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Assessing the Global Response to Proliferation Financing

An Analysis of FATF Mutual Evaluation Data

Emil Dall and Tom Keatinge



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Contents

Acknowledgements	v
Executive Summary	vii
Introduction	1
I. The FATF and Proliferation Financing	3
II. Examining the FATF Mutual Evaluation Data	7
III. New Proliferation Financing Requirements in the FATF Standards	23
Conclusion	25
About the Authors	27
Annex	29

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Executive Summary

IN 2012, THE Financial Action Task Force (FATF) brought proliferation financing (PF) into the scope of threats it considers, requiring countries to implement targeted financial sanctions made under UN Security Council Resolutions related to PF.¹ Since then, through a process of peer-led ‘mutual evaluations’, 118 jurisdictions have been assessed on their available legal and regulatory measures to implement targeted financial sanctions related to proliferation (Recommendation 7), as well as how effectively jurisdictions implement targeted financial sanctions for PF in practice (Immediate Outcome 11).²

A review of these mutual evaluations reveals stark differences in how jurisdictions are assessed to have adopted these PF standards into their domestic legal and regulatory frameworks. The key findings in this study include:

- **After almost a decade of PF being included in the FATF’s standards, the compliance among assessed jurisdictions remains varied.** While 50% of jurisdictions are deemed either compliant or largely compliant with Recommendation 7,³ 20% are still not compliant with the technical requirement within Recommendation 7 to implement targeted financial sanctions related to proliferation ‘without delay’.
- **Only two jurisdictions have received high effectiveness ratings for Immediate Outcome 11.**⁴ Fifty percent of assessed jurisdictions had low effectiveness when it comes to countering PF domestically. This may not capture some subsequent improvements made by jurisdictions as, unlike Recommendations, Immediate Outcomes are not re-rated following initial evaluations.

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1. Financial Action Task Force (FATF), ‘FATF Guidance on Counter Proliferation Financing: The Implementation of Financial Provisions of United Nations Security Council Resolutions to Counter the Proliferation of Weapons of Mass Destruction’, February 2018, p. 3.
 2. The analysis for this paper captures all FATF mutual evaluations published as of 7 October 2021 and is based on the data provided by the FATF in the ‘Consolidated Table of Assessment Ratings’, <<https://www.fatf-gafi.org/publications/mutualevaluations/documents/assessment-ratings.html>>, accessed 10 October 2021.
 3. The FATF rates compliance with its Recommendations on a scale of: compliant; largely compliant (there are only minor shortcomings); partially compliant (there are moderate shortcomings); and non-compliant (there are major shortcomings).
 4. The FATF rates effectiveness on a scale of: high effectiveness (the Immediate Outcome is achieved to a very large extent, minor improvements needed); substantial effectiveness (the Immediate Outcome is achieved to a large extent, moderate improvements needed); moderate effectiveness (the Immediate Outcome is achieved to some extent, major improvements needed); and low effectiveness (the Immediate Outcome is not achieved or achieved to a negligible extent, fundamental improvements needed).

- **Later assessments of jurisdictions are no better than earlier ones.** Given the extent to which mutual evaluations are scrutinised when they are published, it would be expected that those countries that are yet to be evaluated would seek to learn lessons from previous cases and implement changes that improve their prospects when their turn to be evaluated comes. This appears not to be the case and, indeed, in some cases, the results in later assessment years are worse than the results received by jurisdictions in earlier assessment years, raising questions as to how learning and best practice are shared.
- **Although most jurisdictions did receive the same initial ratings for PF and terrorism financing (TF), a meaningful proportion (34%) of jurisdictions performed better on their TF requirements than they did for PF.** This suggests that this latter category of jurisdictions was either more aware of their obligations on TF and devoted more attention and resources to the implementation of TF controls, or that PF was not considered as a threat. Of the jurisdictions that performed worse on PF, a significant majority received a non-compliant rating on Recommendation 7 and a low level of effectiveness on Immediate Outcome 11, respectively.
- **There are key differences between FATF regions and their performance record on PF.** Some regions performed significantly worse than others in their initial ratings on Recommendation 7 but have also improved the most since, as evidenced by re-ratings through follow-up assessments.

The authors first engaged with the FATF's PF standards in 2015 to explore how countries were implementing these new requirements. Based on extensive interviews with government and private sector implementers around the world, their first paper revealed that 'governmental interest in proliferation finance and related outreach to [financial institutions was] highly uneven between national jurisdictions'. The mixed (or absence of) messages governments delivered to their private sectors resulted in a poor understanding of the nature of proliferation and thus poor internal policies for mitigating relevant risks.⁵

As the FATF has introduced new, expanded standards related to counterproliferation financing – the requirement to conduct a PF-focused risk assessment – and is preparing to begin another round of evaluations where countries will be assessed against this new, expanded requirement, lessons from the implementation of current standards should be kept in mind to ensure compliance. The FATF should:

1. Ensure that its FATF-style regional bodies are empowered and equipped to provide the necessary guidance and support to their member countries to avoid regional differences in implementation that proliferators can exploit.
2. Ensure that the new requirement to conduct a risk assessment for PF is prioritised by countries to the same extent as those applied to money laundering and TF. This will help avoid the implementation gaps that have been observed between PF standards and other financial crime risks.

5. Emil Dall, Andrea Berger and Tom Keatinge, 'Out of Sight, Out of Mind? A Review of Efforts to Counter Proliferation Finance', *Whitehall Report*, 3-16 (June 2016), p. 1.

3. Ensure that the lessons and best practices from those that are first subject to the new risk assessment requirement are used to inform the process of jurisdictions whose assessments are later in the assessment calendar. Facilitating the transfer of best practice should be prioritised by the FATF.

Introduction

THE FINANCIAL ACTION Task Force (FATF) recommendations on money laundering (ML), terrorist financing (TF) and proliferation financing (PF) ‘set an international standard, which jurisdictions should implement in their own domestic legal and regulatory frameworks’.¹ In 2012, the FATF updated its standards to include a new Recommendation 7, which focuses on the implementation of targeted financial sanctions against proliferating actors designated by UN Security Council Resolutions (UNSCRs). PF was also included in Recommendation 2, addressing national cooperation and coordination on financial crime risks (including ML and TF).²

Since 2015, RUSI’s Centre for Financial Crime and Security Studies (CFCS) has been tracking the application of these PF-specific FATF recommendations, and the effectiveness with which countries are implementing these requirements. Its work has benefited from the opportunity to: conduct interviews with government and private sector actors on six continents; attend both private sector conferences and government/multilateral events; and work closely with countries to develop laws, methodologies, risk assessments and other remedial actions as they seek to respond to the feedback provided by the FATF’s mutual evaluation process.

Throughout these years, CFCS has drawn heavily on these country mutual evaluations to provide perspective on where the evaluators perceive weaknesses in countries’ responses to PF. As over half of the FATF’s global membership (including both FATF members themselves and those countries that are members of the FATF’s regional bodies) have now been reviewed, a quantitative analysis of these results is timely, particularly as the FATF recently introduced new, expanded standards on proliferation financing – the requirement to conduct PF risk assessments – which countries will soon be expected to implement and be assessed against.

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1. Financial Action Task Force (FATF), ‘The FATF Recommendations: International Standards on Combating Money Laundering and the Financing of Terrorism & Proliferation’, February 2012, updated June 2021, p. 7.
 2. The FATF’s other recommendations which cover preventive measures – such as customer due diligence and suspicious transaction reporting requirements, supervision, beneficial ownership rules and international cooperation – consider money laundering (ML) and terrorism financing (TF) specifically, and do not cover proliferation financing (PF).

This paper therefore draws on mutual evaluation³ data provided by the FATF in the form of a ‘Consolidated Table of Assessment Ratings’,⁴ focused on the Recommendations and Immediate Outcomes that are relevant to PF. Using this data – recorded at the time of a country’s mutual evaluation, and updated via the follow-up process the FATF employs – this paper draws conclusions as to how the FATF’s mission to include counterproliferation finance (CPF) in its standards, alongside the existing financial crimes of ML and TF, has progressed.

Chapter I reviews the elements of the FATF standards that relate to PF. Chapter II analyses the evaluation data related to PF. Chapter III considers the implications of this analysis in light of the new PF-related requirements being introduced by the FATF. The paper concludes with recommendations on how these new requirements can be most effectively implemented by the FATF, its regional bodies and member states.

The FATF mutual evaluation process has faced considerable disruption during the coronavirus pandemic. The FATF’s process includes onsite visits to countries as part of the mutual evaluation and follow-up process. As a result, there has been a hiatus in the concluding of mutual evaluations and the conducting of follow-up assessments. While this has delayed the completion of mutual evaluations, it has not changed the underlying compliance and effectiveness of countries, meaning it is not judged by the authors to impact the analysis in this paper. Future research may identify a slowdown in the rate of mutual evaluation and follow-up engagements; however, the FATF mutual evaluation and follow-up process has managed to adapt to the coronavirus pandemic quite effectively. Thus, notwithstanding the delay to the overall progress of the global mutual evaluation schedule, the findings remain valid.⁵

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3. FATF mutual evaluations are ‘in-depth country reports analysing the implementation and effectiveness of measures to combat money laundering and terrorist financing. Mutual evaluations are peer reviews, where members from different countries assess another country. A mutual evaluation report provides an in-depth description and analysis of a country’s system for preventing criminal abuse of the financial system as well as focused recommendations to the country to further strengthen its system’. See FATF, ‘Mutual Evaluations’, <[https://www.fatf-gafi.org/publications/mutualevaluations/more/more-about-mutual-evaluations.html?hf=10&b=0&s=desc\(fatf_releasedate\)](https://www.fatf-gafi.org/publications/mutualevaluations/more/more-about-mutual-evaluations.html?hf=10&b=0&s=desc(fatf_releasedate))>, accessed 10 October 2021.
 4. FATF, ‘Consolidated Assessment Ratings’, <<https://www.fatf-gafi.org/publications/mutualevaluations/documents/assessment-ratings.html>>, accessed 10 October 2021.
 5. The authors have continued to deliver counterproliferation finance (CPF)-focused technical assistance to various countries remotely and have identified no diminished appetite to approve CPF standards in either the public or private sectors.

I. The FATF and Proliferation Financing

CONCERNS ABOUT PF have been troubling governments since the early 2000s, when information about the existence of large illicit WMD and missile procurement networks began to emerge. A central figure in these networks was A Q Khan, a key figure in Pakistan's nuclear weapons programme who from the mid-1980s to 2004 traded sensitive goods and technology with international buyers such as Libya, Iran and North Korea.⁶ The financing of these transactions used many of the obfuscation tools, such as front and shell companies, familiar in the ML world. The formal financial sector was being exploited to finance the trade in the goods and technologies needed to develop WMD programmes.

In 2004, the UN Security Council adopted Resolution 1540 which sought to address concerns about the proliferation activities of non-state actors.⁷ UNSCR 1540 called on governments to control and prevent the financing of proliferation, specifically requiring states to:

Adopt and enforce appropriate effective laws which prohibit any non-State actor to manufacture, acquire, possess, develop, transport, transfer or use nuclear, chemical or biological weapons and their means of delivery, in particular for terrorist purposes, as well as attempts to engage in any of the foregoing activities, participate in them as an accomplice, assist or finance them.

Establish, develop, review and maintain appropriate effective national export and trans-shipment controls over such items, including appropriate laws and regulations to control export, transit, trans-shipment and re-export and controls on providing funds and services related to such export and trans-shipment such as financing, and transporting that would contribute to proliferation, as well as establishing end-user controls; and establishing and enforcing appropriate criminal or civil penalties for violations of such export control laws and regulations.⁸

Although the actions that flowed from the 1540 regime focused more on goods than finance, rising concerns related to North Korea's nuclear ambitions – and the accompanying raft of UNSCRs – ensured that preventing the financing of proliferation remained a central international security concern.⁹

6. Michael Laufer, 'A. Q. Khan Nuclear Chronology', Carnegie Endowment for International Peace, 7 September 2005.

7. UN Security Council Resolution 1540, 28 April 2004, S/RES/1540.

8. *Ibid.*, pp. 2–3.

9. For a more detailed explanation of the evolution of the FATF's engagement with PF, see Emil Dall, Andrea Berger and Tom Keatinge, 'Out of Sight, Out of Mind? A Review of Efforts to Counter Proliferation Finance', *Whitehall Report*, 3-16 (June 2016).

When the FATF updated its standards in 2012, CPF – and the implementation of targeted financial sanctions related to PF – was added to the list of issues it would scrutinise during its assessments in the form of a specific technical recommendation (Recommendation 7) and an effectiveness assessment (Immediate Outcome 11), as detailed below.

Box 1: FATF Recommendation 7

Recommendation 7 directs countries to:

‘[Implement] targeted financial sanctions to comply with United Nations Security Council resolutions relating to the prevention, suppression and disruption of proliferation of weapons of mass destruction and its financing. These resolutions require countries to freeze without delay the funds or other assets of, and to ensure that no funds and other assets are made available, directly or indirectly, to or for the benefit of, any person or entity designated by, or under the authority of, the United Nations Security Council under Chapter VII of the Charter of the United Nations’.

Source: FATF, ‘International Standards on Combating Money Laundering and the Financing of Terrorism and Proliferation: The FATF Recommendations’, February 2012, updated June 2021, p. 13.

The FATF, and FATF-style regional bodies (FSRBs),¹⁰ supported on occasion by the IMF and the World Bank, carry out evaluations of all member states on their compliance with the standards, with the draft report subsequently reviewed and approved by FATF plenary meetings prior to publication. The FATF measures technical compliance with its recommendations on a four-point scale:

- Compliant.
- Largely compliant.
- Partially compliant.
- Non-compliant.

Since it revised its methodology in 2012, the FATF also measures how effectively these technical requirements are being implemented through a series of Immediate Outcomes. Immediate

10. The FATF is made up of 39 members (37 countries and two regional bodies: the EU and the Gulf Cooperation Council). Over time, in order to represent the interests of those countries that are not part of the FATF itself, FATF-style regional bodies (FSRBs) have been created. Although there is no legal connection between the FSRBs and the FATF, and there is no organisational hierarchy between them, there is necessarily close communication and commonality given their focus on implementing the FATF’s standards to strengthen the integrity of the financial system. Thus, decisions made at the FATF, including the introduction of CPF into its standards, flow down to the FSRBs and their members. See FATF, ‘High-Level Principles and Objectives for FATF and FATF-Style Regional Bodies’, October 2012, updated February 2019.

Outcome 11, as explained further in Box 2, is dedicated to measuring the effectiveness of CPF implementation and is measured on a four-point scale:

- High effectiveness.
- Substantial effectiveness.
- Moderate effectiveness.
- Low effectiveness.

Box 2: Immediate Outcome 11

Immediate Outcome 11 characterises an effective system as one in which:

- ‘Persons and entities designated by the United Nations Security Council Resolutions (UNSCRs) on proliferation of weapons of mass destruction (WMD) are identified, deprived of resources, and prevented from raising, moving, and using funds or other assets for the financing of proliferation.
- Targeted financial sanctions are fully and properly implemented without delay; monitored for compliance and there is adequate co-operation and co-ordination between the relevant authorities to prevent sanctions from being evaded, and to develop and implement policies and activities to combat the financing of proliferation of WMD’.

Source: FATF, ‘Methodology for Assessing Technical Compliance with the FATF Recommendations and the Effectiveness of AML/CFT Systems’, 2013, updated November 2020, pp. 126–27.

Jurisdictions are assessed either as a member of the FATF itself (39 members) or as one of the nine FSRBs, resulting in ‘more than 200 countries and jurisdictions committed to implementing [the FATF standards]’.¹¹

It has been almost 10 years since the FATF first introduced the concept of CPF into its standards, and over half (118 jurisdictions) have now been assessed for their technical compliance with Recommendation 7 and their effectiveness under Immediate Outcome 11.¹²

11. FATF, ‘Who We Are’, <<https://www.fatf-gafi.org/about/>>, accessed 10 October 2021.

12. The data cut-off point for this paper is 7 October 2021, and any mutual evaluation results released after this date are not included.

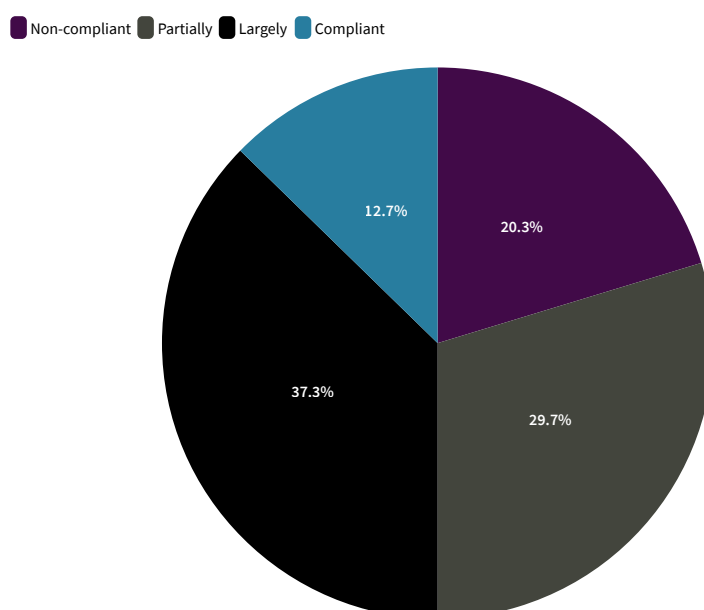
II. Examining the FATF Mutual Evaluation Data

THIS CHAPTER ANALYSES the ratings received in the 118 mutual evaluation reports (and subsequent follow-up reports) conducted so far. It focuses on data related to Recommendation 7 and Immediate Outcome 11, and assesses how effectively members of the FATF and its FSRBs have incorporated PF into their legal, regulatory and procedural frameworks.

Current Implementation Record

Figures 1 and 2 show the breakdown of how the 118 jurisdictions have been rated (reflecting any amendments since the original evaluation was conducted) for Recommendation 7 and Immediate Outcome 11. For Recommendation 7, 50% of assessed jurisdictions have received a compliant or largely compliant rating – the top two ratings for technical compliance. This means that only half of the countries have developed some legal and regulatory measures enabling them to implement UN Security Council mandated targeted financial sanctions related to proliferation in line with the FATF’s recommendation. Currently, 20% of jurisdictions have a non-compliant rating, meaning that they lack any form of technical framework for successfully implementing targeted financial sanctions related to proliferation.

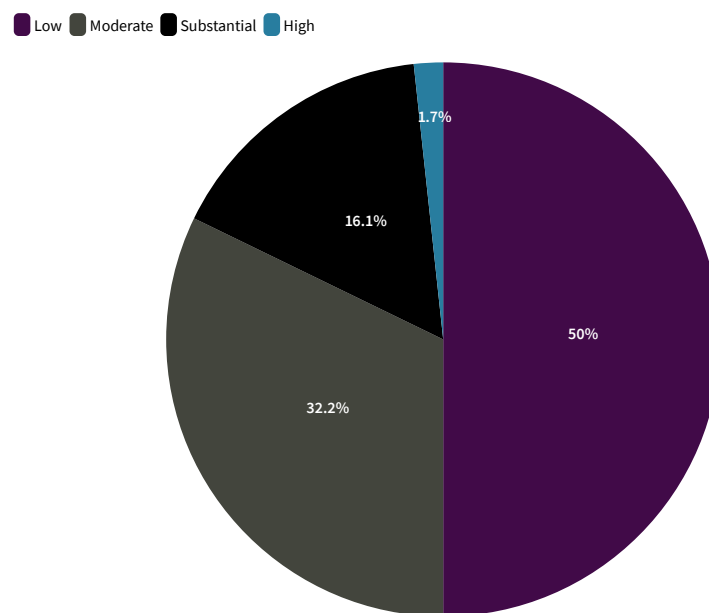
Figure 1: Recommendation 7 Ratings (as of 7 October 2021).



Source: Authors’ analysis of data from FATF, ‘Consolidated Assessment Ratings’, <<https://www.fatf-gafi.org/publications/mutualevaluations/documents/assessment-ratings.html>>, accessed 24 October 2021.

In contrast, for Immediate Outcome 11, 50% of countries have the lowest rating of low effectiveness, with only two out of 118 countries (the UK and the US) being assessed to have a high level of effectiveness on combating PF so far.

Figure 2: Immediate Outcome 11 Ratings (as of 7 October 2021).



Source: Authors' analysis of data from FATF, 'Consolidated Assessment Ratings'.

While Recommendation 7 is focused on the presence in national law of the legal measures required to implement relevant targeted financial sanctions 'without delay' and the development of procedures for the private sector to comply with those legal measures (for example, a *system* to communicate sanctions designations to financial institutions, or the *obligation* that financial institutions conduct sanctions screening and freeze assets of sanctioned entities), those systems and obligations also need to be translated into practice – hence the effectiveness test applied under Immediate Outcome 11. The FATF Methodology provides examples of what an effective response to PF might look like, including: whether financial institutions are aware of their legal obligations; if financial supervisors have issued guidance and monitor the private sector for compliance with the regulations; or if the authorities have adequate resources to address PF.¹³ The analysis of where countries have shortcomings in relation to PF provided by the mutual evaluation process should assist countries in addressing deficiencies.

It is important to note that for the technical compliance requirements, such as Recommendation 7, countries have an opportunity to remedy their deficiencies and be re-rated in frequent follow-up reports conducted by the FATF and its FSRBs. As a result, a total of 31 jurisdictions have successfully improved their initial Recommendation 7 rating. Of these, 24 initially received

13. FATF, 'Methodology for Assessing Technical Compliance with the FATF Recommendations and the Effectiveness of AML/CFT Systems', 2013, updated November 2020, pp. 126–27.

low effectiveness ratings, and it may therefore be the case that those jurisdictions would receive a higher effectiveness rating today if effectiveness were also reassessed alongside technical compliance.

Key Points

- After almost a decade of PF being included in the FATF's standards, the compliance among assessed jurisdictions varies considerably. While 50% of jurisdictions are deemed either compliant or largely compliant with Recommendation 7, 20% are still not compliant with the technical requirement within Recommendation 7 to implement targeted financial sanctions related to proliferation 'without delay'.
- Only two jurisdictions have received high effectiveness ratings for Immediate Outcome 11, with 50% of assessed jurisdictions still recorded as having low effectiveness when it comes to CPF domestically. However, this group might be smaller, as Immediate Outcome 11 is not re-rated like its Recommendation 7 counterpart.

Analysis of the key areas of FATF assessment of PF shows a global system that remains highly vulnerable to abuse. Having introduced the requirement to combat PF in 2012, the international community was slow to take steps that translated that high-level decision into an operational reality.¹⁴ As the mutual evaluation process has revealed, a significant number of countries have no legal mechanisms in place to implement targeted financial sanctions; and where laws have been introduced, little has been done to sensitise private sector actors to their obligations.

These failings are not merely technical. They matter and have an impact on international security as many of the countries that exhibit these failings have proved to be highly vulnerable to financial abuse by proliferators, notably North Korea.¹⁵

Against this backdrop, the upgrade in Recommendation 7 ratings following initial country assessments suggests that countries are addressing their shortcomings, which underlines the extent to which the FATF assessment process can lead to systemic improvements in the integrity of national financial systems.

Learning Lessons from Peers

As the low ratings discussed above suggest, countries require time to fully understand and implement a new standard. The FATF mutual evaluation cycle takes at least 10 years (the current cycle will be longer given the delays caused by the coronavirus pandemic). Those countries that were assessed at the beginning of the current cycle, shortly after the PF requirements were introduced, had less time in which to adapt, compared to the jurisdictions with assessments later in the cycle. The FATF's mutual evaluation reports are made public, meaning one could

14. Berger, Dall and Keatinge, 'Out of Sight, Out of Mind?'

15. Darya Dolzikova and Anagha Joshi, 'The Southern Stratagem: North Korean Proliferation Financing in Southern and Eastern Africa', *RUSI Occasional Papers* (April 2020).

reasonably expect countries who are assessed later in the assessment cycle to perform better, as they are able to learn from the successes of jurisdictions that have already been through the assessment process and avoid any common legal, regulatory or procedural pitfalls.

However, analysing the initial ratings that countries received on Recommendation 7 (and therefore not considering the subsequent upgrade of ratings in follow-up reports) reveals those countries whose assessment fell later in the assessment cycle did not improve on the performance of earlier countries (see Figure 3).

2019 was the first and, so far, the only year in which the most frequently awarded initial rating was largely compliant. In every single assessment year, non-compliant or partially compliant ratings have outnumbered largely compliant and compliant ratings. No jurisdiction has received a compliant rating in its initial mutual evaluation since 2019.

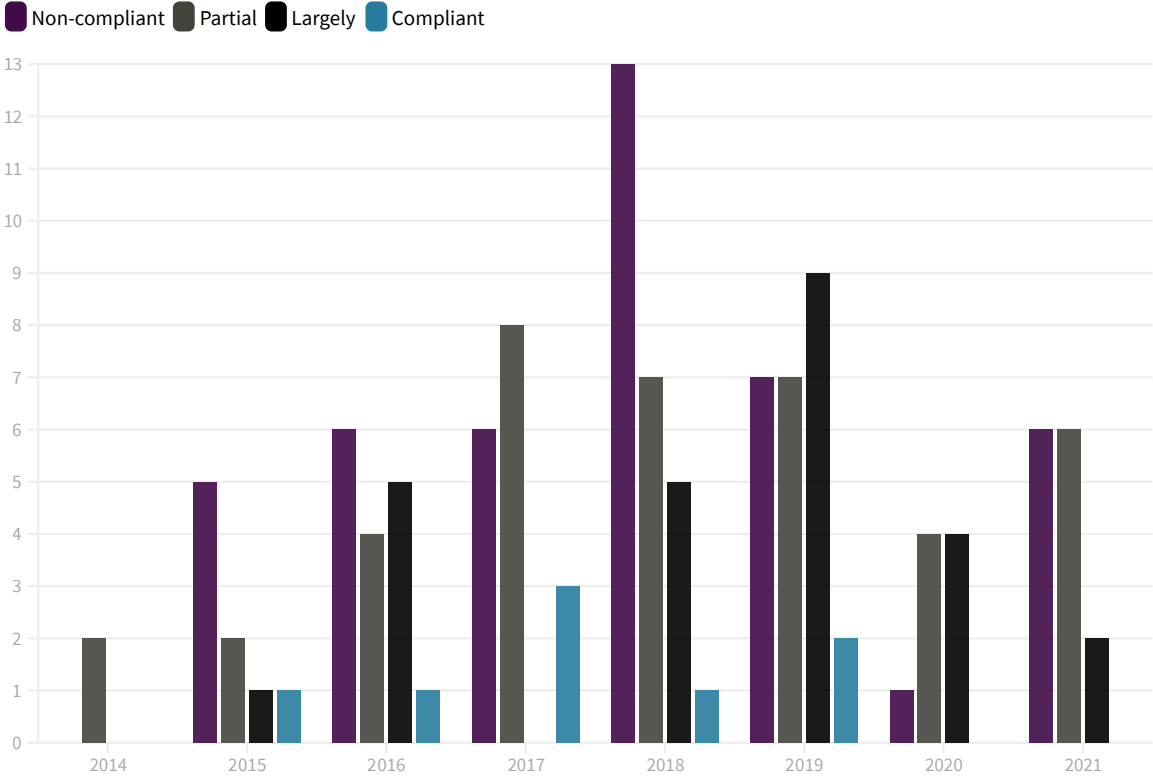
This is striking as the steps required to achieve compliant or largely compliant ratings on Recommendation 7 do not add new requirements on countries. It merely reiterates the need for countries to meet their existing international security obligations by complying with UNSCRs relating to the prevention, suppression and disruption of proliferation of WMD and its financing.¹⁶

This suggests that awareness of Recommendation 7, and perhaps also the UNSCR sanctions it relies on, remains low among officials in many countries. A consistent finding from the authors' ongoing CPF research is that while those in ministries of finance or foreign affairs who are close to the sanctions and FATF process understand their obligations, it is not until *after* a country has been assessed and had its failings publicly exposed that remedial action is taken, unless senior officials and the political leadership also understand the importance of the mutual evaluation process. Observing the successes or shortcomings of other countries appears to have little impact.¹⁷

16. FATF, 'The FATF Recommendations', p. 13.

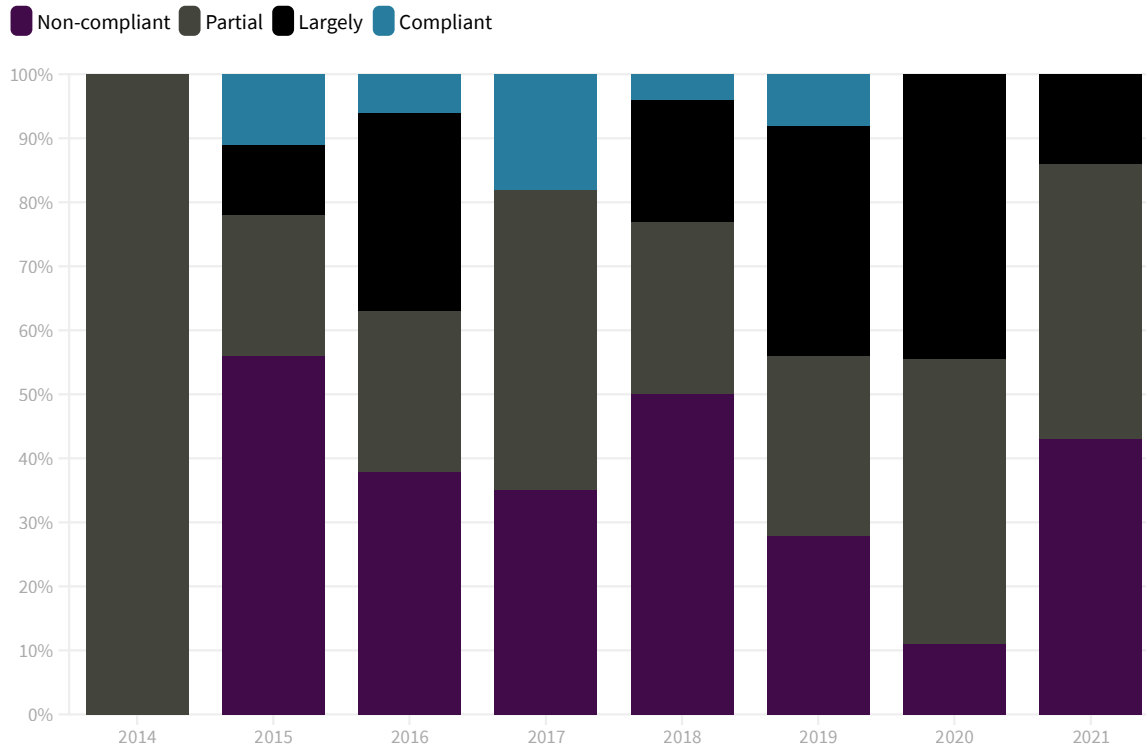
17. It may also be the case that as the assessment teams have themselves become more familiar with PF, they have become rigorous in their assessments, making high ratings more difficult to attain.

Figure 3: Summary of Initial Mutual Evaluation Recommendation 7 Ratings, 2014–21



Source: Authors’ analysis of data from FATF, ‘Consolidated Assessment Ratings’.

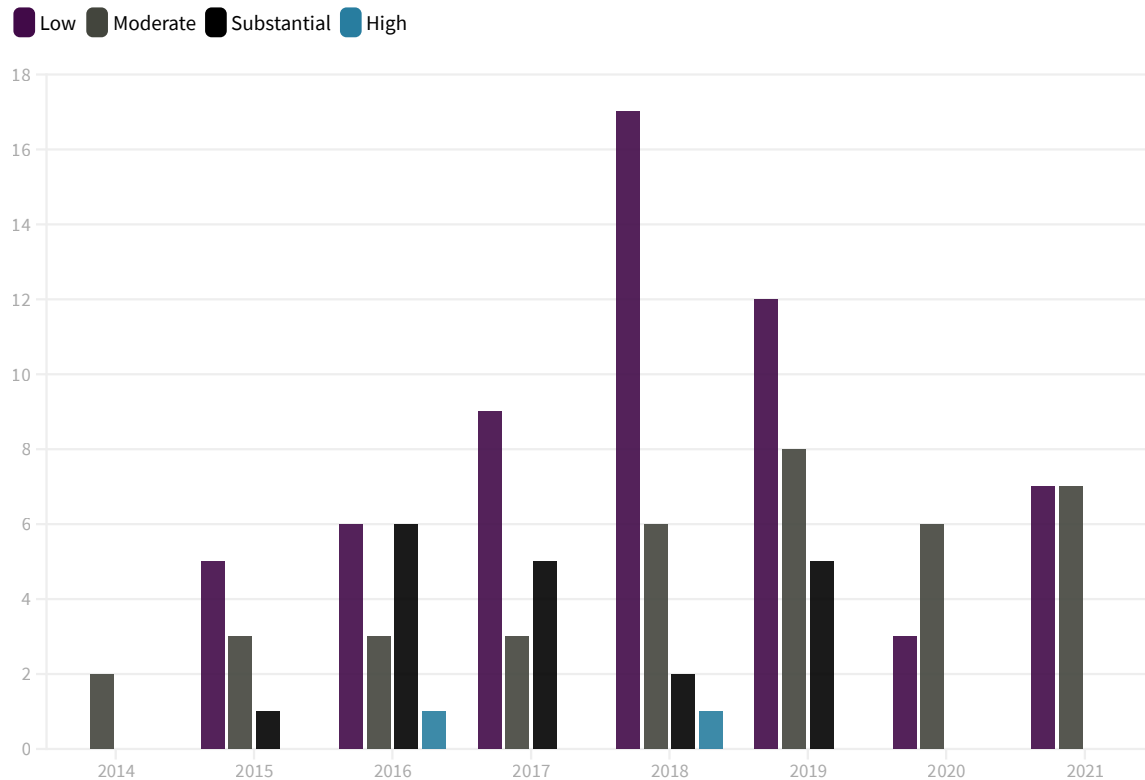
The number of mutual evaluation reports published each year varies, so it is appropriate to consider this analysis on a proportionate basis. As Figure 4 shows, although 2019 and 2020 indicated some improvement in the percentage of compliant and largely compliant ratings for the initial rating of Recommendation 7, there is no significant improvement in initial ratings over time, and indeed 2021 is arguably the weakest ever year.

Figure 4: Proportionate Analysis of Initial Mutual Evaluation Recommendation 7 Ratings, 2014–21

Source: Authors' analysis of data from FATF, 'Consolidated Assessment Ratings'.

The Immediate Outcome 11 ratings received by countries show a similar trend (see Figure 5). This is perhaps less surprising given that demonstrating effectiveness requires a country to develop a track record of activity spanning several years and the coordination, involvement and awareness of a wide array of government agencies,¹⁸ something that cannot be developed as an immediate response to earlier mutual evaluations.

18. Some also argue that the disconnect between export controls and CPF hinders responses. See, for example, Rachel A Weise, Gretchen Hund and Geoffrey Carr, 'Export Controls and Counterproliferation Finance: Two Sides of the Same Underlying Illegal WMD Activity', *Nonproliferation Review* (Vol. 25, No. 1–2, 2018), pp. 129–45.

Figure 5: Summary of Initial Mutual Evaluation Immediate Outcome Ratings, 2014–21

Source: Authors' analysis of data from FATF, 'Consolidated Assessment Ratings'.

Key Points

- The initial assessment record of jurisdictions on PF has not improved over time. In some cases, the results in later assessment years are worse than the results received by jurisdictions in earlier assessment years. While one would expect jurisdictions to be able to learn from the mistakes of others with earlier assessments, this has not been the case so far. This is a missed learning opportunity for those jurisdictions evaluated later.
- However, bringing forward the necessary legislation to meet the FATF's (and the UN's) requirement to implement targeted financial sanctions without delay requires political commitment and intra-state coordination. There is often a lack of political will until a country's shortcomings are publicly revealed by the FATF's mutual evaluation.

Proliferation Financing Performance Compared to Terrorist Financing Ratings

While the analysis thus far has considered PF ratings in isolation, it is important to also consider them on a relative basis. The poor initial assessment record on Recommendation 7 and Immediate Outcome 11 could be consistent with those jurisdictions also receiving low ratings on all other FATF standards. To test whether this is the case, the ratings received on PF can be compared with those on TF.

Recommendation 6 requires countries to ‘implement targeted financial sanctions regimes to comply with United Nations Security Council resolutions’, including freezing ‘without delay’ the funds or other assets related to a designated person or entity.¹⁹ Immediate Outcome 10 focuses on ensuring that ‘terrorists, terrorist organisations and terrorist financiers are prevented from raising, moving and using funds, and from abusing the NPO sector’, including proper implementation of targeted financial sanctions.²⁰ In other words, the legal, regulatory and procedural requirements that countries adopt for TF purposes look similar to those needed for PF purposes (with some PF-specific amendments required). Given these similarities, a comparison with the PF assessment outcomes may be instructive, keeping in mind that the focus on TF has been a FATF requirement since 2001 and the requirements of Immediate Outcome 10 are broader and more comprehensive than Immediate Outcome 11.²¹

Comparing the 118 initial ratings for Recommendation 7 and Recommendation 6, 60% of assessed jurisdictions received the same rating for both (meaning that if a jurisdiction received a non-compliant rating on Recommendation 7, it received the same on Recommendation 6) (Figure 6). Six percent of Recommendation 7 ratings were higher than the rating that the same jurisdiction received for Recommendation 6, but in 34% of assessments the PF rating was lower, meaning that a jurisdiction received at least one rating lower on Recommendation 7 than it received for Recommendation 6.

Among the group of jurisdictions that received a lower rating for Recommendation 7 than for Recommendation 6, 75% were non-compliant on Recommendation 7.

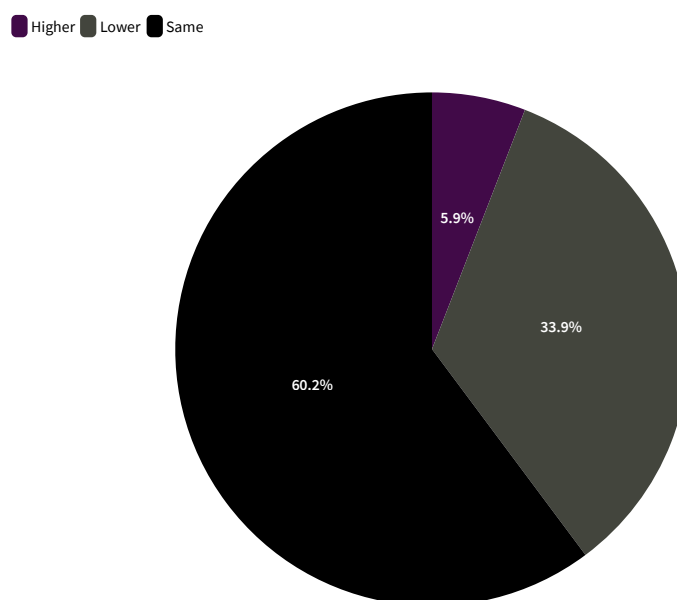
Of the 40 countries that received a lower rating on Recommendation 7 compared to Recommendation 6, only 18 (45% of the 40 countries) have since successfully upgraded their rating by at least one category. It is worth noting that many of the countries that have not yet successfully upgraded were assessed between 2018 and 2021, and may not yet have had adequate time to address the identified legal and policy gaps and be subsequently reassessed.

19. FATF, ‘The FATF Recommendations’, p. 13.

20. *Ibid.* FATF, ‘Methodology for Assessing Technical Compliance with the FATF Recommendations and the Effectiveness of AML/CFT Systems’, 2013, updated November 2020, p. 123.

21. FATF, ‘What We Do’.

Figure 6: Comparison of Initial Mutual Evaluation Ratings for Recommendation 7 in Relation to the Rating Received by the Same Country on Recommendation 6



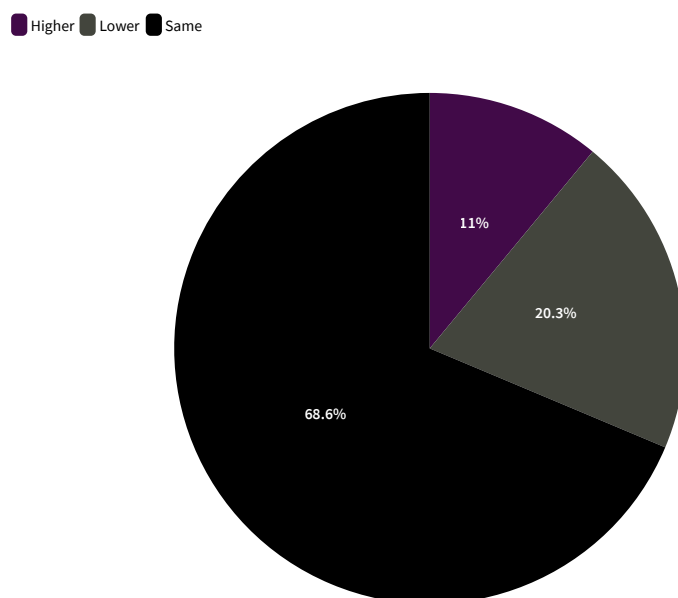
Source: Authors' analysis of data from FATF, 'Consolidated Assessment Ratings'.

For Immediate Outcome 11 and Immediate Outcome 10, the assessment comparison is slightly better,²² with only 20% of jurisdictions receiving a lower initial effectiveness rating for PF compared to TF, and 11% of countries receiving a higher initial rating for PF compared to TF (Figure 7). This may be because effectiveness tests on PF and TF were first introduced at the same time, countries have not had the same head start on TF effectiveness that they have had on technical compliance with the relevant FATF recommendation. It may also be that, as the scope of Immediate Outcome 10 on TF is broader and more comprehensive than Immediate Outcome 11 on PF, demonstrating effectiveness is more challenging than for the objectively less onerous requirements of Immediate Outcome 11.

Among those countries that received a lower effectiveness rating for PF compared to TF, 71% received a rating of low effectiveness.

22. Although Immediate Outcomes 10 and 11 are not identical as relates to TF and PF, their intent is similar and thus a comparative analysis seems appropriate.

Figure 7: Comparison of Initial Mutual Evaluation Ratings for Immediate Outcome 11 in Relation to the Rating Received by the Same Country on Immediate Outcome 10



Source: Authors' analysis of data from FATF, 'Consolidated Assessment Ratings'.

Key Points

- Although a majority of jurisdictions received the same initial ratings for PF and TF, a meaningful proportion of jurisdictions performed better on their TF requirements than they did for PF.
- Two factors may explain this difference. First, in general, countries have a greater awareness of terrorism than proliferation. Thus, addressing TF will attract heightened attention from policymakers, law enforcement and the private sector. Connected with this, the FATF has required a focus on TF since 9/11, more than a decade before it introduced obligations related to PF. A significant architecture related to TF has been built in countries over that time, whereas steps – such as the introduction of the necessary laws and regulatory frameworks – to prioritise PF were not being taken, despite the requirement of the UN for this to occur.
- Second, an effective CPF regime requires a wide range of government agencies to be engaged. Whereas combating TF generally involves the financial crime and security communities (within governments and the private sector), the authors' engagement with countries from across the globe highlights that PF involves a broader cross section of actors. In many countries, ministries of trade, export agencies, customs agencies, and nuclear and dual-use goods-related agencies have a role in CPF efforts. These agencies may not have previously been exposed to the FATF and its assessments and this lack of familiarity may affect a country's assessment outcomes.

Regional Performance

There are also significant regional differences in performance on PF obligations. While some countries are members of both the FATF and an FSRB, for the purposes of this paper they have been counted only as FATF members, and not as part of their respective regional body. This distinction has been made to differentiate between those countries that are close to decision-making (members of the main FATF body) and those countries that are removed from that process and thus less directly exposed to discussions related to developments in the FATF's standards and methodology.

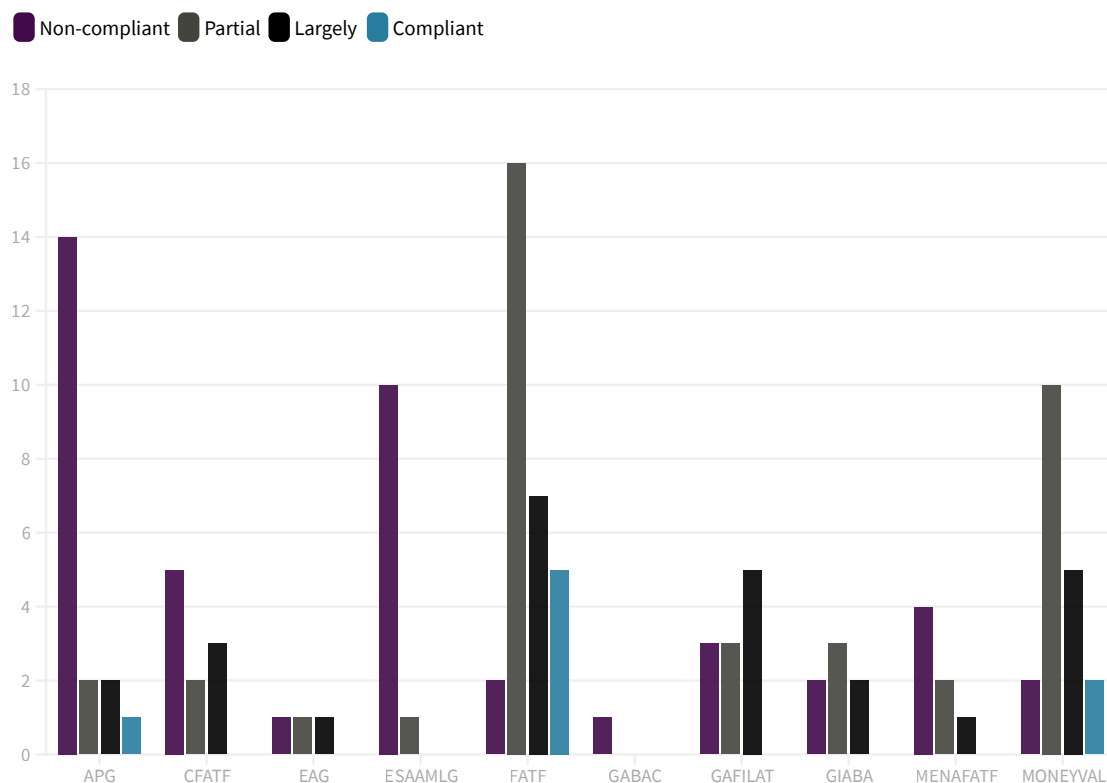
In assessing the performance of countries across the FATF's FSRB membership, it is important to bear in mind their differences in profile. For example, the Task Force on Money Laundering in Central Africa (GABAC) has only been recognised as an FSRB since 2009 and includes just seven country members²³ (three of which are classified by the OECD's Official Development Assistance listing as 'least developed countries'),²⁴ whereas the Asia/Pacific Group on Money Laundering (APG), which has been active on FATF-related awareness raising since the early 1990s, has 41 members spanning the Pacific Islands, South and North East Asia, and South East Asia, and includes several advanced economies.²⁵

Looking at the initial ratings for Recommendation 7, only three FATF regions included countries that received a compliant rating. Some FSRBs, such as the APG and the Eastern and Southern African Anti-Money Laundering Group (ESAAMLG), have a significant majority of countries receiving non-compliant on their initial Recommendation 7 rating.

23. FATF, 'GABAC', <<https://www.fatf-gafi.org/pages/gabac.html>>, accessed 10 October 2021.

24. OECD, 'DAC List of ODA Recipients', <<https://www.oecd.org/dac/financing-sustainable-development/development-finance-standards/DAC-List-ODA-Recipients-for-reporting-2021-flows.pdf>>, accessed 10 October 2021.

25. FATF, 'Asia/Pacific Group on Money Laundering (APG)', <<https://www.fatf-gafi.org/pages/asiapacificgrouponmoneylaundryingapg.html>>, accessed 10 October 2021.

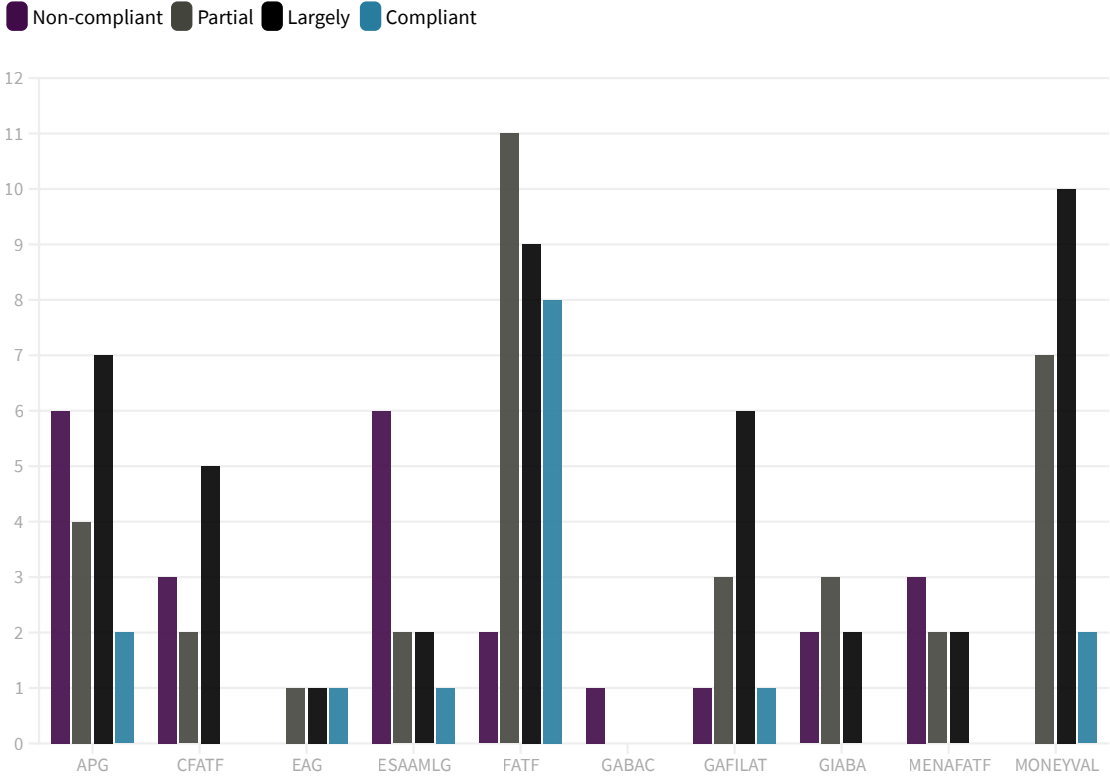
Figure 8: Summary of Initial Recommendation 7 Ratings by FATF-Style Regional Bodies

Source: Authors' analysis of data from FATF, 'Consolidated Assessment Ratings'.

Since the initial assessments were undertaken, however, the regional picture has improved with a number of countries achieving upgrades during their follow-up reports. Regional differences have reduced as a result. Specifically, the number of FSRBs that have countries with a compliant rating for Recommendation 7 has doubled to six. In the ESAAMLG membership, the number of non-compliant ratings has reduced from 10 to six. Among the APG membership, the picture is similar, with the number of non-compliant ratings reducing from 14 to six.

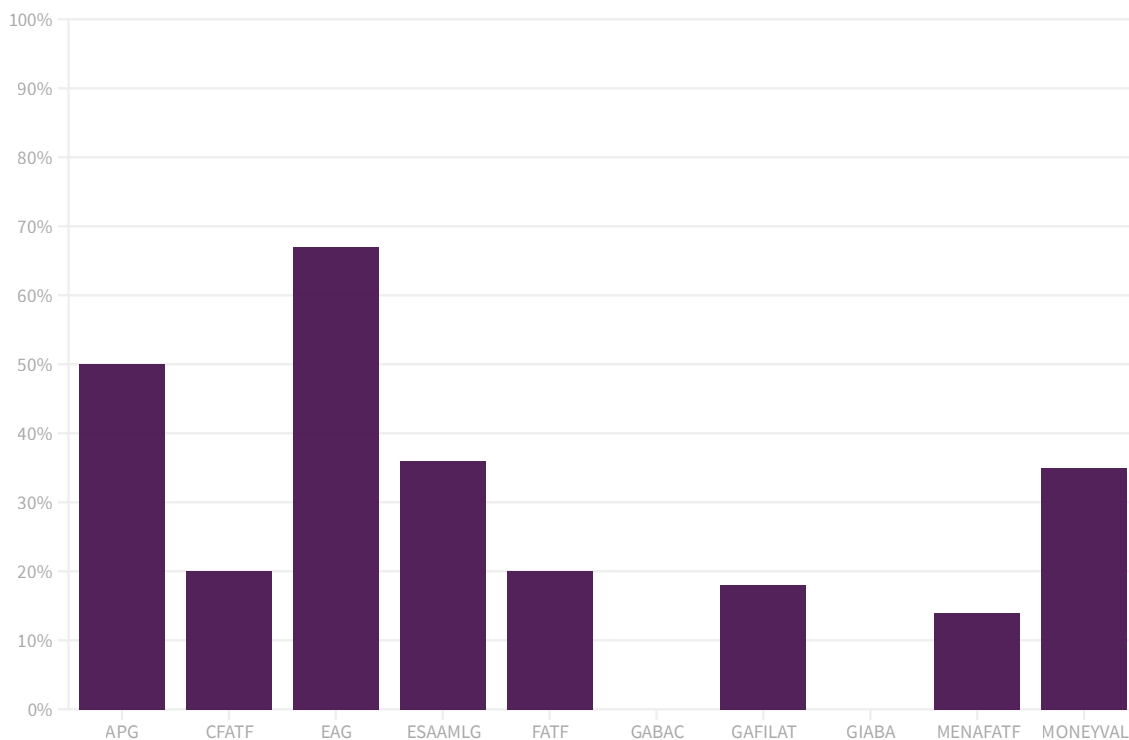
These developments are consistent with the authors' experience that countries have generally not engaged with the CPF requirements of the FATF until they have been evaluated and shortcomings have been highlighted. Thus, it is to be expected that improvements will emerge and gaps in rankings will close as time passes and FSRBs encourage their members to respond to the CPF weaknesses brought to light by their mutual evaluations. This observation is also consistent with the authors' experience engaging with FSRBs across the globe, where the appetite for awareness raising and technical assistance related to CPF is much higher in the aftermath of an evaluation than in advance.

Figure 9: Summary of Current Recommendation 7 Ratings by FATF-Style Regional Bodies



Source: Authors' analysis of data from FATF, 'Consolidated Assessment Ratings'.

In addition to this general improvement, some regions have performed better when it comes to rates of upgrade. Of all the initial Recommendation 7 ratings that could be upgraded (therefore excluding compliant ratings which cannot be upgraded as they are already at the highest level), 36% of 'upgradeable' Recommendation 7 ratings in the ESAAMLG, and 50% of 'upgradeable' Recommendation 7 ratings in the APG, went up at least one category. The Eurasian Group (EAG) saw 66% of its 'upgradeable' ratings improve, although only a small number of evaluations have taken place in this region so far.

Figure 10: Upgraded Recommendation 7 Ratings by Region (Excluding Already Compliant Ratings)

Source: Authors' analysis of data from FATF, 'Consolidated Assessment Ratings'.

These findings are perhaps explained by the extent to which FSRBs have supported their members in responding to the CPF assessments in their mutual evaluations (including via FATF's International Co-Operation Review Group review process).²⁶ From the experience of the authors, the focus on CPF remediation in both the APG and ESAAMLG regions, by the FSRBs themselves along with other technical assistance providers, has been significant, ranging from awareness raising among key private sector industries such as banks and insurance companies, to the drafting of the legal provisions needed to enact the requirements of UN-mandated targeted financial sanctions.

The regions that had the worst initial ratings on Recommendation 7 are also where the most 'upgradeable' ratings have been upgraded since, suggesting that resources and attention to PF have increased in these locations as a result. In contrast, other regions that performed relatively better on their initial ratings have applied less focus and have thus not upgraded as many ratings.

26. For further explanation of the FATF review process, see FATF, 'High-Risk and Other Monitored Jurisdictions', <[https://www.fatf-gafi.org/publications/high-risk-and-other-monitored-jurisdictions/more/more-on-high-risk-and-non-cooperative-jurisdictions.html?hf=10&b=0&s=desc\(fatf_releasedate\)](https://www.fatf-gafi.org/publications/high-risk-and-other-monitored-jurisdictions/more/more-on-high-risk-and-non-cooperative-jurisdictions.html?hf=10&b=0&s=desc(fatf_releasedate))>, accessed 10 October 2021.

This reduced focus may also be a function of the perceived vulnerability of particular countries to PF risk. For example, North Korea has a track record of fundraising in Eastern and Southern Africa through diplomatic and trade relationships,²⁷ and thus remediation among ESAAMLG members is clearly urgent. Likewise, the geographical proximity of many APG members to North Korea requires those countries to have heightened vigilance and effective responses to PF risks.²⁸

Key Points

- There are key differences between the profile and performance records of FSRBs on PF. Some regions performed significantly worse than others in their initial ratings but have also been the regions to improve the most since.
- These initial differences, and subsequent rates of improvement, are most likely explained by the leadership of the relevant FSRB, where awareness of PF risks rose rapidly as their members were evaluated.
- In those regions where PF risk is high, either due to geographic proximity to proliferators such as North Korea, or diplomatic and trade relations that have allowed proliferators to establish fundraising relationships, the urgency with which gaps have been addressed by the FSRBs and other technical assistance providers has resulted in a faster rate of improvement than in other regions where the risk may be perceived as lower, both on an absolute basis as well as relative to other risks such as terrorist financing.

27. Dolzikova and Joshi, 'The Southern Stratagem'.

28. Eda Erol and Leonard S Spector, 'Countering North Korean Procurement Networks Through Financial Measures: The Role of Southeast Asia', James Martin Center for Nonproliferation Studies, Middlebury Institute of International Studies at Monterey, December 2017.

III. New Proliferation Financing Requirements in the FATF Standards

MEASURES FOR CPF were only adopted by the FATF in 2012, and many countries have been slow to embrace these requirements, even if they are only narrowly focused on the implementation of targeted financial sanctions (an existing UN requirement). Reflecting this, in 2018, the incoming US FATF president acknowledged that the FATF's measures on PF 'lag significantly behind those directed at countering money laundering and terrorist financing'.²⁹ One of those significant gaps related to the requirement to conduct a risk assessment for PF. The FATF's Recommendation 1 required jurisdictions to assess risks and apply a risk-based approach to countering financial crime, a requirement which had thus far not encompassed PF.³⁰ Some jurisdictions, including the US and the UK, nevertheless set out to conduct a PF risk assessment despite the lack of a specific requirement from the FATF to do so at the time.³¹

At the end of the US FATF presidency term in June 2019, following a call by the G20 to 'strengthen the global response to proliferation financing',³² the FATF began to formally explore extending the risk assessment requirement of Recommendation 1 to include PF.³³ Subsequently, in October 2020 the FATF agreed and adopted new requirements in Recommendation 1 and the accompanying Interpretive Note, that expand the risk assessment provision to include PF, directing countries to 'identify, and assess the risks of potential breaches, non-implementation or evasion of the targeted financial sanctions related to proliferation financing, as contained

29. Marshall Billingslea, 'Objectives for FATF-XXX (2018–2019): Paper by the Incoming President', FATF, 2018.

30. FATF, 'The FATF Recommendations', p. 10.

31. See US Department of the Treasury, 'National Proliferation Financing Risk Assessment 2018'; HM Treasury, 'National Risk Assessment of Proliferation Financing', September 2021. Reflecting the fact that the absence of a risk assessment requirement for CPF represented an important gap in the FATF standards, RUSI developed a guidance paper for countries wishing to conduct a national proliferation financing risk assessment, along with the publication of an online risk assessment tool in 2020. Both have since been consulted and used by many jurisdictions. See Anagha Joshi, Emil Dall and Darya Dolzikova, 'Guide to Conducting a National Proliferation Financing Risk Assessment', RUSI Special Resources, May 2019; RUSI, 'Proliferation Financing Risk Exercise', <<https://www.rusi.org/explore-our-research/projects/proliferation-financing-risk-exercise>>, accessed 27 October 2021.

32. Ministry of Finance of Japan, 'Communiqué, G20 Finance Ministers and Central Bank Governors Meeting, Fukuoka', 8–9 June 2019, <https://www.mof.go.jp/english/policy/international_policy/convention/g20/communique.htm>, accessed 10 October 2021.

33. Between June 2019 and October 2020, the FATF consulted with key public and private sector stakeholders. The authors took part in the consultation process.

in FATF Recommendation 7, and to take action to mitigate these risks, as well as to enhance domestic co-ordination'.³⁴

Underlining the importance of this development, the FATF emphasised that it 'expects all countries and regions to take concrete steps to ensure implementation of these new obligations ... to enhance compliance with the FATF Standards and better safeguard the international financial system from abuse'.³⁵

In sum, understanding where legal and policy gaps exist, whether sufficient resources have been allocated, and whether the private sector is aware of and implements its obligations, among many other factors to be considered in a risk assessment, will directly aid the effective implementation of targeted financial sanctions, something that the analysis conducted for this paper demonstrates remains highly varied.

However, as the FATF has introduced this new standard and is preparing to begin another round of evaluations where countries will be assessed against this requirement, lessons from the implementation of current standards should be kept in mind to ensure that the uneven implementation record experienced on Recommendation 7 and Immediate Outcome 11, as evidenced in this paper, is not repeated.

34. FATF, 'Public Statement on Counter Proliferation Financing', 23 October 2020, <<https://www.fatf-gafi.org/publications/financingofproliferation/documents/statement-proliferation-financing-2020.html>>, accessed 25 August 2021.

35. *Ibid.*

Conclusion

Since the FATF added CPF requirements to its standards in 2012, country responses – and those of the organisations that promoted the need for the FATF to embrace CPF – have lagged. There is a clear lack of awareness on CPF in both public and private sectors around the world, spanning developing and developed countries alike. Awareness of PF risk varies considerably between countries, and even where PF risks are high due to geographic proximity to a proliferation threat, such as North Korea, or because of the presence of historic diplomatic or trade ties, sensitivity to this risk is often low. This lack of awareness is evident in the poor results revealed by countries' mutual evaluations, on both an absolute basis and relative to TF.

This paper finds that:

- **After almost a decade of PF being included in the FATF's standards, the compliance among assessed jurisdictions remains varied.** While 50% of jurisdictions are deemed either compliant or largely compliant with Recommendation 7, 20% are still not compliant with the technical requirement to implement targeted financial sanctions related to proliferation 'without delay'.
- **Only two jurisdictions have received high effectiveness ratings for Immediate Outcome 11.** Fifty percent of assessed jurisdictions were still recorded as having low effectiveness when it comes to countering PF domestically. This picture may be more positive as Immediate Outcomes are not re-rated as often as Recommendations.
- **The initial PF assessment of jurisdictions has not improved over time.** Given the extent to which mutual evaluations are scrutinised when they are published, it would be expected that those countries that are yet to be evaluated would seek to learn lessons from previous cases and implement changes that improve their prospects when their turn to be evaluated comes. This appears not to be the case and, indeed, in some cases, the results in later assessment years are worse than the results received by jurisdictions in earlier assessment years, raising questions as to how learning and best practice are shared.
- **The data reveals that although a majority of jurisdictions (60%) did receive the same initial ratings for PF and TF, a meaningful proportion of jurisdictions performed better on their TF requirements than they did for PF.** This suggests that this latter category of jurisdictions were either more aware of their obligations on TF or devoted more attention and resources to implementation of TF controls. Of the jurisdictions that performed worse on PF, a significant majority received the lowest ratings for Recommendation 7 and Immediate Outcome 11, 75% and 80% respectively.
- **There are key differences between FATF regions and their performance record on PF.** Some regions performed significantly worse than others in their initial ratings but have, at the same time, also been the regions to improve the most since.

With this analysis in mind, as the FATF introduces its new and expanded CPF standards, notably the requirement to conduct a PF-related risk assessment, the lessons that emerge from the analysis discussed in this paper should be considered. Therefore, in introducing these new requirements, the FATF must:

1. Ensure that its regional bodies are empowered and equipped to provide the necessary guidance and support to their member countries to avoid regional differences in implementation that proliferators can exploit.
2. Ensure that the new requirement to conduct a risk assessment for PF is prioritised by countries to the same extent as other assessments – namely, the requirement to conduct a risk assessment on ML and TF – to avoid the implementation gaps that have been observed between PF and other financial crime risks on the existing PF standards.
3. Ensure that the lessons and best practices from those that are first subject to the new risk assessment requirement are used to inform the process of jurisdictions whose assessments are later in the assessment calendar. Facilitating the transfer of best practice should be prioritised by the FATF.

About the Authors

Emil Dall was previously a Senior Research Fellow for the Centre for Financial Crime & Security Studies at RUSI. His research focuses were on sanctions policy and counter-proliferation finance. Emil's work on counter-proliferation finance examined the design and implementation of international sanctions against proliferators (including North Korea), and aimed at understanding the role of governments and financial institutions in countering proliferation finance. Emil also conducted research on the use of sanctions in foreign policy, including the design and implementation of country-based sanctions regimes, and was involved in the Institute's high-level Task Force on the Future of UK Sanctions Policy. Prior to joining RUSI in 2015, Emil was a risk analyst for a major international insurer operating out of Lloyd's of London, and before that he was a researcher at the Policy Institute at King's College London. He holds degrees from the University of Cambridge and the Department of War Studies at King's College London, and was a 2017 Nuclear Scholar at the Center for Strategic and International Studies in Washington, D.C.

Tom Keatinge is the founding Director of the Centre for Financial Crime and Security Studies (CFCS) at RUSI, where his research focuses on matters at the intersection of finance and security. He has a Master's in Intelligence and International Security from King's College London, where he studied the effectiveness of the global counterterror finance regime. Prior to joining RUSI in 2014, he was an investment banker for 20 years at J.P. Morgan.

Annex

Table 1: Current Recommendation 7 Ratings for the 118 Mutual Evaluation Reports (and Follow-Up Reports) Conducted up to and Including 7 October 2021

Rating	Count of Latest Recommendation 7 Rating
Non-Compliant	24
Partial	35
Largely	44
Compliant	15
Total	118

Table 2: Immediate Outcome 11 Ratings for the 118 Mutual Evaluation Reports (and Follow-Up Assessments) Conducted up to and Including 7 October 2021

Rating	Count of Latest Immediate Outcome 11 Rating
Low	59
Moderate	38
Substantial	19
High	2
Total	118

Table 3: Initial Recommendation 7 Ratings by Year

Year	Non-Compliant	Partial	Largely	Compliant	Number of Assessments
2014		2			2
2015	5	2	1	1	9
2016	6	4	5	1	16
2017	6	8		3	17
2018	13	7	5	1	26
2019	7	7	9	2	25
2020	1	4	4		9
2021	6	6	2		14
Total	44	40	26	8	118

Table 4: Initial Immediate Outcome 11 Ratings by Year

Year	Low	Moderate	Substantial	High	Number of Assessments
2014		2			2
2015	5	3	1		9
2016	6	3	6	1	16
2017	9	3	5		17
2018	17	6	2	1	26
2019	12	8	5		25
2020	3	6			9
2021	7	7			14
Total	59	38	19	2	118

Table 5: Recommendation 7 Ratings in Relation to Recommendation 6 Ratings for the Same Country

Category	Count
Higher	7
Lower	40
Same	71
Total	118

Table 6: Immediate Outcome 11 Ratings in Relation to Immediate Outcome 10 Ratings for the Same Country

Category	Count
Higher	13
Lower	24
Same	81
Total	118

Table 7: Initial Recommendation 7 Ratings by FATF Region

Region	Non-Compliant	Partial	Largely	Compliant	Count
APG	14	2	2	1	19
CFATF	5	2	3		10
EAG	1	1	1		3
ESAAMLG	10	1			11
FATF	2	16	7	5	30
GABAC	1				1
GAFILAT	3	3	5		11
GIABA	2	3	2		7
MENAFATF	4	2	1		7
MONEYVAL	2	10	5	2	19
Total	44	40	26	8	118

Table 8: Current Recommendation 7 Ratings by FATF Region

Region	Non-Compliant	Partial	Largely	Compliant	Count
APG	6	4	7	2	19
CFATF	3	2	5		10
EAG		1	1	1	3
ESAAMLG	6	2	2	1	11
FATF	2	11	9	8	30
GABAC	1				1
GAFILAT	1	3	6	1	11
GIABA	2	3	2		7
MENAFATF	3	2	2		7
MONEYVAL		7	10	2	19
Total	24	35	44	15	118

Table 9: Upgraded Recommendation 7 Ratings by Region

Region	Number of Ratings	Ratings with No Upgrade	Not Possible (Already Compliant)	Ratings with Upgrade	Percentage of Available Upgrades
APG	19	9	1	9	50%
CFATF	10	8		2	20%
EAG	3	1		2	67%
ESAAMLG	11	7		4	36%
FATF	30	20	5	5	20%
GABAC	1	1			0%
GAFILAT	11	9		2	18%
GIABA	7	7			0%
MENAFATF	7	6		1	14%
MONEYVAL	19	11	2	6	35%
Total	118	79	8	31	

Source: All data in the Annex tables comes from FATF, 'Consolidated Table of Assessment Ratings', <<https://www.fatf-gafi.org/publications/mutualevaluations/documents/assessment-ratings.html>>, accessed 10 October 2021.