Nigeria and South Africa Added to the FATF Grey List – Implications for International Investors

8 March 2023

On 24 February 2023, following a long evaluation, the Financial Action Task Force ("FATF") added Nigeria and South Africa to its "grey list" of countries with "*strategic deficiencies in their regimes to counter money laundering, terrorist financing, and proliferation financing*". As part of the grey listing process, the FATF increases its monitoring of grey-listed countries and works with them to address the shortcomings in their anti-money laundering and counter-terrorist financing ("AML/CTF") frameworks.

The FATF is a Paris-based intergovernmental organisation that aims to combat money laundering, terrorist financing and other financial crimes. As part of its role, the FATF evaluates countries' AML/CTF regimes and compliance with FATF standards for national efforts to counter illicit financial activity.

We discuss below the likely implications of grey listing for these two countries, steps that investors and businesses with exposure to or seeking opportunities in those jurisdictions should take at this stage, as well as what the two countries have agreed to do in order to improve their AML/CTF regimes.

What Are the Likely Consequences to Nigeria and South Africa of the Grey Listing?

The FATF's grey listing of South Africa and Nigeria—two of Africa's largest three economies—could result in significant adverse consequences for their economies and financial systems, including a reduction in foreign direct investment. These may be amplified by the fact that both countries are well integrated into the regional and global economy. Additionally, following the FATF's decision, they risk being added to the European Commission's and United Kingdom's lists of high-risk third-country jurisdictions (the "UK/European Watchlists"), which typically take into account whether or not a jurisdiction is grey listed by the FATF when deciding on its addition to the UK/European Watchlists.

The inclusion of Nigeria and South Africa on the UK/European Watchlists would make it more difficult for EU and UK entities to invest in these countries and transact with their nationals, at least in part due to heightened scrutiny of transactions by financial institutions, legal professionals and other persons with AML/CTF obligations under EU or UK regimes.

Mauritius, a key African financial hub, was grey listed by the FATF between 2020 and 2021 and was included on the UK/European Watchlists during part of that time. In fact, it took the European Union several months to remove Mauritius from its watchlist after FATF's removal. Given Mauritius's outsized role as a financial conduit of inward investment into Africa, its experience while grey listed can offer some clues as to what is likely to happen to the economies of Nigeria and South Africa. During the relevant period, Mauritius experienced:

- a significant reduction in foreign direct investment as investors from a number of jurisdictions—including the European Union and the United Kingdom—were unable to invest or dissuaded from investing as usual through Mauritius. This was particularly the case for development finance institutions and publicly owned entities;
- significant barriers to investment and reduced access to international financial services due to restrictions related to grey-listed countries imposed by financial institutions that were more stringent and conservative than legally required;
- loss of investor confidence and significant reputational damage;
- capital and investment flight as investors moved the domicile of their businesses or funds to a more AML/CTF-compliant jurisdiction;
- damage to its financial and professional services industry; and
- greater difficulty for Mauritius-based entities to access foreign financing and send/receive payments.

Other significant jurisdictions, including the Cayman Islands, Turkey and the United Arab Emirates, have recently been included in the FATF grey list though not all of them will be experiencing all of these impacts due to a number of jurisdiction-specific factors (including their wider regulatory and legal frameworks).

What Should Foreign Investors Do?

Investors and businesses that are active in South Africa and Nigeria should:

- map their level of exposure to the two jurisdictions and the operational risks arising from the deficiencies in the AML/CTF frameworks identified by the FATF (e.g., risks relating to entering into transactions with counterparties whose beneficial ownership is not clear);
- continue to monitor applicable AML/CTF requirements and, where relevant, implement robust AML/CTF compliance programs;
- continue to assess potential legal and reputational risks arising from dealing with counterparties in Nigeria and South Africa;
- map operational risks that may arise as a result of the grey listing and potential inclusion on the UK/European Watchlists, which may include delays in, or impediments to, payments, transactions and financings involving these jurisdictions;
- consider any contractual notice and other undertakings that may be triggered by the FATF's decision, for example in fund side-letters with DFIs; and
- monitor whether these two jurisdictions are added to the UK/European Watchlists.

The above actions are a helpful start in addressing concerns that may be raised by counterparties related to inclusion of these countries on the grey list. Once the practical effects of the grey listing on their businesses become clearer, affected investors and businesses may consider ways to better structure their holdings/operations to minimise disruption and mitigate risks.

Next Steps for Nigeria and South Africa

Both South Africa and Nigeria have confirmed that they are working with the FATF to improve their AML/CTF frameworks. Specifically, the two countries have committed to implement their respective action plans agreed with the FATF (the "Remedial Action Plans") by taking the measures set out in Annex 1.

Successfully implementing the Remedial Action Plans would deal with the FATF's concerns. However, given their respective scale and ambition, doing so will require significant legislative and administrative changes that may well take some time. In

Nigeria's case, the upcoming change in administration may also affect the speed of implementation. It is therefore difficult to predict how long it will take for each country to successfully implement its Remedial Actions Plan and be removed from the grey list.

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Please do not hesitate to contact us with any questions.

Annex 1 – Measures to Be Taken by Nigeria and South Africa

Nigeria	*South Africa*
Complete its residual AML/CTF risk assessment and update its national AML/CTF strategy to ensure alignment with other national strategies relevant to high-risk predicate offences.	Increase involvement in outbound Mutual Legal Assistance requests relating to AML/CTF and, when relevant confiscations of different types of assets.
Enhance formal and informal international cooperation in line with AML/CTF risks.	Improve risk-based supervision of Designated Non-Financial Businesses and Professions[1] ("DNFBPs") and demonstrate that all AML/CTF supervisors apply effective, proportionate, and effective sanctions for noncompliance.
Improve AML/CTF risk-based supervision of financial institutions and DNFBPs and enhance implementation of preventive measures for high-risk sectors.	Ensure that competent authorities have timely access to accurate and up-to-date beneficial ownership ("BO") information on legal persons and arrangements and apply sanctions for breaches of BO obligations.
Ensure that competent authorities have timely access to accurate and up-to-date BO information on legal persons and apply sanctions for breaches of BO obligations.	Demonstrate a sustained increase in law enforcement agencies' requests for financial intelligence from the Financial Intelligence Centre[2] for its AML/CTF investigations.
Demonstrate an increase in the dissemination of financial intelligence by the financial intelligence unit and its use by law enforcement agencies.	Enhance its identification, seizure and confiscation of proceeds and instrumentalities of a wider range of predicate crimes, in line with its risk profile.
Demonstrate a sustained increase in AML investigations and prosecutions in line with AML risks.	Update its Terrorist Financing Risk Assessment to inform the implementation of a comprehensive national counter financing of terrorism strategy.

[1] **Note**: These include casinos, lawyers, notaries, accountants, trust and company service providers, real estate agents and dealers in precious metals and/or stones.

[2] **Note:** This is a South African Institution that acts as the country's national centre for financial intelligence and investigations.

Nigeria	*South Africa*
Proactively detect violations of currency declaration obligations and apply appropriate sanctions and maintaining comprehensive data on frozen, seized, confiscated, and disposed assets.	Ensure the effective implementation of targeted financial sanctions and demonstrate an effective mechanism to identify individuals and entities that meet the criteria for domestic designation.
Demonstrate sustained increase in investigations and prosecutions of different types of AML/CTF activities in line with risk and enhance interagency cooperation on AML/CTF investigations.	
Conduct risk-based and targeted outreach to non-profit organisations (“NPOs”) at risk of terrorist financing abuse and implement risk-based monitoring for the subset of NPOs at risk of terrorist financing abuse without disrupting or discouraging legitimate NPO activities.	

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