it require improvement?

On this account, this dissertation has found that the expansion of the scope of PEPs to encompass legal entities will enhance the effectiveness of PEP regulation in combating ML/TF. The objective is to promote substantive compliance with the FATF standards and help South Africa get removed from the FATF's grey list. On this, one notable feature of the EU PEP definition is its recognition of PEP status for legal entities and by recognising the inclusion of legal entities in the definition of PEPs.³⁹⁸ Although, the EU approach remains limited in that it excludes a legal entity that does business with an organ of state.

This section concludes the research and provides findings of the comparison, which reveals that the benchmark definition of PEPs by the FATF hinders national efforts to promote substantive compliance with the FATF standards. It suggests a way to respond to this, which is to incorporate legal entities in the definitions of PEPs.

³⁹⁷ Basel Committee on Banking Supervision 'Consultative Document Customer due diligence for banks' available at <https://www.bis.org/publ/bcbs77.pdf> accessed on 22.06.2023.

³⁹⁸ Christelle Ahlers op cit note 30 at 78.

6.2. FINDINGS

6.2.1. SOUTH AFRICA

PEP definitions under South African law when compared to the FATF PEP definition, adhere to international best practices.³⁹⁹ However, the international best practice is too narrow.⁴⁰⁰ The dissertation investigated the effectiveness of the current PEP definition under the FATF standards in combatting ML/TF. According to research, the current definition of a PEP is inadequate to combat ML/TF, implying that a more comprehensive definition of a PEP is necessary.⁴⁰¹ As revealed by inter alia, the season of state capture and the Glencore scandal, the incorporation of legal entities in the PEP regulation in South Africa is necessary.

On this account, the 2022 Amendment,⁴⁰² introduced the concept of PIPs and broadened the scope of PEPs beyond the public sector to include individuals involved in the governance and management of legal entities which engage in transactions with state organs, particularly those legal entities benefiting from state contracts is a step toward the right direction.⁴⁰³ However, the scope remains limited so far as it is natural person-centred and excludes legal entities.⁴⁰⁴

Importantly, according to research based on the FATF's MERs, there seems to be low compliance with FATF Recommendation 12 regarding PEPs, and despite South Africa's recent breakthrough in relating compliance with Recommendation 12, most FATF members are still reported to be non-compliant.⁴⁰⁵ For instance, for the longest time, prior to the 2022

³⁹⁹ Recommendation 12 of the FATF Recommendations, 2012 at 16; Schedule 3A and 3B of FICA.

⁴⁰⁰ Kim-Kwang Raymond Choo op cit note 42 at 383; Daniele Canestri op cit note 43 at 360.

⁴⁰¹ Ibid at 383.

⁴⁰² General Laws (Anti-Money Laundering and Combating Terrorism Financing) Amendment Act 22 of 2022.

⁴⁰³ Schedule 3A and 3B of FICA; It provides examples of PEPs as inter alia, the position of chairperson of the board of directors, the chairperson of the audit committee, the executive officer; or chief financial officer, of a company (if the company provides goods or services to an organ of state and the annual transactional value of the goods or services or both exceeds an amount determined by the Minister by notice in the Gazette).

⁴⁰⁴ Daniele Canestri op cit note 43 at 360.

⁴⁰⁵ Ibid at 98.

Amendment,⁴⁰⁶ there was no PEP regulation in South Africa.⁴⁰⁷ This was one of the deficiencies highlighted by MER, 2021,⁴⁰⁸ which resulted in South Africa getting placed on the FATF grey list.

To guarantee that the PEP regulation is properly implemented and compliant with FATF standards, requirements pertaining to it were included in FICA following the 2022 amendment.⁴⁰⁹ PEP regulation requirements are now included in FICA to guarantee their proper enforcement and compliance with the FATF standards. For South Africa's efforts to combat ML/TF effectively, this was a major turning point and was a pivotal development in response to the deficiencies exposed during the state capture era and by MER, in 2021.⁴¹⁰

6.2.2. UNITED KINGDOM

PEPs are considered high risk by the FATF, which requires financial institutions to conduct EDD on PEPs.⁴¹¹ Thus, the broader the scope, the more secure our global financial system will be. Surprisingly, certain countries like the UK continue to employ a strategy that distinguishes between domestic and foreign PEPs, a practice that this dissertation challenges. This dissertation favours the stance that treats domestic and foreign alike in relation to the risk they pose. On this account, MER, 2018, revealed that the current definition of a PEP in the UK is inadequate to combat ML/TF, implying that a more comprehensive definition of a PEP is necessary.

Furthermore, the UK adopts the approach, in recognising legal entities associated with PEPs and their family members as PEPs, which is thought to be the best-established definition.⁴¹² The EU approach remains limited in that it excludes a legal entity that does business with an organ of state.

⁴⁰⁶ The 2022 Amendment Act.

⁴⁰⁷ FATF/ ESAAMLG Mutual evaluation report: Anti-money laundering and counter-terrorist financing measures – South Africa (2009) available at <https://www.fatf-gafi.org/content/dam/fatf-gafi/mer/MER%20South%20Africa%20full.pdf.coredownload.pdf> accessed on 15.11.2023. page 103.

⁴⁰⁸ FATF Mutual evaluation report: Anti-money laundering and counter-terrorist financing measures – South Africa (2021) available at *Mutual-Evaluation-Report-South-Africa.pdf* accessed on 04.05.2023.

⁴⁰⁹ Section 42 of FICA; Schedule 3A and 3B of FICA; Section 39 of the 2022 Amendment.

⁴¹⁰ Cayle Lupton op cit 219 at 43.

⁴¹¹ Recommendation 12 of the FATF Recommendations, 2012.

⁴¹² Christelle Ahlers op cit note 30 at 78.

6.3. RECOMMENDATIONS

The designation of PEPs allows financial institutions and regulatory bodies to subject them to EDD measures.⁴¹³ PEPs as a concept emerged as a response to the inherent weaknesses within the international banking industry, which created opportunities for corrupt leaders from developing countries to engage in illicit activities.⁴¹⁴ The initial objective of the process for identifying and managing PEPs was to detect instances of corruption within the political sphere.⁴¹⁵ The categorisation of PEPs has never been intended to insinuate any wrongdoing or criminal behaviour on the part of individuals. Instead, its purpose is to serve as a signal for financial institutions to implement EDD measures and risk assessments due to the inherent vulnerabilities associated with individuals in high-profile positions and the potential risk of corruption.⁴¹⁶

As alluded to throughout this dissertation, that a PEP is a natural person.⁴¹⁷ This conventional classification mostly focuses on public officials and members of the government, but since some countries have strong ties between business and politics, a broader PEP scope is necessary for AML/CFT efforts.⁴¹⁸ It is for this reason that firstly, this dissertation favours the stance that treats domestic and foreign alike in relation to the risk they pose. Secondly, the EU's definition of a PEP is thought to be the most comprehensive definition of a PEP,⁴¹⁹ since it encompasses legal entities, particularly regarding beneficial ownership.⁴²⁰ It is proposed that the concept of Politically Exposed Entities (PEEs) be introduced to address the requirement of applying the same level of oversight to legal entities.⁴²¹ The EDD should specifically target the

⁴¹³Recommendation 12 of the FATF Recommendations, 2012.

⁴¹⁴ Jackie Johnson op cit note 7 at 291; Christelle Ahlers op cit note 30 at 95.

⁴¹⁵ The Wolfsberg Group 'Wolfsberg guidance on Politically Exposed Person("PEP")' available at *Wolfsberg Frequently Asked Questions ("FAQ's") on (wolfsberg-principles.com)*, accessed on 05/03/2023.

⁴¹⁶ Joint Money Laundering Steering Group 'Prevention of money laundering/ combating terrorist financing' available at <https://www.jmlsg.org.uk/guidance/current-guidance/> accessed on 22.06.2023.

⁴¹⁷ Daniele Canestri op cit note 43 at 360; Jackie Johnson op cit note 7 at 292.

⁴¹⁸ Kim-Kwang Raymond Choo op cit note 42 at 383; The social influence of business and politics frequently overlaps significantly in countries like South Africa, where corruption is rampant.

⁴¹⁹ Christelle Ahlers op cit note 30 at 78.

⁴²⁰ Article 3(11) of the Fourth AMLD.

⁴²¹ Daniele Canestri op cit note 43 at 360.

legal entities themselves rather than just the beneficial owners of the legal entities, particularly concerning their transactional engagements with the government.

For South Africa to be removed from the grey list in quick succession, it needs to broaden the scope of its PEP to encompass legal entities under its domestic law. It is proposed that South Africa adopt the EU-UK model that encompasses legal entities within the scope of PEPs. This follows the observation that the exclusion of legal entities from the scope of PEPs significantly hinders its capacity to adhere to FATF standards.⁴²² South Africa can update its PEP regulation to incorporate legal entities without waiting for the FATF PEP regulation to be revised as it did with the introduction of PIP.

For the UK to improve its PEP regulation to further strengthen its AML/CTF regime, adopting a stance that treats domestic and foreign alike concerning the risk they pose is necessary.

For the EU to further improve its PEP definition, adopting an approach that includes legal entities that do business with the organs of state is necessary.

⁴²² Ibid at 95.

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