

Proposal for remediation
between United Arab Emirates (2016 Kimberley Process Chair)
and the Kimberley Process Civil Society Coalition
January 2016

At the 2015 Plenary of the Kimberley Process Certification Scheme in Luanda, Angola, the Kimberley Process Civil Society Coalition (the Coalition) took the unusual step of announcing a boycott of the 2016 chairmanship of the United Arab Emirates (the UAE). To ensure that engagement by the UAE or any other KP participant on this point remains constructive and relevant, the Coalition will briefly restate the basis for this decision.

The Coalition's decision to distance itself from the UAE's chairmanship is not a self-suspension from the KP in any way: the Coalition will continue to engage with the Kimberley Process (KP) during the coming year (e.g. participating in activities such as working groups, review visits and monitoring the current situation in Central African Republic). However, the UAE's chairmanship of the KP for 2016 poses a threat to the KP's international reputation. It poses a risk to any integrity retained by the KP through the efforts of those invested in securing its efficacy. This is because prominent international organizations,¹ civil society groups both outside² and inside the KP,³ and investigative journalists,⁴ have repeatedly raised serious concerns about the policies and practices of the UAE and the Dubai Multi-commodities Centre (DMCC), in terms of their impact on the flow of conflict diamonds (intrinsically linked to issues of fraud, money laundering and possible terrorist financing, in addition to the KP's *raison d'être*) as well as their contribution to tax evasion, which undermines upstream state efforts under the KP's Moscow and Washington Declarations. Unfortunately, these concerns have been met with no concrete action on the part of the UAE or the DMCC.

The Coalition understands that a number of the issues raised regarding the UAE are also applicable in greater or lesser degrees to other major trading centers, particularly free trade zones. As chair to the KP for 2016 and home to one of the world's largest free trade hubs for diamond trading, the UAE is, however, expected to show leadership on conflict diamond issues specific to large trading centers of this nature.

In Luanda, the Coalition offered to reassess its position should the UAE take urgent remedial action to fix a number of deficiencies, which have undermined not only its own international reputation but the integrity and efficacy of the Kimberley Process. After discussions with governments and industry leaders, the World Diamond Council—the other Observer in the Kimberley Process—offered to act as a third party guarantor and mediator in the UAE's efforts to address the concerns of the Coalition. These

¹ See for example the UN Panel of Experts for the CAR, http://www.securitycouncilreport.org/atf/cf/%7B65BF9B-6D27-4E9C-8CD3-CF6E4FF96FF9%7D/s_2014_762.pdf, and the Financial Action Task Force, *Money Laundering and Terrorist Financing through Trade in Diamonds*, October 2013, <http://www.fatf-gafi.org/media/fatf/documents/reports/ML-TF-through-trade-in-diamonds.pdf>.

² See for example, Partnership Africa Canada, *All that Glitters is not Gold: Dubai, Congo and the Illicit Trade of Conflict Minerals*, May 2014, <http://www.pacweb.org/images/PUBLICATIONS/All%20That%20Glitters.pdf>.

³ See for example: Enough Project, *Behind the Headlines: Drivers of Violence in the Central African Republic*, May 2014, <http://www.enoughproject.org/files/CAR%20Report%20-%20Behind%20the%20Headlines%205.1.14.pdf>; Amnesty International, *Chains of Abuse: The Case of Diamonds From the Central African Republic and the Global Diamond Supply Chain*, September 2015, <https://www.amnesty.org/en/documents/afr19/2494/2015/en/>.

⁴ E.g. World Policy Institute, 'Kimberley's Illicit Process', *World Policy Journal*, winter 2014.

concerns led the KPCS to highlight the need for the UAE government to take urgent remedial action on four key issues:

- **The UAE's valuation processes.** In 2014, these processes saw the UAE re-export African diamonds at an average of 44% higher than the value at which they were originally imported from African countries – a figure four times that of competing trading centres.⁵ Together with a lack of government oversight of its internal diamond trade, this markup creates an additional opportunity for conflict diamond infiltration of the legitimate supply chain and represents a massive loss of tax revenues to African treasuries;
- **The UAE's lack of enforcement cooperation with key trading partners.** This has thwarted several diamond related investigations by police in other jurisdictions such as Antwerp;
- **The absence of an enhanced vigilance system** for diamonds emanating from problematic and conflict affected areas like the Central African Republic (CAR) and its immediate neighbours, as required by a 2013 Administrative Decision by the KP. The absence of robust measures has seen Dubai referred to in reports on the CAR conflict as somewhere "where it is easy to 'give illicit diamonds a second lease on life' through forged KP certificates".⁶
- **The need for constructive and genuine engagement with the civil society coalition** in the spirit of the tripartite foundation upon which the KP was founded and is intended to operate. The UAE's future engagement with and conduct regarding the Coalition is one measure of its ability to adhere to the collaborative, tripartite spirit expected of a KP Chair.

Representatives of the DMCC have acknowledged the Coalition's broad concerns. The extent to which the UAE and the DMCC take effective and genuine action on them will prove indicative of their appropriateness for the role of KP chair, as well as their commitment to restoring the tripartite foundation of the Kimberley Process.

Actions required on the part of the UAE to safeguard the KP

Since Luanda, the Coalition has carried out extensive consultations with governments, industry members and associations, and other civil society organizations to develop a comprehensive set of actionable and measurable ways by which the UAE can improve its internal controls and demonstrate the leadership needed to gain the full confidence of all stakeholders of the Kimberley Process.

Below are some of the minimum steps the UAE can take for this to happen. The Coalition has the full expectation and desire that the UAE government will propose its own measures capable of either meeting or exceeding the ones laid out below. While the recommendations reflect the outcomes civil society expect to see, the UAE has latitude in how they decide to implement and achieve them.

The Coalition is open to constructively engaging with and facilitating the UAE in consultation on how best to implement measures to address the concerns raised. In doing so, the Coalition would request that the government of UAE identify a representative from the Ministry of Economy or Foreign Affairs with a sufficient level of seniority to act on the government's behalf in its engagement with the Coalition and to action any measures agreed to.

⁵ See for example: Op cit, Partnership Africa Canada (2014).

⁶ Enough Project, *Behind the Headlines: Drivers of Violence in the Central African Republic*, May 2014, p.10.

The Coalition leaves open the possibility of lifting its boycott of the UAE's chairmanship of the KP in the event that the UAE demonstrates genuine efforts to address the concerns referred to both in this letter and by other civil society actors, such as Amnesty International and the Financial Action Taskforce (FATF), prior to the 2016 Plenary. Such efforts will be continuously assessed by the Coalition. The sooner substantial and demonstrable movement in the identified areas is made, the sooner the coalition's possible re-engagement with UAE's chairmanship.

Below are some minimum and recommended actions that the UAE should take to address some of the civil society concerns about deficiencies in its internal controls:

1. Under Valuation

The establishment of a system of internal controls designed to eliminate the presence of conflict diamonds from shipments of rough diamonds imported into and exported from a participant's territory is a mandatory stipulation of the KP core document (section IV(a)). Accurate valuation forms a key part of this task when it comes to trading states like the UAE, as outlined by the FATF in 2013:

Diamond trade centres like Dubai, which operate as Free Trade Zones (FTZ) are susceptible to vulnerabilities as specified in the FATF report regarding the ML vulnerabilities of FTZ. This, in combination with the specific vulnerabilities of the diamond trade and the mechanism of transfer pricing, creates a significant vulnerability for ML and TF activities. By way of over or under invoicing with affiliate diamond companies located in FTZ, it is possible to illegitimately shift profits from diamond companies in high tax rate countries to FTZs and thus avoid taxes. It is also possible to use the same scheme for ML/TF purposes. The combination of a lack of transparency in the diamond trade with a lack of transparency in a FTZ provides an excellent atmosphere to conduct large volume transactions without being detected.⁷

For this reason, a number of KP recommendations and best practices make reference to diamond valuation. Multiple KP Review Visit reports, most notably in 2008, have raised concerns about the UAE's valuation practices, which see inexplicable increases in the values on re-exports that are not shared by other trading centres.

While the Coalition recognizes that the issue of valuation is complex, several fundamental changes are needed to the UAE's import and export procedures to help with its KP compliance, satisfy the parameters of an enhanced vigilance system and deliver greater economic benefit to producer countries. These include:

- Requiring all shipments be opened and valued by government diamond valuers with at least 10 years of private sector experience and/or with GIA training (or equivalent).
- Creating a system through which anomalous shipments lacking evidence of justifiable value addition and with a valuation differential of +/-15 percent between import and re-export are flagged for special measures, including quarantine and referral to tax, customs and enforcement agencies in the country of original export for possible reappraisal and legal action. In such instances, government valuers and/or inspectors must make a report to UAE Customs authorities, who will investigate and decide on any legal procedures to follow.

⁷ FATF 2013, p.61.

- In instances where there are repeated differences in valuation of +/-15 percent between import and re-export are found in a particular reporting quarter the UAE KP focal point must report the names of the exporters and the reason(s) why to the KP Working Group on Statistics.
- Legally require industry members trading in the UAE to submit to regular independent audits to government authorities of their annual stock declaration forms, imports, exports, local purchases and records.
- Where problems with stock declaration are identified impose mandatory penalties that rise with the frequency with which irregularities are encountered, irrespective of excuse.
- Giving oversight for all stages of the import, export and valuation inspection procedures to government officials from the Ministry of Economy or Customs in place of the DMCC. This measure is needed to avert any real or perceived conflicts of interest with the DMCC, a private sector entity, acting in an oversight capacity over UAE's diamond controls.
- Undertaking widespread, open and transparent discussions with KP Participants, industry experts, the FATF, civil society actors and others, on ways to ensure more accurate and fair market valuation for diamonds, including the conclusion of an Administrative Decision in 2016 to this effect.
- Offering training for the export authorities of major exporting participants with a view to reducing the risk of undervaluation upon export.

2. Enforcement Cooperation

A robust enforcement system is the cornerstone of KP compliance and enforcement cooperation between participants is a mandatory component of the KP core document.⁸ It is therefore important for all participating governments, and even more so major trading hubs such as the UAE, to collaborate on investigations and exchange relevant information necessary to investigative and judicial cooperation.

The Coalition notes with concern that despite the UAE being the world's second largest diamond trading center and a number of serious red flag incidents concerning questionable diamond shipments, there have been no criminal charges or convictions of diamond related crime since the Emirates joined the Kimberley Process in 2003. This is despite several cases in other jurisdictions where enforcement authorities have traced illegality back to the UAE and unsuccessfully sought help from the UAE authorities in building their investigations. With this in mind, and in accordance with the KP Core Document, the UAE must:

- Urgently undertake bilateral meetings with key trading partners to determine gaps in diamond related enforcement cooperation. This should specifically include Belgium and India, where

⁸ KPCS Core Document, Section V (d): Participants should consider favourably requests from other Participants for assistance to improve the functioning of the Certification Scheme within their territories

KPCS Core Document, Section V (g): Participants should encourage, through their relevant authorities, closer cooperation between law enforcement agencies and between customs agencies of Participants.

cases such as those involving Kardiam and Winsome Diamonds have exposed shortcomings in the enforcement cooperation between UAE and its key trading partners.

- Based on this consultation, UAE should sign bilateral enforcement agreements or Memorandums of Understanding (MoU) with key trading partners that address any identified shortcomings that currently impede diamond-related investigations that have a UAE connection.
- Once such bilateral agreements are in effect, the UAE must demonstrate full cooperation with foreign authorities on any current investigations through implementation reporting. Such cooperation should include but not be limited to: evidence of information sharing by UAE enforcement authorities and the DMCC; access by foreign investigators to individuals and companies which reside in the UAE, and their banking and trading data; examples of investigations and/or criminal proceedings against UAE resident companies or individuals linked to criminal activity that undermines the KP compliance of UAE or other Participants.
- Meet with the Financial Action Taskforce (FATF) regarding their 2013 report on anti-money laundering vulnerabilities in the diamond sector and present a firm and implementable plan by which UAE will mitigate against risks raised in the report. In doing so the UAE must publicly communicate and demonstrate what steps it has undertaken in this regard.
- Convene a meeting of leading diamond lending banks (inside and outside UAE's jurisdiction) to discuss ways to create or strengthen commonly applied Know Your Customer procedures that adequately address risk-based threats to the diamond industry and these banks.
- Phase out the practice of allowing diamond transactions to be made in cash instead of through legal banking channels, as required by Annex II (7) of the KP Core Document, and considered a best practice by the FATF and diamond lending banks.
- As recommended by the UN Group of Experts in 2014 , create a due diligence system by which all shipments originating from areas under enhanced vigilance are checked to ensure their origin and documentation is correct.⁹
- Provide government oversight over the Dubai Diamond Exchange as part of the DMCC and its practice over industry self-regulation, as required by the KP.

3. Enhanced Vigilance

The May 2014 seizure by Belgian authorities of an illegal shipment of Kardiam diamonds from the Central African Republic that transited through the UAE made it clear that current policies and practices of the DMCC are not sufficient to interrupt the illicit trade of conflict diamonds.

It is further noted that according to a Kimberley Process Administrative Decision on Central African Republic agreed in 2013, all KP participants need to have an enhanced vigilance system in place to offer credible due diligence on diamonds emanating from areas under KP or United Nations supervision, such

⁹ See p. 56-57, United Nations Group of Experts Report on Central African Republic, October 2014: http://www.securitycouncilreport.org/atf/cf/%7B65BFCF9B-6D27-4E9C-8CD3-CF6E4FF96FF9%7D/s_2014_762.pdf

as Central African Republic and neighbouring countries. To date, the UAE has yet to create or implement such an enhanced vigilance system.

Because of the prominent market share of its diamond trading industry, the urgency for the UAE to develop such a system is not only long overdue but critical to the integrity of the Kimberley Process and the international diamond trade. With this in mind:

- The UAE needs to prioritize the creation and implementation of a credible and enforceable enhanced vigilance plan. The details of this comprehensive vigilance system are for the UAE to determine. However, it must include features that adequately address concerns multiple reports¹⁰ have raised about vulnerabilities in UAE's internal controls system, including reference to existing KP recommendations for best practices and the extent to which they are given meaningful effect.
- At a minimum the proposed system should meet and exceed the criteria currently used by other leading trading centres. The UAE should share any proposed plan with the Coalition, the UN Group of Expert panels and the KP Working Group on Monitoring for constructive feedback. Once an enhanced vigilance system is designed, the UAE should share its system with other KP Participants for their possible adoption.
- The UAE has often spoken about the need to create a photographic database of CAR diamonds. As part of their vigilance system the UAE should develop and operationalize such a database with other KP participants, as well as footprint and fingerprint data that outlines the particularities of diamonds from the country's various mining areas, their morphology and weigh distribution; as well as the known trading patterns of companies in the Central African region. Such information should be shared with all KP Participants.
- Once an enhanced vigilance system is in place, the government of UAE must oversee its implementation and provide KP stakeholders with evidence of its implementation. This would include, but not be limited to, evidence of spot checks, investigations and seizures of suspicious shipments, and invitations to mutually accepted and independent third parties such as the UN Group of Experts to make unannounced visits to monitor the effectiveness of such a system. It should also include provision to ensure the removal of any perception of conflict of interest on the part of those implementing the system by making government rather than private sector officials responsible for its implementation.
- The government of UAE should conduct regular (e.g. annual) audits of industry member inventory records and reporting on outcomes.
- The government of UAE should develop a register of traders importing from countries attracting enhanced vigilance measures and impose spot checks on shipments.
- Any diamonds that are brought into the UAE without a KP certificate or that appear to be illicit must be confiscated, and reported to the Kimberley Process.

¹⁰ See for example, the October 2014 UN Group of Experts report on CAR, Amnesty (2015), and PAC (2014).

4. Relations with Civil Society

The role of the Civil Society Coalition and its status as one of the two founding Observers in the Kimberley Process is well established in both the Core Document and by precedent. The Coalition's current position on the UAE's chairmanship is a demonstration of its commitment to the KP and is in no way, shape or form to be treated as an indicator of withdrawal from the KP. The Coalition will continue to communicate its position to all relevant parties in its efforts to preserve the integrity of the KP's tripartite foundation, which also includes ensuring the independence of the third (civil society) pillar.

With this in mind any attempt by any KP Participant to misinterpret our current position with respect to UAE's chairmanship or move to sanction or unilaterally alter the civil society representation and independence in the KP will result in an escalation of the Coalition's current position.

Since assuming the chairmanship of the Kimberley Process the UAE has publicly committed itself to improving its relationship with the Coalition. A key aspect of this process will be for the UAE to build trust and demonstrate its commitment to the tripartite foundation of the KP through sincere and measurable collaboration with the Coalition on meeting the best practices outlined in this document.

We believe the best starting point for this engagement is for the government of the UAE to propose a government official who will act as the focal point with the Coalition. Partnership Africa Canada (PAC) is the coordinating organization for the Coalition and will act as the first point of contact with the UAE government. The Coalition will shortly nominate a small delegation that will represent civil society in any possible bilateral meetings or formal discussions with the UAE.

The Coalition welcomes a written plan by which the government of UAE intends to address the recommendations laid out in this document, including ameliorating its relationship with civil society groups in the Kimberley Process.