

# FINANCIAL ANALYTICAL OFFICE



ANNUAL REPORT  
2018

*Dear Reader,*

*I am pleased that you decided to familiarize yourself with the 2018 Annual Report of the Financial Analytical Office. The Office was established on 1 January 2017 and fulfils the role of a financial intelligence unit of the Czech Republic.*

*The Report assesses functioning of the Office both in terms of organization and in terms of performance in all its core activities. It summarizes information on activities of the Office in the previous year 2018, provides information on current development in the area of anti-money laundering and countering the financing of terrorism and predicts its further development in the Czech Republic. The information is complemented by an overview of statistical data.*

*As in previous years, I would like to thank all employees of the Office for the good work they have carried out and their enthusiasm. Without all that, it would not be possible to present results of our work in this Report.*

*The Financial Analytical Office has been operating as an independent administrative authority for two years already and that is also a point of view from which its activity has to be assessed. I would very much like to thank all stakeholders, i.e. the so-called obliged entities, particularly from the banking sector, for their helpful cooperation. Without them the effective fight against money-laundering and detection of terrorist financing would not be possible. This collaboration has been on a very high and professional level. The Financial Administration, Customs Administration as well as law enforcement authorities have also contributed significantly to the presented results. In 2018, the AML/CFT system of the Czech Republic was evaluated by the MONEYVAL Committee of the Council of Europe with good results and also future challenges regarding where and how to further improve the system.*

*Results in analysed cases would not be possible without effective international cooperation, which I would like to appreciate as well, in particular very good collaboration with foreign partner financial intelligence units.*

*Libor Kazda*

*Director of the Office*

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# ANALYTICAL WORK

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***The Financial Analytical Office (the FAU) fulfils its statutory competences, particularly the role of a central state body for collection and analysis of transactions suspected of an attempted legalization of proceeds of crime or linked to terrorist financing.***

The primary task within the scope of its competence is prevention of abuse of the financial system of the Czech Republic for money laundering and terrorist financing. More and more attention has been paid to both issues because of their importance and global impact. Money laundering causes astronomical damage to global economy and last but not least generates seemingly legal profits for further criminal activity. In case of drug-related crime the harm caused to often innocent human victims is incalculable. The severity of terrorism is needless to emphasize. The set of measures aimed at both areas is provided in Act No. 253/2008 Sb., on Selected Measures against Legitimation of Proceeds of Crime and Financing of Terrorism, as amended (the so-called AML Act), which defines competences, powers and duties of individual elements of the system. The system is based on providing information on suspicious transactions by legally defined entities, the so-called obliged entities, i.e. banks, other financial institutions and a range of other entities, to the FAU. Analysis of suspicious transactions is the foundation of FAU activity. The aim is to verify the initial suspicion and collection of further information necessary for decision on the course of action. The procedural output of the examination is primarily reporting to the law enforcement authorities, providing information to the tax administration or other institutions based on statutory empowerments and in case of an international element dissemination of information to a foreign financial intelligence unit.

In 2018, the FAU received 4,028 suspicious transaction reports. It is the highest number of reports received in the history of the FAU and a rapid increase of 504 reports compared to the previous year. It is mainly due to widening of the scope of obliged entities and increasing international cooperation in the form of dissemination of information in the global network of financial intelligence units. The statutory exchange of information with tax administration and security forces, in particular with the Police and intelligence services, has also intensified.

**4,028**

**suspicious  
transaction  
reports  
received**

In the long-term, the FAU has paid more attention to large-scale sophisticated cases than to “petty crime”, which can be successfully solved by other state administration bodies without FAU’s participation. This process logically leads to the decrease in reporting to the Police — 395 reports in 2018 compared to 539 reports in 2017. At the same time, the FAU provided the Police with other 160 pieces of information important for Police work, which is a new statutory way of cooperation between the FAU and the Police. Almost 70% of reports to the Police, namely 268, were accompanied by simultaneous blocking of funds.

**395**

**reports to the Police**

In 2018, the FAU seized CZK 7.546 billion, i.e. almost CZK 4 million every working hour.

This is also the highest amount in the history of the FAU and at the same time it represents a rapid increase compared to 2017, when CZK 2.146 billion was seized. These numbers clearly show FAU's endeavour to pay the utmost attention to current cases, where there is a real possibility to seize proceeds of crime, since recovering illegal proceeds usually hurts perpetrators more than application of other criminal-law instruments.



In 2018, mutual cooperation with tax administration was traditionally extensive. 2,362 informative letters containing suspicion on breaches of tax or customs regulations were sent to the Financial Administration and the Customs Administration. It is a significant increase of 609 letters in a year-on-year comparison. In terms of underlying criminal activity, the most frequent were various forms of fraud ranging from simple one to highly sophisticated. Also 'CEO fraud' continues to be frequent. Other often occurring types of crime include tax crime, insolvency offences, corruption and drug-related crime. Traditionally used money-laundering techniques have not changed much and include repeated transfers among bank accounts in the Czech Republic and abroad, cash deposits and withdrawals, bank accounts opened under false or stolen identity, remittance services, tax heavens, investment in real estate and also virtual currencies. More techniques are usually combined depending on the underlying crime, level of organization, intellectual capacity of the perpetrator etc. The statistical data provided confirm, that the Czech AML/CFT system is able to effectively deal with the abovementioned techniques used by perpetrators. In general, the level of AML measures applied in Czech banks is very high. Banks respond flexibly to current trends in the AML/CFT area and take appropriate measures.

Regarding banks, it has to be noted that they have recently significantly increased investment in this area, both in terms of IT and human resources deployed in their AML compliance units. A specific feature of the banking sector is, that most banks are foreign-owned and their parent companies require fulfilment of AML obligations of their local subsidiaries in parallel with domestic regulators (the FAU and the Czech National Bank). Indeed, some of the parent companies have themselves experience with penalties in orders of units of percentage of annual turnover for non-compliance with AML obligations and for this reason they invest in this area even though it does not generate profit.

On the contrary, more room for improvement is in the non-banking sector. A group of non-banking or rather non-financial institutions has become obliged entities only recently based on the assessment of risk they pose in terms of money laundering and terrorist financing. It is now necessary to work adequately with these entities, to raise their awareness, provide them with feedback or respond repressively in case of non-compliance with AML obligations.

## TERRORIST FINANCING

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***Primary detection of terrorist financing in the banking system contributes to reducing the threat of terrorism.***

In 2018, with regard to current global situation, the FAU focused intensively on terrorist financing issues. The FAU received dozens of suspicious transaction reports with terrorist subtext. Not all initial suspicions were subsequently confirmed, nevertheless some examinations led to reporting to the Police or dissemination of information to counterparts. In general, the year 2018 was in the spirit of enhancing cooperation with the Police and intelligence services of the Czech Republic. Methodological work towards obliged entities, in particular towards banks, was also intensified with the aim of facilitating and supporting detection of suspicious activities.

In view of the continuing threat of terrorism worldwide, related financial needs of individual terrorists and terrorist organizations and the complexity of detection of activities used to secure financial resources, the FAU considers countering the financing of terrorism as one of its priorities.

# INTERNATIONAL COOPERATION IN ANALYTICAL MATTERS

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***The FAU is one of 159 members of an international network of financial intelligence units.***

It is no surprise that in 2018 the vast majority of money laundering and terrorist financing cases contained an international element. This international element consisted mainly of cross-border transactions, where perpetrators used modern banking or other payment systems to quickly transfer funds, or otherwise move illegal assets abroad, mainly to jurisdictions with inadequate AML/CFT measures. A number of cases was detected, where perpetrators involved in this type of criminal activity came from abroad or established legal entities abroad and subsequently involved these entities in money laundering. For these reasons, it was necessary to complement the national AML/CFT measures by an effective system of international cooperation. This system allows exchanging a wide range of information necessary for proper analysis of reported suspicious transactions. An important feature of this information exchange system is undoubtedly its promptness which enables adequate response to the speed of today's international money transfers. Last but not least, an effective system of international AML/CFT cooperation should allow for temporary restriction of handling with funds or other assets abroad, in case there is a suspicion of them being proceeds of crime.

Statistics show that the trend of quantitative growth in operational exchange of information with foreign FIUs continued in 2018, and the quality of information exchange also increased. The exchange of information included, *inter alia*, financial information, beneficial ownership information, law enforcement information, customer due diligence documents, information from the Commercial Register including links between legal entities and individuals, property ownership data and other relevant information. During 2018, the suspension of client's order (i.e. temporary blocking of funds) was repeatedly applied in international information exchange both in the Czech Republic on the basis of a foreign request and abroad on the basis of FAU request. An important progress was FAU's active participation in a pilot multilateral case; this type of cooperation should become a common practice in the future. In view of the abovementioned facts, international cooperation in individual cases can be regarded as highly professional and effective.



# PREDICTION OF MONEY LAUNDERING AND TERRORIST FINANCING TRENDS

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***Based on an analysis of cases of suspicious transactions examined during 2018, it can be assumed that in the coming upperiod, same as in previous years, the following forms of legalization of proceeds of crime will prevail among detected money laundering activities.***

- Misuse of bank accounts under false or stolen identity
- Investment of proceeds of crime committed in the Czech Republic and abroad in domestic real estate
- Misuse of business bank accounts in the Czech Republic as pay-through accounts for cross-border wire transfers of proceeds of crime committed domestically and abroad
- Abuse of crypto currencies, electronic payment gateways and e-money wallets

In addition, the assessment of current trends further identified activities in the area of money laundering that may see a significant increase in 2019.

In particular, these phenomena are:

- Abuse of business activities of companies, where the perpetrator has no or insignificant link to the Czech Republic, the companies are controlled by foreign individuals or legal entities established in countries of the former Soviet Union (from the experience to date, wholesale trade in agricultural products is a typical type of business)
- Abuse of services of small-scale payment service providers
- Abuse of so-called non-face-to-face identification when opening a bank account; the account is opened based on an on-line application while using a counterfeit or false identity

In terms of underlying criminal activity, the current experience shows that **various types of fraud** will be also significant in 2019:

- Investment fraud including fraud with corporate bonds
- On-line fraud in connection with goods offered on various websites and e-shops
- Fraud using methods of social engineering, currently e.g. misuse of trust and luring of funds based on pretended interest in starting a relationship, when a perpetrator feigns to be a soldier on a military operation abroad or a woman, who seeks a relationship with an individual from the Czech Republic
- CEO fraud —unauthorized change of a bank account in order to collect an invoiced amount, which includes unauthorized access to victim's IT resources

**Tax fraud, despite pro-active measures taken by the Financial Administration.**

# NEVERENDING STORIES

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*As usually, we bring you often incredible stories that accompany cases analysed by the FAU.*

## **Money from prostitution ended on Czech bank accounts**

The FAU received an urgent request from a foreign financial intelligence unit regarding individuals and companies that were investigated abroad for particularly serious crime (child abuse, human trafficking and prostitution).

An organized group active in many countries used a web-based advertising portal to offer sexual services. Minors were also abused for these services. Almost 100 million US dollars (real estate, bank funds and personal property) was seized by the prosecution abroad, revealing that part of the proceeds of this crime was transferred to bank accounts held in the Czech Republic.

A foreign FIU asked the FAU to secure funds in the bank accounts that had been identified in connection with this crime. Thanks to the fast response and professional work performed by the FAU, approximately CZK 234 million was secured and a report was filed with the Police.

## **Not-responding individuals and hundred million turnover**

Also, this case clearly shows how important the FIU to FIU cooperation is. Foreign individuals established a business corporation in the Czech Republic for which they opened a Czech bank account. Payments from abroad in orders of hundreds of millions of crowns a year were deposited to the account. The funds were subsequently withdrawn in cash. The fact that this business corporation did not have any business premises in the Czech Republic in which it would have carried out its business activities was also suspicious, as objects of the company was Intra-Community supply of goods that were hardly identifiable (bulk goods, without serial numbers, used goods).

It was found by the tax administrator that the business corporation reported only trilateral transactions with other Member States in the VAT return. Foreign FIUs informed that alleged foreign customers are not responding and do not carry on business. These facts gave rise to a reasonable suspicion that proceeds of crime were laundered through the Czech commercial corporation and the bank was presented with fraudulent documents on the purpose of transactions.

In view of the circumstances identified, the FAU issued a decision to suspend the handling of funds in the bank account of the corporation and reported to the Police a suspicion of committing a money laundering offence under Section 216 of the Criminal Code and a crime of fraud under Section 209 of the Criminal Code. Subsequently, the law enforcement authorities secured the funds in the bank account of the corporation under the relevant provisions of the Criminal Procedure Code.

## **Maybe Sylvester appears as well**

When entrepreneurship in the home country brought only a distraint and a police investigation for fraud to a thirty-year-old foreigner, he moved his activities to the Czech Republic, where he became the executive of several companies, which he later controlled through another foreign entity. Exaggerated advertising attracted residents to meet with action film star Sylvester Stallone. However, this event, as well as similar previous events, did not take place and was moved by the organizer because of 'unpredictable organizational problems on the part of the foreign organizer'. Funds for purchased tickets were continuously withdrawn from the company's accounts by cash or transferred to accounts of the entrepreneur and his girlfriend. And Sylvester Stallone? He was not in Europe at that time and does not participate in similar events. The FAU reported the case to the Police.

## **Straw man from abroad and USD 13 million**

Unfortunately, also in the Czech Republic there are cases where the main motive is to launder criminal money. There are entities and individuals involved in professional money laundering which are part of an international criminal organization. In the Czech Republic, a Czech corporation with a fictitious seat and an opaque foreign ownership structure was identified, which never showed any economic activity. The managing director of this company was a foreign straw man.

This corporation opened a bank account in the Czech Republic, which was managed directly from the Russian Federation by a Russian citizen based on a power of attorney. The managing account holder was found to be in the Panama Papers (note: a leak of 11.5 million secret documents from Panamanian company Mossack Fonseca, which details more than 214,000 offshore companies and their ownership structure), and was investigated for money laundering in the past. Within five days, a total of USD 13 million was credited to the account of the Czech corporation for computer components from a Russian company without notable business history. The Czech corporation declared the delivery of computer components to the Russian Federation, which it purchased from a Bahamian company with an account in Luxembourg.

Contracts and invoices submitted to document these payments subsequently proved to be fictitious. By examining the flow of goods and reimbursements for them, it was found that the allegedly purchased goods for more than USD 13 million from a Bahamian company was never acquired or paid by the Czech corporation. In addition, the analysis of the Czech corporation's cash transactions revealed that in fact the financial flow was entirely the opposite of what it should be from a commercial point of view (the trade in goods could not take place according to the claims of engaged individuals).

Subsequently, other foreign individuals involved in the case were screened, and it was found that they were also investigated for money laundering in the past. Suspicion of committing the crime of legalization of proceeds of crime and the crime of fraud and suspicion of tax crime overlapping abroad were reported to the Police and bank accounts of the Czech corporation identified as an accomplice with respect to criminal liability of legal persons were secured. The FAU has seized USD 13.3 million in this case.

## **Hundreds of thousands of US dollars from Eastern European countries**

As part of standard AML procedures, a bank informed the FAU of a problematic transaction in a client's account. The FAU initiated an investigation and found that the account holder was a Czech company with a vague past, whose owners had changed a few weeks before from a Polish citizen to a Czech citizen who, after a week, sold the company to his neighbour.

Until the last time it was sold, the company did not show any economic activity, but soon after the last change of ownership, it received payments of hundreds of thousands of US dollars from Eastern European countries. The company owner tried to send the received funds to other always Eastern European accounts that were held in countries outside the EU.

In a very short time, the FAU gathered enough evidence from which it was possible to infer with a high degree of probability the misuse of an account at the Czech bank for money laundering. This was reported to the Police and a decision on suspension of the execution of the client's order was made under the relevant provisions of the AML Act. Thanks to this procedure, an amount in excess of USD 6 million was seized.

## **Misuse of cryptocurrency**

The FAU detected an increasing trend of so-called 'ICO fraud', i.e. publicly and non-publicly offered new cryptocurrency emissions based on fraudulent projects, in order to lure funds from investors.

In the period of eight months, payments to foreign currency bank accounts of a Czech company were credited mainly from foreign individuals in the total amount of approximately EUR 7 million. The company intended to transfer part of the credited funds to other foreign accounts. The reason of the transfer should have been an alleged investment in a newly issued foreign cryptocurrency, which was nowhere publicly traded.

The available information showed that those interested in ICO of a foreign company are persons recruited at non-public seminar, especially organized abroad where the offer of the cryptocurrency was present.

The Czech company provided some contradictory statements to clarify the source of funds, including contractual documentation, which had been continually amended as required under the customer due diligence, with the obvious objective of concealing the origin of the funds received.

Indirect evidence demonstrating the possible fraudulent modus operandi of the case included negative information in open sources on both the cryptocurrency issued and to the individuals acting on behalf of the foreign issuer. The project scheme is referred to as 'MLM', i.e. multi level marketing, based on the Ponzi scheme, similarly to other already known fraudulent ICOs, e.g. OneCoin, etc.

Based on the facts found, the FAU seized foreign-currency balances of the Czech company (including outgoing payments entered) in the order of millions of euros and reported the case to the Police.

## **EUR 170 thousand in a Porsche car**

The FAU received from the Directorate General of Customs information on a roadside control of two Italian citizens at the former Italian-German border crossing. Their Porsche Panamera car carried cash amounting to about EUR 170,000. When asked by the German customs authorities for what purpose the funds were being transferred, they were told by the driver that the money would be used to purchase two vehicles in the Czech Republic through the company they own. Thus, the FAU became interested in this company, finding that there were suspicious transactions on its accounts, especially incoming payments from foreign entities controlled by Italian citizens. Auditing these accounts, high incoming transactions were identified, mainly from Italian accounts of Italian companies trading mineral oils, mainly supplied to the Slovenian and Italian markets.

A more detailed analysis of selected transactions detected an unusual flow of funds for the acquisition of mineral oils. Part of the funds was sent for the purchase of goods from refineries, part of them was sent to Polish and Bulgarian accounts. The following investigation revealed that transactions in Polish accounts were used for the acquisition of base oil-like goods, which are not classical mineral oils usable directly as fuel, but historically this type of oil was misused as fuel without the excise duty being paid to the State.

Funds were sent to the Bulgarian accounts for the purchase of mainly electronics and textile goods, a relatively heterogeneous commodity to trade in mineral oils.

In the context of all the information analysed, in cooperation with domestic and foreign banks and cooperation with foreign FIUs, it was predicted that oils purchased in Poland could have been sold on the Italian market without excise duty and value added tax. Unpaid taxes could have been laundered by the purchase of goods through the Bulgarian bank accounts.

On the basis of these conclusions, a report was filed with the Police on a suspicion of possible legalization of tax proceeds and the FAU also seized EUR 1.5 million.

## **Tens of thousands of dollars were supposed to be transferred to Asia**

A new customer, a legal entity, signed a contract with a banking institution on the use of currency conversion services and foreign payment intermediation. Shortly thereafter, the customer's legal representative placed orders for tens of thousands of US dollars in foreign exchange payments directed to recipients, both natural and legal persons, in Vietnam and China, and paid the corresponding amount in Czech crowns. In accordance with the AML Act, a standard customer due diligence was launched to confirm the financial profile. Due to the low level of customer's interaction, the bank reported a suspicious transaction and the execution of payment orders was suspended.

Analysis found that the customer did not have a properly registered business account with the tax administration and was not registered for VAT. In the past, the relatively new statutory body of the company featured in companies with registered VAT arrears and executions records. A representative of the company stated that another company's account to which he had managing rights was the company's customer account. The representative was able to comment on the origin of the cash deposit only 'after consultation'. Copies of underlying invoices sent by him were in contradiction with the company's registered business and formal errors of invoices were also evident.

In view of the suspicion that he acted as a straw man engaged in companies threatened with distraint by the tax administrator, tax arrears or executions that were not repaid and whose economic activity was subsequently shifted to another entity, the funds on the customer account were seized. Justified suspicion of possible legalization of proceeds of crime was reported by the FAU to the Police and relevant information was provided to the Czech tax administration.

# INTERNATIONAL ACTIVITIES AND LEGISLATIVE WORK

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## ***Development in the area of money laundering domestically and internationally.***

In May 2018, General Data Protection Regulation, the so-called GDPR, came into effect. The FAU, as well as almost all public authorities and private entities, had to take certain steps in order to comply with this Regulation. In connection with GDPR and taking into account the wide range of obliged entities and experience with international requirements, the AML Act had to be amended so that essential elements of data protection were either incorporated into the Act or at least specifically referred to. The amendment proposed clear legal title for processing personal data, which is the fulfilment of legal obligation. Entitlement of legal entities to process personal data without consent of the data subject results directly from the GDPR. In accordance with requirements of the Regulation and because of specificities of FAU activities and the scope of its competences, it was necessary to propose FAU's own data protection officer, thus an amendment of the institution of data protection officer was also proposed.

On 19 June 2019, Directive (EU) 2018/843 of the European Parliament and of the Council of 30 May 2018 amending Directive (EU) 2015/849 on the prevention of the use of the financial system for the purposes of money laundering or terrorist financing, and amending Directives 2009/138/EC and 2013/36/EU (hereafter as '5<sup>th</sup> AML Directive'). As its title implies,



it is a revision of the previous Directive, and a response to terrorist attacks in Europe, as well as response to the Panama Papers case. The basic implementation period for most of its articles is 18 months and expires on 10 January 2020, the time limit for provisions dealing with beneficial ownership register and bank accounts register is longer.

In this context, the FAU currently prepares an amendment to the AML Act and related legislation, reflecting in particular requirements of the 5<sup>th</sup> AML Directive and taking into account and incorporating recommendations from the 5<sup>th</sup> AML/CFT Mutual Evaluation Report of the Czech Republic produced by the Council of Europe's independent monitoring and evaluation body - the Moneyval Committee. When drafting the proposed AML Act, requirements arising from practical application of the Act are also taken into account on the basis of consultations with representatives of obliged entities and cooperating state authorities. The main changes that the draft amendment contains are the introduction of enhanced customer due diligence, the possibility of non-face-to-face identification for all types of obliged entities, the introduction of electronic identification through a qualified trust service provider under the Electronic Identification Act, the publication of a list of public functions whose holders are regarded as politically exposed persons, the introduction of a register of persons providing services related to virtual currency and the adjustment of sanctions for committing a delict in the AML/CFT area. It is also necessary to implement those measures of the 5<sup>th</sup> AML Directive which introduce a publicly accessible register of beneficial ownership information, a compulsory register of bank accounts, the unification of approach towards high-risk third countries, the reduction of limits on anonymous prepaid cards, the extension of FIU's authorization and the extension of cooperation between supervisory authorities.

An important change that will affect a wide range of entities is the extraction of the beneficial ownership issue into a separate law. At present, the transparency of ownership issue is widely addressed and discussed not only in terms of prevention of money laundering and terrorist financing. All legal entities registered in a public register and all trusts registered in a register of trusts have the duty to register their beneficial owner in the register of beneficial owners. Due to the fact, that this obligation is binding not only for obliged entities under the AML Act, but on all above-mentioned legal entities, and because this issue goes beyond the scope of the AML Act, it is proposed to extract it into a separate law. The register of beneficial owners was established as of 1 January 2018 and legal entities registered in the Commercial Register had to be registered in it by 1 January 2019; other legal entities registered in other public registries (including trusts registered in the register of trusts) have to register their beneficial owner until 1 January 2021. Registry courts keep records of beneficial owners. The 5<sup>th</sup> AML Directive newly introduced an obligation that data recorded by Member States

in registers of beneficial owners are adequate, accurate and up-to-date and that effective, proportionate and dissuasive measures or sanctions are imposed for the failure to fulfil this obligation.

On 1 October 2018 Decree of the Czech National Bank no. 67/2018 Sb., on Selected Requirements for the System of Internal Rules, Procedures and Control Measures against Legitimation of Proceeds of Crime and Financing of Terrorism came into effect. The Decree extends and specifies obligations of selected obliged entities, namely financial and credit institutions, and non-bank providers of consumer credit and their intermediaries. These institutions are obliged to identify and assess risks of money laundering. The Decree further specifies duty to develop a system of internal rules, in which the obliged entities determine the level of risk they are willing to take and the way they deal with such risk. The Decree, beyond the scope of the AML Act, also requires an evaluation report to be drawn up at least once every 12 consecutive calendar months.

# MONEYVAL

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## ***How the Czech Republic did in the 5<sup>th</sup> round of mutual evaluation and what needs to be improved.***

The fundamental elements of the fight against money laundering and terrorist financing are set in the FATF Recommendations 2012. Compliance of individual jurisdictions with the Recommendations and the effectivity of prevention, detection, investigation, prosecution and conviction in this type of crime in practice is comprehensively assessed. The purpose of the international anti-money laundering and counter terrorist financing framework is clear - to ensure the most comparable conditions in the international financial market and to align to a large extent money laundering and terrorist financing standards and practices in order to prevent abuse of the financial market for criminal activity.

The Czech Republic was evaluated from 2017 to 2018. On 5 December 2018, the 57<sup>th</sup> Plenary Session of the Moneyval Committee in Strasbourg adopted the 5<sup>th</sup> round Mutual Evaluation Report on the Czech Republic. In this report, Moneyval acknowledged progress made by the Czech Republic from the last evaluation in 2011, but also highlighted some shortcomings that needs to be resolved in the Czech Republic in order to be in compliance with the FATF Recommendations. The shortcomings involved primarily limited resources, effectivity of supervisory authorities, missing aspects of risk assessment, more active approach to investigation of standalone money laundering and third party money laundering and duration of the cases starting from initial detection to final court decision.

Based on the results, the Czech Republic was placed under enhanced follow-up procedure. As part of this process, it will report to Moneyval on the implementation of binding recommended actions, the first report is due in mid 2020.

Recommended actions that have to be implemented in the coming years include e.g. the need to update and extend the national risk assessment so that it comprehensively analyses risks in all areas and works with all available information while at the same time being "user friendly" for the private sector. The report also takes note of the need for active feedback on the use of financial intelligence from the FAU. The Czech Republic should more support the investigation of complex money laundering cases and seek to shorten the pre-trial period so that the time from detection to the final judgement is shortened.

A number of recommended actions focuses on supervision of compliance with the AML Act. Recommended actions involve strengthening of human resources, the need to impose higher pecuniary sanctions, and possibility to impose penalties for delicts not only on legal entities, but also on individual members of senior management. Last but not least, Czech authorities should continue in outreach activities, providing lectures for and consultations to the private sector, and also improve licencing of private entities in terms of preventing criminals from exerting influence on obliged entities and verification of origin of funds.

The results of evaluation can be divided into two areas — effectiveness of the national AML/CFT system and technical compliance with the FATF 40 Recommendations. The technical compliance evaluation focused on analysis of legal rules in individual areas addressed by the FATF Recommendations. Evaluation of effectiveness is entirely new and its assessment was carried out for the first time. The jurisdiction concerned is assessed in terms of effectivity of compliance with objectives of FATF Recommendations. The effectiveness evaluation is divided into 11 parts and the effectiveness of national AML/CFT regime is assessed as low/moderate/substantial/high.

Extensive communication with five evaluators and three members of the Moneyval Secretariat and a two week on-site visit of the evaluators and members of the Moneyval Secretariat in Prague on 5-16 March 2018 preceded the adoption of the report. The FAU was responsible for drafting the programme of the visit, invitation of experts, substantive coverage of a number of topics and other organizational issues, including simultaneous interpretation during the on-site visit to create a pleasant environment on a professional level for both evaluators and national experts.

The fact that over 430 national experts from public, private and non-profit sector participated at more than 50 meetings clearly demonstrates the complexity of this task and extraordinary commitment of FAU staff. In September a part of the evaluation team with the Vice-Chairman of the Moneyval Committee headed again to Prague in order to further discuss primarily confiscation of proceeds of crime and implementation of international sanctions, which are one of the most pressing issues for the FATF at the moment.

The evaluation report, which was published on the Council of Europe and FAU website on 11 February 2019, is a crucial background document for preparation of an action plan on implementation of recommended actions. The action plan will address identified shortcomings by proposing concrete measures and dividing responsibilities of individual ministries in these tasks.

# MONEY LAUNDERING AND TERRORIST FINANCING RISK ASSESSMENT

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***In the second half of 2018, the FAU began to work on a second round of an extensive national risk assessment process.***

The purpose of the national risk assessment process is to identify and evaluate risks of money laundering and terrorist financing in cooperation with all stakeholders and draft a report thereon.

The process is coordinated by the FAU and governed by the FATF Methodology, the AML Directive and the AML Act. Stakeholders in the public sector include: AML supervisory authorities, law enforcement authorities, tax administration, relevant sectoral and substantive regulators, ministries etc. The scope of involved actors reflects the breadth of the process, i.e. prevention of and combating money laundering and terrorist financing, which starts by customer due diligence and ends by conviction of perpetrators.

Stakeholders from the private sector such as obliged entities and their self-regulatory bodies and non-profit organizations, that demonstrate a legitimate interest in preventing these phenomena, will also take part in the process.

The FAU assumes that the cooperation will take place mainly through expert consultations. Those interested in joining the second round will find the information on the FAU website under the [National Risk Assessment](#).

The second round of national risk assessment will, *inter alia*, be based on the international evaluation by the Moneyval. Moneyval regarded the first round of the national risk assessment as a transparent and realistic analysis, yet pointed out some other relevant topics that need to be worked on.

New tasks arising from the Moneyval evaluation, supranational evaluation by the European Commission and from the 5<sup>th</sup> AML Directive will have to be incorporated into the national risk assessment process.

FAU had also carried out tasks from the first round, which were imposed by a resolution of the Government. The nature of these tasks was both legislative and non-legislative.

Furthermore, the FAU continued in dialogue with representatives of legal and advisory professions and in risk awareness raising. At several occasions, the FAU trained representatives of non-profit sector on possible abuse for terrorist financing. Last but not least, work on carefully drafted amendment of the AML Act was underway.

## INTERNATIONAL SANCTIONS

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### ***Information on implementation of international sanctions, which are binding in the Czech Republic.***

In 2018, in the area of implementation of international sanctions, the focus was mainly on strengthening sanctions against North Korea. The EU also agreed to continue its autonomous sanctions against the Russian Federation in the context of Russian-Ukrainian conflict.

In relation to Iran, unlike the United States of America which unilaterally withdrew from the agreed Joint Comprehensive Plan of Action (JCPOA) in May 2018, the EU as a whole continues to fulfil the Plan which, at the beginning of 2016, significantly reduced (but not repealed) counter Iranian sanctions. However, apart from the sanction regime targeting Iranian nuclear programme, the EU sanction regime imposed due to violations of fundamental human rights in Iran remain in force.

In 2018, sanctions were imposed against Maldives due to dissatisfactory situation in this island republic in the Indian Ocean in order to protect fundamental human rights. These sanctions are so-called autonomous EU sanctions, i.e. measures that are not based on a decision (resolution) of the Security Council of the United Nations. The sanctions imposed restriction on entry in the EU territory of designated individuals and the freezing of funds and other assets of designated natural and legal persons. By the end of 2018, the list of designated natural and legal persons remained empty, so there was not anyone on whom to impose the sanctions.

On the contrary, following the decisions of the UN Security Council, at the end of 2018, the EU completely and without substitution repealed sanctions against the African state of Eritrea. Due to the considerable geographical isolation of the territory and the small volume of mutual trade, the FAU has not dealt with any case relating to these sanctions, as well as to sanctions against Venezuela, which were adopted in 2017.

In the area of administrative proceedings in 2018, the FAU ruled on four applications for exemptions from various sanction regimes. One permit was issued in relation to South Sudan

and one in relation to the Russian Federation. Two other proceedings in relation to the Russian Federation were terminated. Apart from that, the FAU issued 31 explanatory statements on practical implementation of international sanctions and in the framework of collaboration of public authorities provided 39 opinions on specific cases of business cooperation with individuals and legal persons in territories affected by international sanctions.

In 2018, the FAU neither ruled on, nor imposed penalty for a breach of international sanctions. As in 2017, in 2018, measures imposed in the past on the property of two designated individuals, citizens of the Russian Federation and Ukraine, which was seized in the Czech Republic, remained in force.

In 2018, as part of its outreach in the form of educational and methodological work, the FAU staff took part as lecturers on a number of events organized mainly for the professional public and focused on possibilities of business cooperation with jurisdictions affected by international sanctions.

By the end of 2018, based on recommendation by the Moneyval evaluation, the FAU commenced to publish on its website not only information on persons newly designated by the UN but also on amendments to current UN listings and on delisting of persons from the UN sanction lists.

# SUPERVISION

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***The main pillars of supervisory activity are supervision of obliged entities and proceedings on transgression. An important part of supervisors' work is also the assessment of systems of internal rules of obliged entities.***

The supervisory activity of the FAU is performed by the Supervision Department in the Legal Division. The main document for supervisory work is the Yearly Inspection Plan. In its compilation, the FAU drew from the Instruction of the Director of the FAU dated 10 October 2017 on the Performance of Supervisory Activities and Compilation of the Yearly Inspection Plan, from new trends in the area of money laundering and terrorist financing and from the risk-based approach. In order to save money and avoid excessive burden on obliged entities, the FAU coordinates its Inspection Plan with other authorities supervising compliance with obligations from the AML Act (the Czech National Bank, the Directorate General of Customs and the Czech Trade Inspection Authority). The coordination consists mainly of the exchange of information on planned inspections and sharing of specific findings which can be used during inspections themselves.

Based on the risk-based approach, the Yearly Inspection Plan included supervision of entities, where major shortcomings in complying with AML obligations had been identified in the past, and of obliged entities that were subject of FAU internal motions. Systemic checks (i.e., inspections of more obliged entities of the same type) were also included in the Inspection Plan. In 2018, the FAU systematically inspected gambling operators because they became obliged entities on 1 January 2017.<sup>1)</sup>

In 2018, a total of 33 inspections was carried out, including 12 mystery shopping. Due to the incorporation of systemic checks into the Yearly Inspection Plan, gambling operators were the most frequently checked obliged entities — in 9 cases, out of which 2 were carried out in cooperation with the Directorate General of Customs with the aim to unify the application of inspection procedures by both supervisors. Banks were the second most frequently inspected obliged entities (4 cases).

Mystery shopping was performed at two locations with the highest share of shortcomings

<sup>1)</sup> Until 31 December 2016 only holders of casino betting licences under the Lotteries and Other Similar Games Act were considered obliged entities



identified in the past. One case concerned a regional city and the other case concerned a major touristic area with numerous foreign clients. The aim of the follow-up mystery shopping was to verify the functionality of measures taken by the obliged entities following previous inspections and violation proceedings. A major improvement was noted as “only” 4 out of 12 cases of mystery shopping showed certain deficiencies.

In comparison to 2017, the number of inspections was reduced by about one third. This decrease was caused by lower number of mystery shopping, as in 2018 mystery shopping was performed at only two locations (compared to four in 2017). Although the number of inspections was lower compared to previous years, the number of administrative proceedings remained almost unchanged. One of the reasons is appropriately applied risk-based approach when drawing up the Yearly Inspection Plan, because potentially high-risk entities were chosen for inspection.

The total volume of fines imposed in 2018 corresponds to the amount of fines imposed in previous years. The highest fine imposed amounted to CZK 1 million. Most frequent transgression was unduly performed customer due diligence under Section 44 of the AML Act and the most serious transgression in terms of money laundering and terrorist financing was failure to report a suspicious transaction under Section 46 of the AML Act.

The supervisory activity of the FAU also includes verifying the compliance of obliged entities' systems of internal rules with requirements imposed on them by the AML Act. Compared to 2017, the number of assessed systems of internal rules decreased. This was due to the fact that in 2017 the number of systems of internal rules sent for assessment enormously increased because of an amendment of the AML Act, according to which obliged entities had to update their internal regulation in terms of risk assessment by 30 June 2017 and send it to the FAU for review by 30 July 2017. At the end of 2018, the total number of systems evaluated was also influenced by the Czech National Bank's Decree No. 67/2018 Sb., on Selected Requirements for the System of Internal Rules, Procedures and Control Measures, as amended, effective from 1 October 2018, which the obliged entities subject to the supervision of the Czech National Bank have to implement.

# MANAGEMENT OF THE FAU

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## *The operation of the FAU is duly managed.*

The year 2018 was the second year of the independent operation of the FAU, which replaced the former Financial Analytical Unit of the Ministry of Finance on 1 January 2017. All powers and tasks of its predecessor have been transferred to the new office by law and the FAU continues to serve as a financial intelligence unit of the Czech Republic. The Act on the Budget of the Czech Republic for the first time approved own budget of the FAU in the below-mentioned breakdown.

### **Expenditures**

For the year 2018, statutory expenditures amounted to CZK 78,225 thousand, of which capital expenditures amounted to CZK 9,585 thousand and current expenditures amounted to CZK 68,640 thousand. The adjusted budget comprised total expenditures of CZK 77,375 thousand, of which capital expenditures amounted to CZK 5,950 thousand and current expenditures to CZK 71,425 thousand. After inclusion of unused expenditures in the amount of CZK 19,851 thousand, the total budget was in the amount of CZK 97,227 thousand, of which capital expenditures were in the amount of CZK 13,644 thousand and current expenditures amounted to CZK 83,583 thousand.

According to a Government Resolution, the FAU transferred the amount of CZK 850 thousand for the benefit of the Ministry of Transport.

The actual expenditure as of 31 December 2018 was CZK 66,046 thousand, of which capital expenditures were CZK 2,275 thousand, current expenditures CZK 63,771 thousand.

The FAU in cooperation with other authorities carried out acquisition of new personal computers, printers, a motor vehicle and improved employees' working conditions by increasing the comfort of the working environment. The abovementioned actions were part

of the approved programme 012V51 — Development and Renewal of Material and Technical Background of the FAU. In connection with the performance of its activity, the required information need, i.e. provision of access to external information systems, was provided to the Analytical Division. The FAU carried the major workload of evaluation by the Moneyval Committee of the Council of Europe both during the evaluators' on-site visit to the Czech Republic and at the plenary meeting in Strasbourg, which was reflected in an increase of current expenditures.

Wages and salaries of civil servants and employees constituted the major part of current expenditures. There was no termination of civil service or employment in the budgetary year 2018, with 53 ordinary employees as of 31 December 2018, of which 48 persons in civil service and 5 persons under the Labour Code. The percentage of salary utilization in 2018 is 114.1% compared to 2017. The comparison of 2018 with 2017 is influenced by a change in the systemisation that has resulted in an increase of personnel by 5 employees. In the course of the year, an analysis of vacant posts lead to a de facto reduction of the systemisation by 3 positions for 2019 by a decision of the Chapter 312 the Ministry of Finance.

Foreign business trips were carried out to the extent necessary for FAU activities and the fulfilment of international obligations stemming from membership in European and international organizations aimed at combating money laundering and terrorist financing and the application of international sanctions. In 2018, FAU employees carried out 41 foreign business trips with a total cost of CZK 531 thousand. In 2018, the frequency of business trips abroad was higher compared to the previous year due to the evaluation by Moneyval.

### **Revenues**

In terms of non-tax revenues, the FAU received a total of CZK 3,260 thousand in 2018. Of this, fines were imposed in administrative proceedings in the total amount of CZK 2,110 thousand and costs of administrative proceedings CZK 4 thousand. From Purchase Agreements, where the performance was completed with a 130-day delay, a contractual penalty of CZK 1,146 thousand was paid.

# PERSONNEL SITUATION AND SYSTEMIZATION

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## *Human resources management strategy.*

Systemization of the FAU, as an independent administrative authority, was approved in accordance with the Civil Service Act and on the basis of a decision of the State Secretary of the Ministry of Finance. The FAU is internally divided into two Divisions and one Independent Department. Specifically, it is the Analytical Division, the Legal Division and the Independent Department Office of the Director. The total systemisation of the FAU for 2018 includes 64 functional positions, of which 59 are so-called 'service post' under the Civil Service Act (with a higher share of 13<sup>th</sup> and 14<sup>th</sup> grades) and 5 positions are under the Labour Code.

The current systemization of individual organizational units have the following structure.

The FAU is led by a head of service authority in the position of director.

The Analytical Division consists of 33 working positions, it is headed by director and internally divided into two departments, Analysis I and Analysis II. Analysis I consists of 17 systemised posts, Analysis II by 15 systemised posts, a head leads each department.

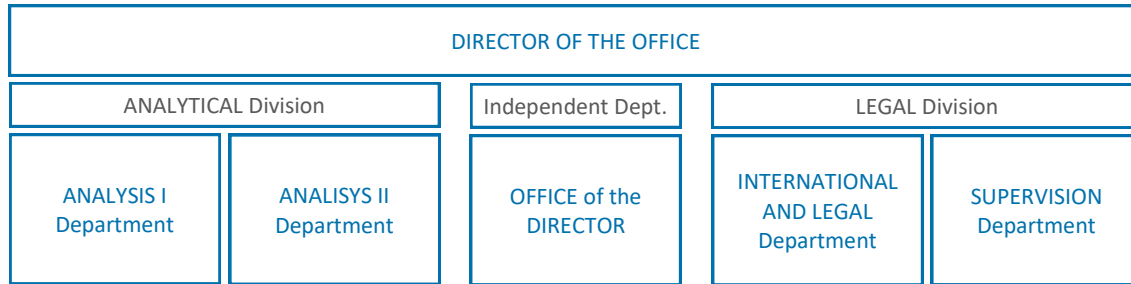
The Legal Division consists of 17 working positions, headed by director and divided into two departments, International and Legal Department and Supervision Department. Each of these departments consists of 8 systemised posts including the head of department.

Office of the Director consists of 13 working positions, of which 5 are under the Labour Code.

The Office of the Director is lead by the head of independent department.

The basic field of service for all working positions is the field no. 08 - Economic Protection of the State, but this does not exclude other fields of service at individual service posts.

The FAU is highly committed to a stable personnel situation, which contributes positively to effective management and to achieving very good results.



Organizational structure of  
the Financial Analytical Office  
as of 31 December 2018

## JOINT FORCES

### *We inform you on current events.*

The activities and significance of the FAU are becoming increasingly known to the general public. In 2018, there were frequent meetings between the FAU and professional public, consisting mainly of representatives of obliged entities, in the form of lecturers and regular consultations. The success of the fight against money laundering and terrorist financing is conditional on the joining of forces of state authorities, commercial sector and general public. Last year, the FAU regularly informed on its website [www.financnianalytickyurad.cz](http://www.financnianalytickyurad.cz) on current developments in the AML/CFT area. Up-to-date information on international sanctions was also regularly provided, as the FAU serves as the national coordinator of their implementation in the Czech Republic.

Representatives of obliged entities form the majority of 500 persons interested in automatic notifications on the latest FAU web contributions. In 2018, more than 25,000 users regularly visited FAU web presentation, compared to the first year of operation it was a 19% increase. At the same time, there were 140 thousand accesses to articles. FAU web pages are fully

responsive, allowing access to information from mobile devices. The number of visitors from mobile phones and tablets was 4% in 2018 and did not differ from 2017. Visitors were most interested in news in the area of international sanctions, legal regulations, news and FAU opinions, followed by systems of internal rules, careers and contacts. The official board recorded the lowest number of visitors. As part of its preventive work, the FAU methodically worked with obliged entities by issuing a non-public methodical publication aimed at detecting terrorist financing. In the course of the year, the FAU also published, in cooperation with the Banking portal, four expert articles on money laundering. There was also a public guide on the recognition and follow-up of online fraud. The material was created in cooperation with the European Cybercrime Centre within Europol, the European Banking Federation, the Czech Police, the Czech Banking Association within the #CyberScams Europe-wide information campaign.

# IN NUMBERS

*"Every human activity must eventually manifest itself in numbers"<sup>2)</sup>*

	2016	2017	2018
Number of received suspicious transaction reports	2,948	3,524	4,028
Total number of reports to the Police	556	539	395
Number of reports to the Police with seized funds	402	377	268
Amount of seized funds [CZK mill.]	3,836	2,146	7,546
Number of information send to the General Financial Directorate	1,419	1,647	2,230
Number of information send to the Directorate General of Customs	64	106	132
Number of foreign incoming requests	275	384	404
Number of requests send abroad	297	277	232
Number of foreign incoming spontaneous information	133	217	230
Number of outgoing spontaneous information abroad	469	800	641
Number of mystery shopping	32	26	12
Number of admin. proceedings initiated in connection with mystery shop.	4	11	4
Number of inspections under the AML Act	55	48	33
Number of assessments of systems of internal rules	42	251	92
Number of administrative proceedings for breach of the AML Act	18	16	15
Number of fines imposed for breach of the AML Act	16	14	13
Amount of fines for breach of the AML Act [CZK mill.]	2.385	2.490*	2.114
Number of notifications on transfer of funds to/from Iran	11**	-	-
Number of requests for transfer of funds to/from Iran	17**	-	-
Number of proceedings for violation of international sanctions	0	0	0
Number of imposed fines for violation of international sanctions	0	0	0
Number of proceedings on exemptions from international sanctions	8	4	4
Number of granted exemptions from international sanctions	5	4	2

\* amount for fines on the Office's income account in a given year

\*\* the measure was repealed on 15 January 2016

<sup>2)</sup> Tomáš Baťa, Czechoslovak factory owner (1876 - 1932)

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