

Non-Restricted Version

The Main Findings of the Money Laundering National Risk Assessment



2017

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Preamble

This document summarizes the main findings of the Money Laundering National Risk Assessment of Israel.

The risk assessment is designed to assist the public and private sectors in identifying the risks of money laundering in the country, to understand the potential risk of these phenomena to the financial system and to national security, and to become familiar with the measures taken by the state to deal with these risks. In addition, the risk assessment is meant to serve as a basis for setting policy and priorities in the field of prohibition of money laundering and terror financing, for the application of a risk-based approach and the efficient allocation of resources.

The risk assessment was conducted under the instruction of the Attorney General, during a period of two years, as part of a comprehensive process which included all relevant counterparts, and was coordinated by the Israel Money Laundering and Terror Financing Prohibition Authority (hereinafter: "IMPA"). The main counterparts who participated in the assessment are:

- a. Law Enforcement Authorities, including: the Israel National Police, the State Prosecution, the Israel Tax Authority, the Israel Securities Authority, the Forfeiture unit, the Anti-Trust Authority, the Corporations Authority, IMPA, the Anti-Drug Authority; and the Ministry of Justice.
- b. Supervisors, including: the Bank of Israel, the Israel Securities Authority, the Israel Capital Markets, Insurance and Savings Authority, the MSB Supervisor, the Postal Bank Supervisor, the Supervisor of Diamond Dealers, the Supervisor of Business Service Providers (BSPs) and IMPA.
- c. Private sector partners, including representatives of relevant financial institutions and DNFBPs (including data and sectorial risk assessments by the Israeli Bar Association, the Institute of Certified Public Accountants, Trust Service Providers, and the Diamond Exchange).

The NRA is combined of three main documents:

- (1) **National ML risk assessment** – includes an analysis of risks stemming from two different perspectives: Predicate offenses and ML typologies, methods and instrumentalities. Analysis includes data and insights produced by LEAs combined with the sectorial risk assessments of the financial system.

(2) **Financial system risk assessment** – a set of sectorial risk assessments in which the supervisors of financial institutions assessed the specific ML risks that are relevant to each sector.

(3) **National TF risk assessment** – risk assessment produced by intelligence and security agencies together with additional relevant partners, and includes an assessment of terror and terror financing risks (a non-restricted version will be published separately).

It should be mentioned, that in recent years, a range of risk assessments, including focused assessments of specific sectors or themes, and assessments at national level of issues relevant to ML/TF, were produced within inter-governmental committees. These assessments relate to risks of serious and organized crime, tax offenses, gambling, Money Service Businesses, cash, corruption, and alternative payment methods. Those risk assessments were updated and included in the ML NRA.

Methodology

ML risk assessment

The current ML risk assessment document provides an analysis of the ML risk stemming from two perspectives:

- (a) Predicate offenses.
- (b) Money laundering typologies, methods and instrumentalities.

The process was conducted through several stages:

1. **Identification** - Collection of Information: wide range of quantitative and qualitative information from various sources was identified and used. Extensive information was gathered from all relevant counterparts, including law enforcement authorities, financial supervisors and governmental databases. In addition, the private sector played an important role in the exercise, providing substantive statistical data and information on the various risks inherent to their activities, the services provided by them and certain types of customers, as well as on the scope of such risks and the control measures put in place to reduce them. The extensive information collected was classified as restricted, hence not specified in this public version document, but rather available to the relevant counterparts.
2. **Analysis** – Discussions among various authorities: the collected data was analyzed and discussed among authorities with a view to identifying threats (financial value,

likelihood), the mitigation measures (vulnerabilities, control measures) and the consequence (financial loss, social implications), characterizing them and rating them based on the weighting of the various criteria. It should be noted that the identified risks in the sectorial risk assessment (the financial system NRA) were taken into account in the ML NRA (and *vice versa*), although they may differ from each other due to specific characteristics of the assessed sector.

3. **Assessment:** systematic and uniformed analysis process was conducted, and each factor of each risk was assessed using the risk matrix, explaining the grounds for each rating. In accordance with this assessment, the final rating of each of the risks identified was weighted. Hereinafter is the risk assessment model.

Risk criteria		Low risk (1)	Medium-low risk (2)	Medium risk (3)	Medium-high risk (4)	High risk (5)
Threat	Scope and frequency	Low The scope of laundered property is low/the number of known cases related to predicate offense/typology is low	Medium-low The scope of laundered property is medium-low/the number of known cases related to predicate offense/typology is medium-low	Medium The scope of laundered property is medium/the number of known cases related to predicate offense/typology is medium	Medium-high The scope of laundered property is medium-high/the number of known cases related to predicate offense/typology is medium-high	High The scope of laundered property is high/the number of known cases related to predicate offenses/typology is high
	Likelihood to increase	Very low As far as is known, the likelihood of the use of money laundering means or property related to predicate offenses is very low	Lower than before As far as is known, the likelihood of the use of money laundering means or property related to predicate offenses is lower than before	Same as before As far as is known, the likelihood of the use of money laundering means or property related to predicate offenses is the same as before	Higher than before As far as is known, the likelihood of the use of money laundering means or property related to predicate offenses is higher than before	Very high As far as is known, the likelihood of the use of money laundering means or property related to predicate offenses is very high
Mitigation Measures	Vulnerabilities (legislation, regulation)	None There are no deficiencies in legislation or	Low level There are few deficiencies in legislation or	Medium level The level of deficiencies in legislation or	High level The level of deficiencies in legislation or	Very high level The level of deficiencies

		regulation	regulation	regulation is medium	regulation is high	in legislation or regulation is very high
	Control measures (identification, investigation, indictment, conviction)	High level Supervision and enforcement measures are sufficient for money laundering attempts to be identified, no improvements required (or only negligible improvements required)	Significant Supervision and enforcement measures provide a high likelihood that money laundering attempts will be identified, minor improvements required	Medium Supervision and enforcement measures provide a medium likelihood that money laundering attempts will be identified, moderate improvements required	Limited Supervision and enforcement measures are limited, money laundering attempts might not be identified, significant improvements required	None Difficulty identifying money laundering activity, supervision and enforcement measures are weak or non-existent, very few indications for suspected financial behavior exist, critical improvements required
Consequence	Financial loss	Minor loss Laundered amounts are very low, or no effect on the financial system or on the national economy (commerce, credit, etc.)	Medium-low loss Laundered amounts are medium-low, or the effect on the financial system or on the national economy is medium-low	Medium loss Laundered amounts are medium, or the effect on the financial system or on the national economy is medium	Medium-high loss Laundered amounts are medium-high, or the effect on the financial system or on the national economy is medium-high	High loss Laundered amounts are high, or the effect on the financial system or on the national economy is high
	Social or national implications	No effect or negligible effect Individuals outside the criminal circles are not affected or no national effect (corruption levels, international	Medium-low effect Low number of individuals outside criminal circles are effected, or national effect is medium-low	Medium effect Medium number of individuals outside criminal circles are effected, or national effect is medium	Significant effect Significant number of individuals outside criminal circles are effected, or national effect is significant	High effect The entire society or many individuals outside criminal circles are effected, or national effect is

		status, etc.)				high
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The assessment of the risk was conducted using a statistical formula, based on the ratings given to the threat and to the mitigation measures.

The formula used to rate actual risks was:

$$R=T-e*M$$

The constant R represent the actual risk; the constant T represent the level of threat, as determined by the WGs; the constant e represent the threat reduction rate (see explanation below); and the constant M represent the level of mitigation measures.

Threat reduction rate (e) was estimated in accordance with the rating of the mitigation measures, as follows:

- ✓ Where mitigation measures were rated 1-2: no reduction was made;
- ✓ Where mitigation measures were rated 3: the reduction rate was set to 10%;
- ✓ Where mitigation measures were rated 4-5: the reduction rate was set to 20%.

Materiality, Structural Elements and Contextual Factors

Following are several characteristics of the country that enable the effective mitigation of criminal activity and money laundering, and therefore influence their type and extent.

1. The primacy of the law is a fundamental principle in The State of Israel. Israel manages its public affairs in a transparent, accountable and equitable manner. Israel enjoys an independent and accessible judicial system that guarantees all citizens basic access to legal instances.

2. Israel has a strong tradition of legal and professional independence and impartiality which enables all relevant authorities (Police, State Attorney's Office, etc.) to investigate and inquire into any suspicion. These institutions have also systems for ensuring the high ethical and professional behavior of their staff, as do professionals in the private sector, such as accountants and lawyers.

3. Israel is a sophisticated, highly technological, diverse and open free market economy. Development towards a modern and open business environment in Israel has been strengthened by comprehensive deregulation across all sectors of the economy.

4. Israel is recognized as a developed market by many major indices. Israel is also known for its unique entrepreneurial and innovative spirit.

5. As evident from the World Trade Statistical Review, Israel does not appear in the lists of major exporters and importers of financial services in 2015 and 2016. This combined with the low foreign participation in the financial sector and the abovementioned statistics indicate that Israel does not serve as a global or regional financial center.

6. The Israeli government set the goal of targeting illicit proceeds as a primary objective in the combat against serious and organized criminal activity. Following government decision no. 4618 (2006), all relevant agencies are required to operate in collaboration, subordinated to program objectives and a work plan lead by the Attorney General, together with the directors of all relevant law enforcement authorities.

7. It should be noted that according to the 2017 Basel AML Index (Aug. 2017), Israel is ranked 137 out of 146 countries in the level of risk of AML, being one of the 10 countries with the lowest risk and ranked third on the list of top 10 improvers in the Index ranking. In a geographical aspect, Israel is ranked the lowest risk in the MENA region to which it is attached in the Index (and is also the lowest risk compared to countries of all regions except for the EU countries and New-Zealand). Israel has also been excluded this year from the US INCR list of jurisdictions of primary concern for AML. This is a testament to the effectiveness

of the wide array of steps and the commitment in Israel to the struggle to curb ML and its ill effects on the local as well as the global economy.

8. According to International reports, Israel is not rated as highly corrupt country. However, measures to prevent and counter domestic and foreign corruption were given high priority by all law enforcement agencies. The Government has funded and encouraged a combined and joint effort against corruption in general and corruption in public systems in particular, and has acted to minimize illegal financial activity. As part of Israel's unwavering commitment to combat corruption, it is also an active member to international conventions in the field of Anti-corruption and Bribery.

Money Laundering Risks – Predicate Offenses

(a) Tax evasion

The Income Tax Ordinance [New Version], 5721 -1961 (hereinafter: "the Ordinance" or "the Income Tax Ordinance") establishes offenses of evasion of tax payment by means of voluntary or intentional acts of a person intended to achieve the goal of reducing the tax burden on said person, or on another person whom he wishes to assist. The offenses include the specific purpose of evading tax or helping another evade tax. In the amendment to the Prohibition on Money Laundering Law, 5760- 2000, (hereinafter: the "PMLL"), those offenses were added to the list of predicate offenses.

The Land Taxation Law (Appreciation and Purchase), 5723- 1963 (hereinafter: the "Land Taxation Law") establishes a series of criminal offenses which were also added to the list of predicate offenses, mainly failure to report or making false statements about transactions in real estate.

An analysis of data from law enforcement authorities reveals that the scope of unregistered capital in Israel reaches tens of billions of NIS, and that there is a direct connection between tax offenses and money laundering offenses of extensive financial scope. However, in view of the enforcement measures implemented on the criminal level and the supplement of serious tax offenses as predicate offenses, it appears that a significant increase in the phenomenon is not expected. Overall, the **threat** posed by money laundering as a result of tax evasion is rated as **high (5)**.

The **vulnerabilities** relating to taxation in Israel derive from the fact that the tax audits are carried out only in respect to a small percentage of the taxpayers and in most cases, rely on the taxpayer's self-report. In addition, the absence of a general reporting regime to the Tax Authority makes it difficult for the Tax Authority to receive and verify all the data. However, a lifestyle that does not conform to the reported income level may serve as a basis for suspicion of tax offenses and serves as a basis for foreclosure of property seized under Section 194 of the Income Tax Ordinance. This difficulty is exacerbated by the existence of aggressive tax planning aimed at reducing the tax burden. The legitimacy and legality of these actions is often questioned and raises difficulties as to how best to deal with them. In this context, it should be noted that the Income Tax Regulations stipulate a list of tax plans that require reporting, and failure to report in the annual report on such tax planning constitutes a criminal offense, but it is not always possible to verify the data and reach all cases where aggressive tax planning that has not been reported was employed. In light of the tax system

used in Israel, whereby the tax liability is determined according to the residency test, it is difficult to enforce the tax laws on the income of Israelis outside of Israel, *inter alia*, due to the difficulty in determining residency in certain cases and the difficulty in locating Israelis living abroad, and determining the precise center of their lives. Additional vulnerability in this context is the exemption for immigrants from the obligation to report the Tax Authority the capital in their possession.

The **control measures** taken in order to reduce the scope of the serious tax offenses and the laundering of the money generated through them, include, *inter alia*, supervision and reporting to the Tax Authority on transactions in real estate, including information on beneficial owners; the use of a database to trace cases where the lifestyle is not compatible with the reported income (unexplained wealth); initiated applications to residents to submit reports (based on reviews in the Tax Authority's database); initiatives and international cooperation of the Tax Authority to locate assets of Israelis abroad, including by virtue of the FATCA and the CRS. An additional control measure was introduced with the amendment of the PMLL, which established serious tax offenses as predicate offenses, as well as a mechanism authorizing IMPA to disseminate information to the Tax Authority for the purpose of investigating tax offenses. It is noted that integrated activities are carried out by law enforcement authorities within the framework of joint investigative teams. In light of the existence of these mechanisms, the expectation is that, following the amendment of the PMLL, the ability to identify and investigate money laundering offenses arising from direct taxation offenses will be increased.

Therefore, when weighing the vulnerabilities and control measures, the rating of the **mitigation measures is moderate (3)**.

In terms of the **consequence**, the potential for money laundering in relation to proceeds generated from tax offenses is very high, as is the financial loss and the effect on society, in view of the impact on state's treasury and on the tax burden.

In summary, the incidence and financial scope of tax offenses in Israel is significant and is estimated at tens of billions. The assessment is that the likelihood of an increase in offenses in this area is low, although some control measures have not yet been implemented. In light of all the above, the risk deriving from tax evasion is rated as high (4.7).

(b) Criminal organizations

A criminal organization is a group of persons, incorporated or unincorporated, operating in the country or outside it, in an organized, systematic and ongoing format, for the commission of felonies or other offenses specified in the Combating Criminal Organizations Law, 5763–2003. Criminal organizations engage in a variety of criminal offenses, and their activities effect public order, personal security, social strength, democracy, and also cause significant financial loss to the economy. The offenses specified in the Combating Criminal Organizations Law are prescribed as predicate offenses under the PMLL. Furthermore, the criminal offenses often carried out in the course of the activity of a criminal organization, such as drug trafficking, gambling and extortion of protection, also constitute predicate offenses under the PMLL.

Organized crime extends over an extensive range of criminal activity and is carried out on a large financial scale, which also increases the likelihood of money laundering activities.

Israeli criminal organizations are active in "classic" criminal activities such as domestic and international drug trafficking, arms trafficking and use of arms, violence of all kinds, gambling, extortion, fictitious invoices, non-bank credit loans and debt collection, fraud and money laundering. In addition, there is a tendency among criminal organizations to penetrate legitimate areas such as real estate, investments in companies, and more.

In recent years, a comprehensive and extensive infrastructure of international cooperation has been established between the Israeli Police and foreign enforcement agencies to counter organized crime, enabling operational activity against criminal organizations, interception, investigation and extradition of heads of criminal organizations operating in Israel and leading to numerous arrests and indictment of heads of criminal organizations and giving a fatal strike to the criminal organization in Israel.

The year 2016 was a milestone in the combat in organized crime, in light of a complex investigation that was conducted against a known criminal organization in Israel. This investigation led to the filing of significant indictments against members of criminal organizations and against other offenders, causing serious damage to the organizational structures of prominent Israeli criminal organizations and disrupting the hierarchical order in which they existed.

With regard to future assessments, information indicates that the existence of certain financial and social conditions constitutes a risk factor for the strengthening of organized crime. The potential for international alliances between Israeli criminal organizations and their counterparts in the world will increase as a result of the globalization of organized crime and the fact that many criminal organizations recognize the advantages of international activity.

Large amounts of money are laundered through their transfer overseas and its concealment there. The funds are transferred mainly via currency service providers, front-men, real estate purchases and laundering through cash-intensive businesses. Another area in which there may be an increase in the involvement of criminal organizations is the implementation of sophisticated fraud, while committing acts of fraud against financial institutions abroad.

In light of the above, and according to this data, the **threat** of money laundering as a result of the activities of criminal organizations was rated **high (5)**.

The main **vulnerability** identified is a limited use of the Combating Criminal Organizations Law as a tool to mitigate money laundering, which may indicate a limited use of the tools provided by the legislator for the benefit of law enforcement authorities to counter organized crime.

The control measures implemented as part of the fight against organized crime include the establishment of dedicated task forces to combat criminal organizations and their money launderers and effective enforcement activities for the identification, investigation and prosecution of money laundering offenses committed under their activities. Some of the cases resulted in convictions and prison sentences, as well as seizures in large amounts. The weighting of the data demonstrates that the vulnerabilities with respect to the activities of criminal organizations are not significant, as the measures targeted by law enforcement authorities bear fruit, and that the consistent and uncompromising treatment of the phenomenon of money laundering within criminal organizations leads to effective results. Therefore, the **mitigation measures** were rated **moderate-high (4)**.

Consequence – organized crime has significant implications on the Israeli economy, the financial system, the level of crime and personal security in Israel.

In conclusion, despite the enforcement activity taken and despite the severe damage to the infrastructure of the criminal organizations in Israel, the threat they pose is still significant. In view of the trend of the relocation of these organizations' activity abroad, their involvement in international drug trafficking and sophisticated international fraud is expected to increase. In light of the above, the risk of money laundering as a result of the activity of criminal organizations is rated moderate-high (4.2).

(c) Fictitious invoices

The offense of issuing fictitious tax invoices is specified in the Value Added Tax Law, 5735 - 1975 (hereinafter: the "VAT Law").

An analysis of the data provided by the various law enforcement authorities revealed that this phenomenon is widespread and has a very large financial scope, which is estimated at several billion NIS a year, and therefore the **threat** posed by this offense is rated as **high (5)**.

The **vulnerabilities** identified include the fact that it is easy to issue fictitious tax invoices (in part due to the absence of restrictions regarding format on tax invoices), which reduces the ability to monitor the amount of tax invoices issued; and the ease of setting up front ("straw") companies or taking control of companies, so that a seller of fictitious tax invoices can fraudulently identify himself as the owner of a company and issue fictitious tax invoices on its behalf.

Control measures are taken by the Tax Authority's Investigations Division, which handles the investigation of the phenomenon of the distribution and offsetting of fictitious tax invoices and, when necessary, cooperates with other law enforcement authorities. At the same time, civil auditing and assessment procedures are carried out, in addition to the regular assessment procedure, based on reinstatement of the state previous to the illegal offset of a tax invoice received unlawfully. In addition, starting in 2010, the Tax Authority requires some of the businesses to submit a monthly report online to the VAT Authority. The report includes a breakdown of all tax invoices issued by the taxpayer and enables the Tax Authority to conduct complex analysis and identify the activity of issuing fictitious invoices. In addition, the Tax Authority carries out prevention and thwarts activities in order to identify entities suspected of distributing fictitious invoices. Another control measure is the amendment to the PMLL, which established tax offenses as predicate offenses, and also regulated a mechanism for dissemination of information from the IMPA to the Tax Authority for the purpose of investigating such offenses. It will be further noted that in light of the frequency of this offense, over the past years many resources were allocated to cope with this phenomenon, including joint activities of law enforcement authorities leading to investigations and indictments.

In view of the above, it appears that there is an ability to identify, investigate and prosecute money laundering offenses through use of fictitious invoices. In addition, the establishment of serious tax offenses as predicate offenses under the law, and the development of a mechanism for dissemination of information between authorities, is expected to increase the ability to counter financial crime. Accordingly, the rating of the **mitigation measures is moderate-high (4)**.

The **consequence** of the phenomenon of the distribution and use of fictitious tax invoices is widespread and may lead to losses of billions of NIS a year and negatively affect the financial system. A review of the case law dealing with these offenses demonstrates that this

phenomenon may constitute large-scale tax fraud, and as a result, may cause a substantial financial loss to the state's treasury.

In conclusion, given the frequency and financial scope of these offenses, on the one hand, and the ability of the authorities to mitigate it, on the other hand, as well as their financial and social implications, the risk of money laundering as a result of fictitious invoices was rated as moderate–high (4.2).

(d) Drug trafficking

The Dangerous Drugs Ordinance prescribes a series of offenses involving the use and trafficking of drugs, including export, import, trade and supply offenses, brokering and transport at border crossings. The Israel Anti-Drug and Alcohol Authority, which assesses the value of the drug market in Israel, have estimated the market's value in recent years at more than 4 billion NIS. The law enforcement agencies note a number of ways of smuggling drugs through Israel's borders, mainly through the borders with Egypt and Jordan, when drug seizures at the Ben-Gurion Airport indicate the use of couriers and mail packages. In addition, intelligence assessments for 2017 point to a growing transition in drug trafficking via the Internet.

Given the wide scope of the phenomenon and the wide variety of ways in which money can be laundered by drug trafficking, from assimilation in the financial system to the purchase of real estate, the **threat** of money laundering stemming from drug trafficking offenses has been classified as **moderate-high (4)**.

The **vulnerabilities** in the context of drug trafficking include the relative ease with which capital can be generated from drug-smuggling across land borders, as well as online trade, which also creates enforcement challenges.

The **control measures** include a comprehensive normative framework in the Dangerous Drugs Ordinance, which establishes a significant level of punishment for drug trafficking offenses (which are also predicate offenses), and providing extensive enforcement powers including confiscation in accordance to a "drug dealer criminal lifestyle" presumption. In addition, integrated activity of law enforcement authorities is being carried out to mitigate proceeds of drug offenses, which enables effective and efficient enforcement, including identification and investigation by competent authorities, filing indictments and forfeiture of property. There are also international collaborations to mitigate the global phenomena of drug trafficking and laundering of its proceeds.

In view of the above, the rating of the **mitigation measures is moderate (3)**.

In terms of the **consequence**, since the extent of money laundering compared to the money derived from drug trafficking offenses is very high, the potential for financial loss is significant, as is the impact on society.

In conclusion, this is an offense that is estimated in billions and its prevalence is high. The methods of trade become more advanced and difficult to locate, so it is estimated that these channels are increasing. However, in recent years there has been a significant increase in the scope of seizures by the police, which indicates the effectiveness of the control measures, and the data indicates that attempts to launder property originating from drug offenses are indeed identified and treated as required. In view of the above, the risk of money laundering as a result of drug offenses is moderate-high (3.7).

(e) Gambling

Organizing gambling is illegal in Israel. The Penal Law prohibits the organization or participation in prohibited games, lotteries and gambling, which may win the participants money, money equivalents or a benefit based on results dependent on fate or guesswork rather than on understanding or ability. Despite the legal prohibition, there is a phenomenon of illegal gambling in Israel. In addition, the data collected from law enforcement authorities indicates an activity of prominent criminals and criminal organizations in the operation of casinos in various countries abroad. These findings indicate a criminal base of operations that is exploited for wider criminal operations. Thus, according to the estimates of law enforcement authorities, the operation of illegal gambling businesses is a platform for the exploitation of gamblers for purposes of courier activity and capital smuggling. Furthermore, criminals engaged in this field perpetrate tax offenses on a substantial scale, including tax evasion in countries where the casinos operate, money laundering by reporting proceed as gambling profits and failure to report income smuggled into Israel in various ways. The gambling industry is a significant source of income for criminal organizations, since the scope of income in this field is estimated in billions of NIS. This data undoubtedly increases the motivation of criminals to continue operating in the field.

The most prominent trends in the gambling market in Israel include the misuse of apartments, commercial real estate and businesses for the purpose of gambling, usually through the extortion of protection fees by criminal organizations, online gambling, and sending criminals to carry out gambling business abroad.

Given the financial scope of the illegal gambling market in Israel estimated at billions and the development of new gambling channels, it seems likely that the phenomenon will increase. In light of the weighting of this data, the **threat** rating in this area is **moderate-high (4)**.

The **vulnerabilities** identified include the transition to online gambling using alternative and advanced means of payment for the transfer of funds. It should be noted that this sector is expected to undergo comprehensive regulation, including licensing, supervision and imposition of the money laundering prohibition regime on those engaged in the provision of services through these means of payment. This regulation, which is in various stages of legislation (there is different regulation regarding various means of payment), is also expected to affect the possibility of making use of these means of payment for illegal gambling activities.

Other vulnerability is the absence of sufficient enforcement measures against gambling site operators. The law restricting the use of the premises to prevent the commission of offenses does not include reference to gambling sites on the internet, and the effect of enforcement activity against online gambling sites is relatively limited due to the minor impact on the operators of the sites and the absence of comprehensive systemic treatment in the field. Part of the difficulty lies in the ability to place servers used for illegal online gambling activity in foreign countries where gambling activity is legal. Thus, it is difficult to investigate these offenses, while the funds generated from them are transferred to Israel under the guise of gambling payments. In this context, it should be noted that according to case laws, a company that operates a gambling site that is directed at the Israeli public violates the provisions of the law even if it is registered in a country where gambling is permitted and its internet server is outside the borders of Israel. However, conducting criminal proceedings against site operators and obtaining sufficient evidence to prove the extent of the offense require the investment of many resources, including the need for skilled investigators who are familiar with the computer world and in handling requests for legal investigations that usually take a long time.

The **control measures** include a designated task force to combat this phenomenon, which led to investigations that resulted in indictments, convictions, and prison sentences, as well as the forfeiture of large sums; monitoring of gambling activity through the monitoring of financial institutions' reports to IMPA according to their obligations under the PMLL; publishing a list of account numbers belonging to illegal gambling sites; and publications of typologies and red flags by IMPA.

In light of the above, the **mitigation measures** are rated as **moderate (3)**.

In examining the **consequence** of the gambling offense, it is possible to point to the

significant financial loss in view of the extent of the laundered proceeds, as well as significant social impact.

In conclusion, the amounts laundered through gambling offenses are extensive and crime in the field is also expected to increase due to the accelerated development of the online gambling market and the advanced means of payment. The control measures and enforcement efforts only partially mitigates the risk, while the consequence of this phenomenon is significant. Therefore, the risk was rated as moderate-high (3.7).

(f) Fraud offenses

Fraud offenses, which are set forth in Article 6 of Chapter Eleven of Part Two of the Penal Law, are predicate offenses under the PMLL. Crime trends in the field of "classic" fraud and deception include retroactive payment fraud; phishing and identity theft; forgery of money, documents and certificates; defrauding foreigners; fraud and deception against the state (support funds); fraud and deception in the field of intellectual property. As for online fraud, criminal activity includes fraud by trading in binary options.

Law enforcement authorities indicate that the extent of fraud and deception in Israel is significant. In 2016, the financial scope of the phenomenon reached more than NIS 1 billion. In addition, the development of new forms of fraud, and the use of technological and online means to commit the offenses, increases the likelihood that the scope of their performance will increase. The weighting of these factors led to a rating of the **threat** of money laundering resulting from fraud and deception as **moderate-high (4)**.

One of the **vulnerabilities** revolves around "classic" fraud and deception offenses, which are carried out in relatively low sums of money, and therefore are usually handled by the police prosecution units that investigate the fraud offenses, and most cases resolve in compensation of the victims. In major fraud cases, the Police's national unit will conduct the investigation, and money laundering offenses will be pursued.

Other vulnerability relates to trade platforms managed in Israel, but intended only for overseas customers, and therefore not subject to regulation under the Securities Law, 5728-1968. This fact resulted in cases, particularly in connection with the marketing of binary options, where this activity served as convenient grounds for fraudulent activity. This concern was supported by an increase in the number of requests from abroad to law enforcement authorities in Israel regarding the involvement of Israelis in investor fraud abroad. This phenomenon has led to significant damage to Israel's reputation in general and to the capital

market in Israel in particular. It should be noted that a government bill recently submitted to the Knesset for approval demands the complete prohibition of trading in binary options.

The **control measures** employed by law enforcement authorities include, *inter alia*, police activity focused on the handling and investigation of fraud and deception offenses, in particular offenses committed by sophisticated means requiring special expertise and fraud offenses committed outside the country, as well as various actions of the Tax Authority, including the enforcement of civilian tax laws on criminals.

Another control measure is the adoption of various technological means to prevent identity theft, including the Inclusion of Biometric Means of Identification and Biometric Identification Data in Identity Documents and in a Database Law, 5770-2009, whereby identification documents containing an electronic chip will be issued to residents of the State of Israel that will allow the verification of the identity of their holders using biometric information that will also be kept in a central database. In addition, for the protection of credit information, the Bank of Israel ordered the issuance of debit cards with a uniform and secure format for payment transactions with a charge card containing a chip.

Another measure is regulation, including the application of the regime of the Prohibition on Money Laundering and Terror Financing Law to trade platforms.

In view of the aforesaid, the rating of the **mitigation measures** is **moderate (3)**.

The **consequence** involved in this risk includes insignificant social impact, since in most cases the victim of the fraud is an individual or a certain number of individuals; but with respect to social engineering fraud or binary options fraud, there is a significant financial loss and impact on the country's reputation and its international standing.

In conclusion, fraud offenses are very common and generate significant proceeds of crime, with the financial scope of the classic fraud offenses estimated at billions and the extent of the more sophisticated fraud offenses even higher. These offenses become more lucrative, accessible and easier to operate because of the use of online platforms and web tools that extend and simplify classic fraud patterns. In addition, it appears that there is a probability of an increase in the scope of these offenses, and there is ongoing development of new fraud methods. In light of these findings, the risk of money laundering resulting from fraud offenses is rated as moderate-high (3.7).

(g) Bribery and corruption

The Penal Law establishes a broad criminal prohibition in connection with offenses of

bribery, receipt of bribes, and bribery of foreign public officials. Bribery offenses are included in the list of predicate offenses in the PMLL. The broad definition given to this offense within the framework of the law creates a criminal network designed to capture all the behaviors and patterns of action whose purpose is to improperly influence the integrity of public administration.

The Government has funded and encouraged a combined and joint effort against corruption, although the assessed financial scope of bribery is not significant (compared to other predicate offenses), but the financial and social consequence is significant. Appropriate measures to prevent and combat domestic and foreign corruption were given high priority by all authorities. A strong tradition of professional independence and impartiality enables all relevant authorities to investigate and inquire into any suspicion.

Various international publications indicate that there has been a significant improvement in the level of enforcement of criminal prohibitions on bribery and public corruption. Thus, the United Nations Convention against Corruption report recently noted that Israel is implementing a wide array of legislation designed to deal with the scourge of corruption, including primary legislation, state attorney's directives, and various arrangements concerning forfeiture of assets. It was also noted that Israel's enforcement authorities have implemented a "zero-tolerance" policy in relation to offenses of government corruption, which led to the prosecution of a number of senior public figures in Israel.

The phenomenon of corruption in municipal councils was also examined by various authorities, including the State Comptroller, as well as in a report recently published by the an Inter-ministerial Committee convened to review possibilities to strengthen the rule of law and integrity in municipal councils. Despite the existence of corruption in municipal councils, its precise scopes have yet to be determined. Law enforcement authorities estimate that the value of money received as part of bribery offenses are not significantly higher than other predicate offenses, but they are usually laundered in sophisticated ways that make it difficult to locate the offense and to forfeit its proceeds. Law enforcement authorities further estimated that the scope of this phenomenon is not expected to increase and that in light of the increased enforcement in this area, the likelihood is that this phenomenon will gradually decrease. In view of the prevalence and lack of precise information about its extent, the **threat** posed by bribery and corruption was rated as **moderate-high (4)**.

The **vulnerabilities** include the fact that AML/CFT orders that apply to financial institutions do not all include a definition of a domestic politically exposed person (PEP), and therefore financial institutions are not obliged to examine whether there is a high risk in performing financial activity for a domestic PEP, with all that entails.

Another point that needs to be examined is how to implement the obligation of certain PEPs to submit a capital declaration. The examination of declarations in Israel is carried out in a technical manner and lacks a thorough and substantial examination of the differences between the various declarations submitted over the years, the reasonableness of the declaration, and cross-checking with other information, such as the Tax Authority's databases.

The **control measures** include police's use of sophisticated intelligence and research methods, combining forces with all law enforcement authorities, including the Tax Authority, the Antitrust Authority, IMPA, and others. In recent years, the National Fraud Investigation Unit in the Israeli Police has undergone a structural change that has led to an increase in the number of cases handled by it. The National Unit for Countering Financial Crime has been mitigating corruption in governmental companies, and a dedicated task force was established in the police, focusing on the criminal interface between corruption and criminal organizations or prominent criminals.

Another control measure is the obligation of senior public officials, including ministers, deputy ministers, Knesset members, mayors and their deputies, to submit a capital declaration. Under the Public Service Law (Capital Declaration), 5767-2016, the scope of public employees obligated to submit a capital declaration is expanded and includes all the public figures listed in the First Schedule of this law, including policemen with the rank of superintendent or higher; a prison guard with the rank of deputy warden or above; an officer with the rank of colonel and up and other senior officers, and a number of local authority employees.

Additional control measures include the Israeli legal system characterized by independence and self-sufficiency. The public corruption cases heard in recent years in which senior public figures were charged and convicted testify to a strong desire to eradicate the phenomenon and to denounce it.

Financial institutions also demonstrate a good ability to identify unusual activity connected to PEPs, a factor that provides a substantial control measure.

A review of the data relating to investigations, prosecutions and convictions of public figures reveals that both the legal framework and the enforcement of corruption and bribery by law enforcement authorities are significant and comprehensive. In view of the above, the overall rating given to the **mitigation measures** is **moderate-high (4)**.

Consequence - government corruption is an unacceptable phenomenon adversely affecting the public's trust in the authorities and may even cause significant financial and social loss, in light of the impact on growth, economic efficiency and equality.

In conclusion, although the exact scope of bribery offenses is unknown and given that Israel is not a highly-corrupt country, the assessments indicate its existence, especially among municipal councils. The information presented above, including the number of investigations and files opened against public figures for these offenses, also constitute an indication of the extent of the phenomenon and its presence at the highest levels, but also reflects the fact that Israel combats corruption aggressively. Law enforcement authorities estimated that in light of the significant enforcement efforts in this area, the likelihood of its increase is low. In view of the above, the risk of money laundering as a result of bribery and corruption offenses was rated moderate (3.2).

(h) Pandering and human trafficking

The Penal Law includes several offenses related to prostitution and obscenity, some of which constitute predicate offenses under the PMLL. These offenses include, for example, offenses of pandering acts of prostitution; bringing a person to an act of prostitution or to engage in prostitution; exploitation of minors for prostitution; and holding a place for prostitution. Other relevant offenses in the Penal Law, which are predicate offenses in the PMLL, are kidnapping for purposes of prostitution; the holding of a person under conditions of slavery for purposes of work or services, including sexual services; motivating a person to leave his country in order to engage in prostitution; and human trafficking.

According to the findings of the assessment, the volume of prostitution in Israel is approximately NIS 1.3 billion. The information provided by law enforcement authorities demonstrate that the phenomenon of trafficking in women for prostitution has decreased considerably in recent years and today Israel is no longer a target country for trafficking in prostitution. As for human trafficking, the data also points to a significant downward trend, as evidenced by the US State Department's 2016 report, in which Israel is considered to hold the highest level of effectiveness in preventing human trafficking. The data also points to the ability to identify and enforce these offenses, but at the same time raise a problematic picture of the level of punishment. Moreover, and despite the determined struggle against trafficking in women for prostitution, the phenomenon of pandering for prostitution in itself remains widespread and has considerable financial scope. Therefore, the **threat** posed by offenses of pandering and bringing a person to an act of prostitution is rated as **moderate (3)**.

Vulnerabilities – in some cases, it is difficult to prosecute trafficking offenses, in light of the fact that the victims prefer to return to their origin countries and not to remain within the State of Israel for the purpose of assisting in criminal cases and giving testimony in court.

Control measures – offenses of pandering and human trafficking for the purpose of prostitution are identified and enforced. Law enforcement authorities also point to the existence of extensive activity to reduce the scope of activity in brothels and to track advertisers of paid sex advertisements. However, as can be seen in the information reviewed, the patterns of operation in human trafficking for purposes of prostitution are constantly changing, which requires constant vigilance and monitoring by the authorities. In light of the above, the rating given to the **mitigation measures** is **moderate-high (4)**.

Consequence – the phenomenon of pandering and human trafficking has significant negative consequences, mainly in the social aspect, and in the international aspects.

In conclusion, the risk posed by these offenses is in a continuous downward trend. Although the scope and frequency of the phenomenon are not negligible, the control measures are comprehensive and effective. Therefore, in the weighting of the data, the risk of money laundering stemming from pandering and human trafficking was rated as moderate-low (2.2).

(i) Securities offenses

The offenses regarding the use of insider information by an insider, the use of insider information originating from an insider, and offenses of fraud in connection with securities pursuant to Sections 52c, 52d and 54 (respectively) of the Securities Law, 5728-1968 (hereinafter: "the Securities Law"), are predicate offenses under the PMLL, 5760-2000.

The capital market constitutes a major part of the financial system and is of central importance to all financial activity in the economy. The capital market is characterized by its being a global, open and competitive market. Trading in the capital market is electronic, fast and anonymous, and is characterized by significant volume and innovation in the products and services offered to investors. These characteristics may increase concern of exploitation of the capital market for the execution of unlawful transactions, as well as its exposure to money laundering offenses.

In light of the fact that the Israeli capital market is part of the global capital market, there is concern that foreign "black" capital may enter the Israeli financial system and inject domestic "black" capital into foreign markets around the world. In order to reduce the scope of the aforesaid concern, and in order to deter potential offenders, the Securities Authority employs advanced systems used to monitor trading in securities and to expose activities that appear to be irregular. Enforcement in the field of securities helps maintain the credibility of the capital

market and contributes to the ability of the reasonable investor to make informed decisions, based on all the relevant information for assessing the chances and risks of the investment.

Despite the large volume of trading in securities, the volume of criminal activity out of the total trading activity in the capital market is limited. This is due, *inter alia*, to the various control measures used by the Securities Authority, including the fact that the main players in the capital market (consultants and investment portfolio managers, marketers, stock exchange members, etc.) are supervised by the Israel Securities Authority; the existence of effective monitoring and control measures aimed at exposing activity that appears to be unusual; and to the execution of extensive and advanced intelligence activity, which is also intended to expose criminal activity. The data collected also indicate that the enforcement actions, and in particular requests for the freezing of property for purposes of forfeiture, do contribute to the deterrence of potential offenders. In view of the above, the **threat** to money laundering derived from securities transactions was rated as **moderate (3)**.

There are **vulnerabilities** in the legal framework related to the prevention of money laundering arising from securities offenses, including the absence of a legal mechanism for the transfer of information directly between IMPA and the Securities Authority; as well as the fact that the seizure arrangements in the Securities Law does not allow value seizure.

Control measures – trading in securities is regulated through reports of public companies to the Securities Authority and through computerized systems. There is extensive regulation in the field, as well as extensive and effective enforcement, both in the criminal and administrative spheres. The phenomenon of money laundering through securities trading is investigated and prosecuted and significant sanctions apply.

In light of the above, the rating given to the **mitigation measures** is **moderate-high (4)**.

Consequence – securities offenses have significant financial implications on the Israeli capital market and on the stability of Israel's financial system.

In conclusion, in light of the fact that the scope of criminal activity within the capital market is limited, and in light of the existence of effective enforcement activity despite the minor deficiencies within the legal framework, the risk was rated as a moderate-low (2.2).

(j) Property offenses

The "classic" patterns of activity in property offenses include, *inter alia*, theft of vehicles; breaking into apartments, businesses and warehouses; damage to infrastructure; and

agricultural crime. In recent years, there has been a worldwide decline in this type of crime, mainly due to the migration of criminal organizations to other, more sophisticated crime areas such as fraud and technological crime.

The review of the data demonstrates that the threat posed to Israel in the area of money laundering stemming from property offenses is not high. Despite the fact that property offenses are widespread and encompass a wide range of criminal activities, the trend of gradual decline, as well as the low amounts that characterize such offenses, lead to the **threat** rating as **moderate – low (2)**.

With regard to the **control measures**, it should be noted that most of property offenses constitute predicate offenses under the PMLL. The data relating to investigations, prosecution and convictions of such offenses, including the constant decline in the number of cases opened on these matters, indicates the effectiveness of enforcement measures. In light of the above, the overall rating given to the **mitigation measures** with respect to property offenses is **moderate (3)**.

Consequence – property delinquency has no significant financial consequences, but there is social impact, especially because of the implication on personal security.

In conclusion, for the purpose of rating the risk posed by property offenses, the scope of property delinquency which is in a gradual downward trend was considered, as was the fact that the profit potential from these offenses compared to other predicate offenses is relatively low. The legal framework was also examined with regard to property offenses, which also leads to effective results in the field of prosecution and punishment for these offenses in Israel. In view of the above, the risk of money laundering as a result of property offenses was rated as moderate - low (1.7).

Money Laundering Risks - Typologies, Methods and Instrumentalities

(a) Money service businesses

Money Service Businesses (hereinafter: "MSBs") are financial institutions that provide a wide range of financial services, from currency exchange and international wire transfers up to the provision of more complex financial services, including discounting checks, factoring, and the credit services. MSBs have significant social and financial importance. They compete with banking corporations and provide services to populations that, for various reasons, are not adequately addressed by the banking sector. However, in addition to its contribution and importance, this is a sector in which there is a significant risk of misuse for money laundering.

The information provided by law enforcement authorities indicates that registered and unregistered MSBs are involved in activity that serves as an infrastructure for money laundering. This activity may include "gray market" loans and, in extreme cases, collection using violence, extortion and the takeover of businesses. Some MSBs' services are used to launder gambling money and fraud money, as well as for the transfer of capital generated in crime into Israel and abroad.

The extent of the financial activity of the MSBs is estimated at NIS 150 billion per year, and in view of this significant scope of activity and in view of the market characteristics as detailed, it appears that the sector is particularly vulnerable to delinquent activity and money laundering. In view of the above, the **threat** posed by the MSBs was rated as **high (5)**.

Vulnerabilities – until the enactment of the Financial Services Supervision Law, there were many vulnerabilities that enabled money laundering through MSBs, including partial regulation under the PMLL that included inadequate threshold requirements that did not prevent criminals from entering the industry, at times, by use of front-men; the absence of supervision over the activity of granting non-bank credit; the lack of enforcement activity in order to assess the scope of activities of unregistered MSBs, and to take appropriate measures, including prosecution; and negligible and non-detering regulatory oversight activity. Some of these vulnerabilities have been comprehensively addressed under the Financial Services Supervision Law.

Control measures – the regulation in the field of MSBs has undergone a significant but comprehensive change recently, with the enactment of the Regulated Financial Services Supervision Law. The law is intended to authorize a new financial regulator that will

supervise MSBs and regulate the entire field of financial services and non-banking credit services, with the objective of creating an appropriate and accessible alternative, which will provide competition for the banking sector and will help prevent the entry of criminals into this sector. The law expands the definition of a service provider in a financial asset and applies it to transactions that thus far have not been regulated, such as activity with prepaid cards and virtual currencies. In addition, the law distinguishes between a service providers in a financial asset and credit service providers and extends the application of regulation also to entities engaged in the provision of non-bank loans. The PMLL was also amended so that the obligations under it will also apply to all the entities supervised by the new law.

Another bill aimed at significantly reducing the risk inherent in the activity of MSBs is the bill to reduce the use of cash, in which significant restrictions on trading cheques were imposed. The bill has passed the first reading and is on the agenda of the Knesset Constitution, Law and Justice Committee.

Furthermore, the phenomenon of misuse of MSBs for money laundering activity is identified and investigated by law enforcement authorities, among others, within the framework of task forces. This, together with the overall regulation in the area, leads the rating of the **mitigation measures to moderate (3)**.

Consequence – currency service providers serve as an important alternative to the traditional financial system. At the same time, there is a phenomenon of misuse of MSBs for criminal purposes, including the commission of tax offenses and money laundering, which has a negative impact both from a financial and a social aspect. In addition, it impairs the ability of MSBs to provide a suitable alternative to a banking system that enables to protect its customers.

In conclusion, in view of the scope of financial activity in this area, as well as the possibility of its exploitation for criminal purposes on the one hand, and the fact that despite of the significant improvement in regulation, the current situation still allows the use of MSBs for money laundering, the overall risk of money laundering through MSBs was rated high (4.7).

(b) The use of cash

The use of cash, especially in transactions of significant scope, is a prevalent pattern of activity among criminals and characterizes many predicate offenses, since its use is anonymous and easy to conceal and assimilate as part of legitimate financial activity.

The use of cash in the Israeli economy was discussed at length in the deliberations of the inter-ministerial committee to examine the reduction of the use of cash, which was expressed in the proposed bill for the reduction of use of cash currently before the Knesset.

The phenomenon of money laundering through the use of cash is widespread, but there are no statistical metrics and data about its exact scope. Most of the use of cash is done under the perpetrating of predicate offenses in the field of drugs, gambling and fraud. Another phenomenon of money laundering through the use of cash has been identified among illegal migrants who wish to transfer money to their countries of origin.

An examination of the threat posed by the use of cash indicates that this is a widespread and available pattern of action that characterizes many predicate offenses. In view of the above, the **threat** of money laundering posed by the use of cash is rated as **high (5)**.

Vulnerabilities – The absence of a comprehensive arrangement of means of payment in the economy that may constitute an alternative to cash use. In this context, the bill to reduce the use of cash should be noted, as well as the final report published by the Committee for the Promotion of the Use of Advanced Payment Methods, which has not yet been drafted into a proposed bill.

The **control measures** in this area include the AML/CFT orders that impose reporting obligations on financial institutions regarding the performance of cash-based transactions carried out by their customers. In addition, the use of cash is identified and investigated by law enforcement authorities in all money laundering cases, including in cases involving cash-intensive businesses. In addition, a recent court ruling views the use of cash as evidence of the existence of intent to disguise the source of the funds. In weighing this data, the **mitigation measures** were rated as **moderate (3)**.

Consequence – the use of cash for criminal purposes generates significant financial loss in light of its extensive use in the Israeli economy.

In conclusion, the use of cash in characterizes many predicate offenses and embodies a significant risk of money laundering. The main vulnerability in this area lies in the absence of a comprehensive legislative arrangement to reduce the use of cash. The control measures for monitoring the use of cash are, among other things, the obligation applies to financial institutions to report cash related currency transaction reports to IMPA. In view of the extensive use of cash in the Israeli economy and the use of this pattern of activity for the purposes of money laundering, it seems that the existing control measures do not provide sufficient response. Thus, the risk of money laundering through the use of case was rated high (4.7).

(c) International crime

The level of laundering in Israel by individuals living abroad or by organised crime groups operating from outside Israel is difficult to quantify. Authorities consider the financial institutions to be vulnerable to international money laundering from individuals and transnational groups from the USA, Europe and the countries of the former-Soviet Union. The authorities are equally conscious of the potential risks of illicit assets entering the Israeli financial system as an inadvertent result of open immigration policies.

Information gathered in recent years indicates the involvement of Israeli criminals in large scale acts of fraud abroad, with the resulting estimated financial loss of billions of Euros. Among the fraud offenses are binary options fraud and social engineering fraud. The information indicates on cross-border money laundering, both with regard to domestic proceeds laundered abroad, and with regard to foreign proceeds laundered in Israel. In light of the above, the **threat** of money laundering as a result of international crime was classified as **moderate – high (4)**.

Vulnerabilities – As a common law jurisdiction, there are inherent challenges in proving foreign predicate offenses as the court cannot rely on the evidence collected in an investigation conducted abroad. The court may permit the submission of the minutes of testimony given abroad as evidence in a trial only where sufficient evidence has been presented to justify the absence of the witness and it has been proven that the defendant or his attorney was given a proper opportunity to question the witness.

In addition, there are minor shortcomings in the confiscation mechanism in the Mutual Legal Assistance Law. Another problematic aspect in the context of property confiscation stems from the fact that interrogation procedures involving international components are slow and protracted. One of the consequences of the protracted proceedings is the release of property seized in Israel due to the time schedule established in the legislation for the temporary seizure and forfeiture of property.

The information provided by law enforcement authorities further indicates that although the criminal activity is carried out from Israel, it is not always carried out against Israeli victims, and therefore complaints are not necessarily filed with the police. Therefore, the intelligence information received does not match the number of requests for legal assistance from various countries, which highlights the gaps in information regarding the extent of the phenomenon and those involved in it.

With regard to the **control measures**, mention should be made of the effective legal framework in Israel enabling legal assistance and extradition. In addition, the obligation to report cross border money transfers, as well as the reporting obligations imposed on the financial institutions in connection with cross-border activity, also reduces the threat of money laundering from the international perspective.

The threat of money laundering generated by international crime is identified by law enforcement authorities that investigate and prosecute those cases in cooperation with foreign counterparts. In appropriate cases, and in order to overcome the abovementioned shortcoming, domestic investigations are being conducted. Consequently, the **mitigation measures** were rated as **moderate-high (4)**.

Consequence – transnational crime has a negative impact on the stability of the financial system and has the potential to cause significant financial. In addition, this phenomenon has implications for Israel's international standing.

In conclusion, the scope of Israeli criminal activity in foreign countries is wide and includes a variety of common money laundering patterns. The vulnerabilities identified include limitations on the use of investigative materials from an investigation conducted abroad, and more. The control measures include a legislative framework enabling legal assistance and extradition, the FIs' wire transfer reporting obligation, and the robust and frequent practice of international cooperation with other law enforcements authorities in ML investigations. In light of the above, the risk of money laundering through international crime was rated as moderate-high (3.7).

(d) Diamond trading

Diamond trading serves as an important trading sector in the Israeli economy and Israel is a prominent diamond trading centers. The diamond industry has a longstanding tradition and is an important part of the development of Israeli exports.

At the same time, the unique characteristics of the diamond trade industry make it, across the globe, to be a high-risk instrument for money laundering offenses. International typologies indicate that diamonds transactions can often be conducted anonymously, with a handshake and minimal documentation, making it difficult to track the money route. The physical characteristics of diamonds, their small size, the difficulty in locating them, and the ease with which significant sums can be transferred through the movement of diamonds are all a convenient platform for money laundering. In addition, diamonds are often considered to be

used as a substitute for other means of payment because of the difficulty of valuing them objectively and definitively.

The diamond trade industry is supervised by the Diamond, Gems and Jewelry Director at the Ministry of the Economy (hereinafter: the "Diamond Director"). The Diamond Director is responsible for issuing licenses to diamond dealers and operates a customs duty station for the import and export of diamonds. This station is the only entity in the country authorized to release diamonds as export import shipments, and is responsible for the statistical records of trade in the industry.

The Israel Diamond Exchange Ltd. is a private company whose members engage in the trade, production, marketing, purchase, brokerage, import and export of diamonds. Despite the decline in the scope of its activity in recent years, the Israeli Exchange is still among the prominent diamond exchanges in the world. The Exchange manages internal judicial and penal institutions that are operated in the event of deviation from the rules of conduct and the accepted commercial norms in the sector, and it has also adopted self-regulation for the purpose of preventing trade in blood diamonds (the "Kimberley Process"). The Exchange assists its members, through its institutions, in finding solutions and settling business disputes through the Arbitration Tribunal.

The phenomenon of money laundering through diamond trading is identified and investigated by the enforcement authorities. The information gathered indicates the involvement of other "players" in the diamond industry, including MSBs and criminal organizations operating under the guise of diamond trading. The volume of trade in the diamond industry and its unique characteristics make it a sector with high risk for money laundering. When weighing the data, the **threat** in this area was rated as **moderate-high (4)**.

The **vulnerabilities** in the diamond industry are in the simplified procedures in the management of account books given to a diamond dealer, whereby the diamond dealer can determine the cost of its inventory. Additional procedures relate to the transactions ledger and the additional documentation obligations that a diamond dealer is required to maintain. Following the recommendations of the Taxation Committee established to examine the matter in the Tax Authority, a number of legislative amendments are planned, including an amendments to the bookkeeping procedures according to which, the simplified measures apply to diamond dealers will be repealed. These legislative amendments will significantly reduce the impact of this vulnerability.

Another vulnerability lies in the autonomy of the Exchange complex and the lack of transparency toward the authorities, which makes it difficult to perform routine or

spontaneous inspections. Additionally, the reporting mechanism at border crossings on the import of diamonds into Israel, impairs the ability to trace money laundering activity in this sector.

The **control measures** include the Prohibition on Money Laundering Order, which applies obligations under the PMLL on the diamond industry, and the Diamond Inspection, Import and Export Order, 5739-1979, which provides conditions for the receipt of a business license and provisions for the import and export of diamonds. The control measures also include dedicated and focused activity of task forces for locating professional money launderers; regulation of taxation in the industry; the Regulations of the Israel Diamond Exchange, which define rules of conduct and proper trading, and enables disciplinary proceedings and the suspension of the membership of a member of the Diamond Exchange; an ethical code for members of the Diamond Exchange whose objective is to create an additional layer of rules expected from members of the Diamond Exchange; training activity at the Diamond Exchange; stricter conditions of entry to the Diamond Exchange through a renewed issuance of membership cards in a more restricted and controlled manner.

The phenomenon of money laundering through diamond trading is being investigated by law enforcement agencies. The identification of the threats posed by the diamond trade contributes to the promotion of more effective actions to eradicate this phenomenon. Nevertheless, the existing regulation has not yet been fully implemented as part of regulatory activity, nor does it cover the problematic areas of activity in full. Therefore, the rating given to **mitigation measures** in the field is **moderate (3)**.

Consequence - Money laundering activity in the diamond sector has significant financial implications due to its scope in the Israeli economy, although the social impact is negligible.

An overview of the information indicates that considerable efforts are being made to reduce the risk of money laundering and to increase transparency in this sector. At the same time, the extensive scope of the phenomenon requires continued enforcement activity, including against criminals operating under the guise of diamond trade. In view of the above, and weighting all the data, the risk of money laundering by means of diamonds was rated as moderate-high (3.7).

(e) **Real estate**

The real estate market in Israel is a significant market in terms of the number of transactions carried out in it and their financial volume. The increase in the scope of the market and the

prices level therein enables the assimilation of property generated in crime more easily. In recent years, there has been a gradual increase in the volume of real estate transactions, as well as in the prices of apartments in Israel. To that one must add the sharp drop in the number of small apartments in Israel since the 1990s, and the development of a secondary market for luxury housing. These phenomena are causing an increase in housing prices in the market and, as a result, an increase in potential profit from money laundering through the purchase of real estate.

The attractiveness attributed to investment in real estate stems from several factors, including the fact that the yield on investment in solid assets is very low, and constitutes an incentive to search for other channels where the yield is higher, such as the real estate market. With regard to the threat of money laundering, the absence of a developed rental market in Israel at the same time as the rise in rental prices creates another channel for money laundering by means of long-term real estate leasing, while achieving a significant return and "double laundering" of the funds obtained in the offense – in the first stage, through the purchase of an asset, and in the second stage, by receiving rent for use thereof.

Taking advantage of the real estate market to launder funds is a worldwide phenomenon that is well known and simple to execute, due to the unique characteristics of real estate, which include large scale transactions that can be carried out in cash, diversity of the property values which allow for manipulations regarding the value, lack of obligation to record the complete chain of ownership of the property (meaning, the ultimate beneficial owners), and more. In addition, in a period of low interest rates, the real estate sector, which is relatively stable and yields profits, can serve as a favored route for criminals to invest the proceeds of crime.

A review of the information on the financial status of real estate purchasers in Israel shows that the income level of about a fifth of them is not higher than the average in the economy. This fact raises concerns that some of the funds that financed the purchase stemmed from unreported revenues. However, a significant portion of real estate transactions are carried out through the taking of mortgages, in which case the transaction will be carried out through the banking system, and within this framework will be subject to all the control measures applied by it, including examination of the parties to the transaction and the source of the money used in the transaction, thus significantly reducing the threat.

As noted, the real estate market in Israel is at its peak both in terms of the volume of transactions executed and in terms of the level of prices prevailing therein. These characteristics enable money laundering activity, although mainly in cash transactions that are *not* executed within the financial system. In light of the above, the **threat** of money laundering as a result of real estate assets was rated **moderate-high (4)**.

The **vulnerabilities** mainly include the cases in which transactions are made in cash, since these transactions can be carried out outside the financial system that applies control measures for the prevention of money laundering.

Another difficulty exists in monitoring the beneficial owners of real estate, mostly where the owner is a corporation, or when the acquisition of the real estate is done by a trustee (this vulnerability is relevant mainly when the purchase is made in cash or by a foreign check, since in payments through a financial institution, there is an obligation to declare the identity of the beneficial owner).

Another vulnerability is the non-application of the AML regime on real estate agents. However, it is important to emphasize that the risk posed by the activities of real estate agents in Israel is very low, since they are licensed by law, they rarely get involved in the financial transactions and their main role is limited to bringing together the parties to the transaction.

Control measures – the vast majority of estate transactions in Israel are carried out with the assistance of lawyers, which reduces the risk of money laundering, as lawyers carrying out transactions in real estate are subject to the PMLL and required to conduct CDD at the time of service. In addition, lawyers are subject to ethical rules that require them to refrain from carrying out a transaction that they believe has a high risk of money laundering. Additionally, the reporting obligation to the Tax Authority on real estate transactions (including information on beneficial owners) also reduces the threat, as the obligation apply to all transactions (including cash). The financial sector also operates control measures, including an examination of the source of the funds, an examination of the reasonableness of the transaction, conducting CDD (including tracing the beneficial owners), and a refusal to carry out transactions entailing the risk of money laundering.

In addition, the amendment of the PMLL, in which offenses under the Land Taxation Law were supplemented as predicate offenses, and the mechanism for transferring information between the Money Laundering Prohibition Authority and the Tax Authority will assist in the detection and monitoring of money laundering through real estate.

In this context, it should be noted that a government bill that has been submitted in recent months seeks to prevent the use of cash in large transactions, including real estate transactions, which will prevent the ability to launder money by real estate.

In view of the above, and after weighing the data of law enforcement authorities regarding the effectiveness of enforcement activity, the rating given to the **mitigation measures** is **moderate (3)**.

Consequence – money laundering activity in the real estate market has significant financial

and social implications, *inter alia*, because it affects the increase in real estate prices in the market.

In conclusion, in view of the wide scope of this market in Israel on the one hand, and the control measures detailed on the other hand, the risk of money laundering through the real estate was rated as moderate-high (3.7).

(f) Legal Persons and arrangements

The legal entities and legal arrangements discussed in the context of the risk of money laundering are companies (public, private, foreign), partnerships, trusts (private, public - charities, religious). In addition, the involvement of trust and company service providers was also examined.

Alongside the differences between types of entities and legal arrangements, they also have common characteristics that may turn them to attractive for money laundering, including – difficulties in tracing the ultimate beneficial owners, the possibility of creating a complex structure of corporations, the possibility of using "nominees" who act on behalf of criminals in a bank account (including a trust account) or in a corporation (as shareholders or directors), as well as the involvement of professional financial intermediates involved in money laundering through corporate structures and trusts (for example, by finding opportunities to exploit regulatory deficiencies in foreign countries that enable the concealment of the ultimate beneficial owner).

Information gathered indicates that there are differences in the level of threat posed by different types of entities and legal arrangements (e.g. trusts vs. public companies). In addition, there is not clear information regarding the volume of assets held in trusts..

When weighing all the data, the **threat** (mostly in relation to private trusts) was rated as **moderate-high (4)**.

The main **vulnerabilities** include difficulties in tracing the ultimate beneficial owner in companies under circumstances involving a foreign company; the lack of a complete and accessible database on trusts; and the non-application of the PMLL to trust and company service providers.

There is also a difficulty with regard to religious trusts, which stem from the lack of reliable and up-to-date information regarding the number and scope of assets held in them, and especially the absence of a regulator with effective supervision and control powers.

The **control measures** include obligations applicable to private and public companies to provide information to the Companies Registrar and to the Securities Authority, including all

of their shareholders, controlling stakeholders, etc.; the obligation applicable on trustees of public trusts to submit reports to the Registrar of charities, including the trust's assets; sharing of information between the Companies Registrar and law enforcement authorities; obligations imposed on supervised entities under the PMLL, which include provisions requiring the identification and verification of beneficial owners and controlling persons in legal persons and arrangements; a draft bill proposing streamlining the supervision on public trusts; and the available information on trusts in the Tax Authority.

The weighting of all of the above, results in the rating of the **mitigation measures** as **moderate (3)**.

In conclusion, due to the lack of adequate registration and supervision with respect to private trusts, these legal arrangements are vulnerable to money laundering, whereas the risk that arises from the other types of legal persons and arrangements is lower. Recent legislative changes improved the situation regarding the identification of ultimate beneficial owners in legal persons and arrangements. Therefore, the risk of money laundering arising from legal persons and arrangements is rated as moderate-high (3.7).

(g) Non-profit organizations

The non-profit sector in Israel consists mainly of non-profit associations ("*Amutot*"), charitable companies, unincorporated charitable organizations (*Gemach* – "acts of kindness"), public and religious trusts (discussed in the "legal persons and arrangements" chapter). This sector is significant in the activity of the civil society, and the vast majority of its activity is legitimate.

However, this important sector is also exposed to money laundering risks. The degree of risk posed by each of these organizations varies according to the characteristics and the differences in the control and monitoring mechanisms that apply to them; for example, there are supervisory gaps and lack of reliable and up-to-date information on unincorporated charitable organizations (*Gemach*), however, their activity does not have significant financial scope within the financial sector. In light of all this, the **threat** was classified as **moderate-high (4)**.

The main **vulnerabilities** identified were the absence of the obligation to register *Gemach*, as well as the fact that they are not subject to the PMLL, which becomes especially relevant if the financial activity is not conducted through the financial institutions.

The **control measures** vary according to the type of non-profit organization. The data provided indicated that with respect to *Amutot* and charitable companies, there is an adequate regime of supervision and control, which includes various reporting requirements, record keeping, and restrictions on anonymous donations. On the other hand, with respect to the certain types of non-profit organizations (*Gemach*), there are gaps in the current supervision but there are initiatives to amend the legislation, including a bill under discussion in the Knesset intends to arrange the regulation of *Gemach*.

After weighting the control measures that apply to the non-profit sector as a whole, and after weighting the various legislative initiatives designed to address the main identified vulnerabilities, the **mitigation measures** were rated as **moderate (3)**.

In conclusion, in light of the size of the non-profit sector and the estimates regarding its financial scope, and the fact that most of the non-profit organizations have comprehensive and effective arrangements for supervision and control, the final risk of money laundering in non-profit organizations, was rated as moderate-high (3.7).

(h) Alternative payment methods

The global market of alternative payment methods is constantly evolving, and includes, among other things, online payment services, electronic wallets, payments through social networks, digital checks, virtual currencies and more. The payment system in Israel has developed greatly in recent years through various technologies that enable non-contact payments; mobile payment terminals; Internet payments; and using electronic wallets and payment applications for computers and smartphones.

According to law enforcement authorities' information, currently there is no evidence indicates the existence of a money laundering through alternative payment methods. However, the threat inherent in alternative payment methods, results in the **threat** being rated as **moderate (3)**.

The **vulnerabilities** identified in respect of alternative payment methods include the lack of supervision over the cross border transfer of prepaid cards; the lack of adequate supervision over the use of electronic wallets that allow anonymous transactions to be performed; and the lack of supervision over the use of virtual currencies, which enables the execution of various transactions in a completely anonymous manner, so that the funds will not be traceable.

The **control measures** include the AML/CFT orders that apply supervision to the issuance of prepaid cards; the MSBs Order that requires monitoring and apply reporting obligations with

regard to financial activity through an electronic wallet; and the regulation of virtual currency service providers and prepaid cards under the Financial Services Supervision Law. Note should also be made to the draft bill formulated to regulate payment systems, which resulted from the report of the Committee for the Regulation of alternative payments methods.

The phenomenon of money laundering using alternative payments methods is not identified by law enforcement authorities as a risk, although there is not sufficient information to clearly indicate the scope and the extent of these means in money laundering schemes. The control measures are partial at this point, although it appears that they will be reinforced later upon completion of the various legislative processes. In light of the above, the rating of the **mitigation measures is moderate-low (2).**

In conclusion, there is not much information regarding the volume of money laundering that is carried out through alternative payments systems, but this area is developing and contains an inherent risk of money laundering, and regulation in this area is at its inception and is expected to develop in the near future. Therefore, the risk posed by it is rated as moderate (3).

(i) Business service providers (lawyers and accountants)

Business service providers are an important and vital part of the legal and financial system in Israel, and adhere to strict ethical rules that apply to them. However, there is a risk of their misuse for money laundering activities, especially in cases where criminal entities seek to abuse the professional knowledge of business service providers in order to disguise their activity and launder capital.

In September 2015, Amendment No. 13 to the PMLL came into force, imposing various obligations under the PMLL, including the obligations of identification and due diligence of customers, imposed on lawyers and accountants, when they perform financial activity defined by law as "business service." These activities are real estate activities, buying and selling of a business, managing assets and finances, receiving possession or transfer of funds for the establishment and management of corporations, and establishing or managing a corporation, business or trust for another. Most of these activities are more commonly performed by lawyers, compared to accountants.

Business service providers are not required to report to the Money Laundering Prohibition Authority about their customers' activities, but rather are subject to a disciplinary sanction where they provide service to a customer despite the existence of a high risk of money

laundering or terror financing. The detailed content of the obligations, including the duties of identifying, verifying, assessing the risk and keeping documents, was determined in the Prohibition on Money Laundering Order (The Business Service Providers Requirements Regarding Identification, Record-Keeping for the Prevention of Money Laundering and the Financing of Terrorism), 5775-2014, as well as the ethical rules published by the professional chambers.

A widespread pattern of action in this context relates to money laundering activity through the establishment of complex legal structures and trusts, when criminal elements seek to exploit the professional knowledge and the advantages of professional privilege in order to disguise their activity. However, the order along with the fact that these are not new modes of operation, indicate that this pattern of action will not increase. Thus, the **threat** to money laundering by business service providers was rated as **moderate (3)**.

The **vulnerabilities** include the absence of obligation on lawyers and accountants to report to the IMPA, as well as the legal restrictions on wiretapping to a lawyer.

The **control measures** in this area include the application of CDD procedures on lawyers and accountant who provide a "business service" and the disciplinary prohibition on a business service provider to provide service to a customer in case of a high risk of money laundering or terror financing. In addition, most of "business services" provided by lawyers and accountants, are performed through the financial system that applies its monitoring measures, hence reduce the risk.

The phenomenon of money laundering through business service providers is identified and investigated by law enforcement authorities. Applying the prohibition on money laundering regime to lawyers and accountants significantly reduces the risk of money laundering, despite its partial suitability to the international standards. Therefore, the **mitigation measures** were rated as **moderate (3)**.

The constant growth in the number of business service providers makes it accessible to use their professional services in a variety of areas that constitute a threat to money laundering. In weighing these data, compared with the existing control measures, the risk of money laundering by business service providers was rated as moderate (2.7).

(j) Gold trading

The physical characteristics of gold make it relatively easy to smuggle and move from place to place, and therefore easy to conceal. Due to the inherent value of gold and the ability to

convert it easily around the world, it is often used as a substitute for cash and as a means of paying debts and distributing proceeds of crime. The pattern of activity relating to gold relates to the import and smuggling of gold, the transfer thereof through several geographical points until it reaches the destination in a manner that makes it difficult to trace its route, and issuing fictitious invoices in order to disguise its source. These patterns of activity enable criminals involved in trading thereof to distance themselves from the laundering chain through intermediaries and couriers who transport gold through the various land borders.

The data collected does not indicate significant activity in respect of the gold trade, and there are no significant indications of the existence of extensive criminal activity in Israel in the field. The weighting of these data led to the **threat** of money laundering by using gold as **moderate-low (2)**.

The **vulnerabilities** in the field of gold in Israel are mainly focused on the legislative level, since precious metals dealers are not subject to the money laundering prohibition regime. The patterns of the use of cash in the precious metals industry, along with varied and sophisticated trading methods on the Internet, make it difficult to identify the source of the money. On the other hand, the **control measures** include the registration requirements that apply to gold dealers as "dealers" in the Tax Authority, which require them to manage the business inventory, issue tax invoices and file periodic reports. Another control measure is the obligation of gold importers to open a file in the customs and VAT authorities. Furthermore, the publication of red flags has also contributed to the identification of the phenomenon. Therefore, when weighing the data, the **mitigation measures** in the field were rated as **moderate (3)**.

The gold sector has unique characteristics that enable anonymity, but this is not a market with significant volume in Israel. Examination of the vulnerabilities reveals that the scope of the control measures is sufficiently high in view of the scope of the threat. Consequently, the risk of money laundering by trading in gold was rated as moderate-low (1.7).

(k) Cross border money transfer

Cross border money transfer is a well-known global pattern of money laundering, in part because of the ease of transferring cash or other negotiable instruments between countries. Money laundering can be done either by the offender himself or by a courier on his behalf, and can be done through various border crossings and by means of cargo or mail. In light of the above and the extent of the phenomenon, as emerges from the data of law enforcement

authorities, the **threat** resulting from the phenomenon is **moderate (3)**.

The **vulnerabilities** include the threshold for reporting cross border transfers, which is higher than the international standard; the restrictive definition of the term "money" in the PMLL, which does not include any negotiable instruments.

The **control measures** include reporting obligations on cross border transfers which also apply a sanction (criminal or administrative); and investment of resources for the identification and seizure of undeclared cross border transfers, including cooperation with enforcement agencies abroad. In addition, a proposed bill amending the PMLL is currently being submitted to the Knesset Constitution, Law and Justice Committee, which proposes to reduce the declaration threshold, and to expand the definition of the term "funds" in the law in a way that will address the aforementioned vulnerabilities.

In view of the above, there is an ability to identify and investigate money laundering activities through cross border transfers. Despite the vulnerabilities, and in light of the control measures and the advanced legislative initiatives in this matter, the **mitigation measures** were rated as **moderate-high (4)**.

In conclusion, cross border money transfers is a well-known international ML method, and due to its low scope in Israel, it is estimated that there will be no increase in this phenomenon. Although there are certain vulnerabilities, it seems that some of them are related to legislation, while the rest do not carry much weight. In weighting these data, it was assessed that the risk of money laundering through cross border money transfers is moderate-low (2.2).

(1) Trade (under/over invoicing) and smuggling of goods

Money laundering through trade activity has been identified by international organizations as a money laundering pattern, which is based on the abuse of business operations carried out for the purposes of international trade. The simple methods of laundering include the issue of fictitious invoices, the transfer of funds between different parties in the same business organization for the purpose of exploiting different tax rates in different countries and government incentives, and money laundering through trade in services.

The smuggling of goods at border crossings is also a known pattern of money laundering. The PMLL defines offenses of smuggling goods into and out of Israel as predicate offenses, and authorizes the customs to investigate them and the money laundering involved therein. The inclusion of these offenses in the list of predicate offenses was derived both from its severity

and from the fact that the transfer of goods enables and embodies, in practice, the transfer of money; as well as from the fact that smuggling offenses are often related to the activities of criminal organizations that seek to transfer assets from or to the country, without any report or control. In view of the above and on the basis of the analysis conducted of inflow/outflow against import/export information, and intelligence of law enforcement authorities, which indicate that the scope of the phenomenon is not significant, the **threat** of money laundering through trade and the smuggling of goods is rated as **moderate (3)**.

The **vulnerabilities** in this area relate to practical difficulties in identifying fictitious transactions when concealed within legitimate import/export activity. On the other hand, the **control measures** used by the Customs Authorities to prevent the abuse of trade activity for money laundering purposes, allow the identification of goods smuggling and investigations of money laundering where the predicate offense is smuggling. In this context, it should be noted that the *National Cargo Identification Center* assists the Customs in locating cargoes with risk characteristics passing through the international borders, as well as collaborations and information sharing with counterpart authorities abroad. In view of the above, the rating of the **mitigation measures** is **moderate-high (4)**.

In conclusion, it seems that the scope of the phenomenon is limited. At the same time, several control measures have been identified by the customs authorities in order to prevent the abuse of trade for money laundering. Therefore, the risk of money laundering through trade is rated as moderate-low (2.2).

(m) Purchase of lottery winnings

The legal gambling activity in Israel includes National Lottery and gambling carried out by the Council for the Regulation of Sports Gambling. The National Lottery has been subjected, within the framework of the permit granted to it by the Ministry of Finance, to certain obligations in the area of money laundering. The Council for the Regulation of Sports Gambling has also recently been subjected to similar obligations, which will come into force at the beginning of 2018.

Money laundering by means of permitted lotteries is done by means of the purchase of gambling winnings by criminal elements, in order to launder proceeds of crime.

The activity of purchase of winnings by criminal entities in order to launder proceeds is estimated at tens of millions of NIS only. In view of the above, the **threat** of money laundering was rated as **low (1)**.

The **vulnerabilities** that arise in relation to the phenomenon of purchase of winnings are the absence of a complete and uniform regulation of the legal gambling field in Israel. For example, the ML obligations apply to the National Lottery, but at this stage, the Council for the Regulation of Sports Gambling is not yet subject to them. Another vulnerability lies in an ineffective reporting mechanism between the National Lottery and the police regarding suspicions of money laundering.

The **control measures** include the application of certain ML obligations to the National Lottery, including the reduced threshold of NIS 20,000 for identification of the Lottery participants; and also the application of the legislative obligations to the Council for the Regulation of Sports Gambling as part of the adoption of the recommendations of the Committee for the Regulation of Legal Gambling In Israel, as it was recently anchored in legislation, which will come into effect soon. In light of the above, the **mitigation measures** were rated as **moderate-high (4)**.

In conclusion, in light of the low scope of the phenomenon on one hand and the existence of effective control measures on the other, the risk of money laundering by purchase of winnings was rated as low (0.8).