

KALOTI  
JEWELLERY  
INTERNATIONAL DMCC

Hong Kong | Singapore | Dubai | Istanbul | Miami Assoc.

DMCC Responsible Sourcing of Precious Metals Guidance

Compliance Report

27<sup>th</sup> November 2013

## Background

In April 2012, the DMCC issued a risk management reference manual in order to assist DMCC-licensed members and other industry participants in the UAE to enforce acceptable standards of due diligence and responsible supply chain management when sourcing gold and precious metals from conflict-affected and high-risk areas. The DMCC guidance incorporates a '5-Step' framework that relies on each stakeholder within the supply chain to collectively work together to ensure due-diligence is carried out at the highest level. In November 2012, DMCC issued the 'Responsible Sourcing of Precious Metals Review Protocol' to help ensure that Dubai Good Delivery (DGD) accredited member refineries and global industry participants that have adopted the guidance are compliant with the DMCC issued guidelines. Version 3.1 of the Review Protocol was released in June 2013 with minor updates, which provided clarification on amended areas such as role of the DMCC review committee and definition of compliance with low risk deviations.

This Compliance Report outlines the steps taken by Kaloti Jewellery International DMCC (KJI) and Kaloti Jewellers Factory Ltd. (KJF) to achieve full compliance with the DMCC's Responsible Supply Chain Guidance as well as following all international regulations covering Anti Money Laundering and Terrorist Financing. Kaloti Jewellery International DMCC (KJI), which is based in Dubai, is responsible for the management of all aspects of the physical precious metals business in the United Arab Emirates. It is the licensed entity that faces clients and counterparty service providers such as international bullion banks, security and logistics companies, insurance and airline firms. Kaloti Jewellers Factory Ltd. (KJF), an independent entity based in Sharjah, is the refinery service provider of the Kaloti's United Arab Emirates operations and is the entity that enjoys Dubai Good Delivery accreditation. References to systems, procedures and controls in this refinery report collectively cover both KJI and KJF.

## Details of The Reporting Entity

Name:	Kaloti Jewellers Factory, Sharjah, United Arab Emirates Kaloti Jewellery International DMCC, Dubai, United Arab Emirates
Reporting Periods:	1 <sup>st</sup> June 2012 – 31 <sup>st</sup> December 2012
Date of Report	27 <sup>th</sup> November 2013
Senior Management Responsible for this Report	Tarek El Mdaka, Managing Director Osama Al Kaloti, Managing Director

## Our Evaluation

This report covers the period 1<sup>st</sup> June 2012 to 31<sup>st</sup> December 2012 ("the initial audit period") with a remediation period to 3<sup>rd</sup> August 2013 for the non-compliance items noted during the initial audit period that are described at the end of Steps 1 and 2.

The requirements that need to be satisfied in order to be in full compliance with the DMCC's Practical Guidance on Responsible Sourcing of Gold and Precious Metals are set out below.

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**Step 1. Establish Robust company supply chain management systems**

Compliance Statement: **We are fully compliant** following the implementation of our corrective action plan

We have developed and implemented robust policies and processes for responsible supply chain, the role of our compliance officers, adequate security requirements and training on responsible supply chain.

**a. Has the refinery adopted a company policy regarding due diligence for supply chains of gold?**

Compliance Statement: **We are fully compliant.**

Our policy is published on our website [http://www.kalotico.com/our\\_policy.php](http://www.kalotico.com/our_policy.php) and sets out our responsibility and full commitment to establish and maintain strong management systems in order to:

- i. Fight human rights violation.
- ii. Avoid any actions that might contribute to conflict.
- iii. Fight money laundering and the financing of terrorism.
- iv. Conduct stringent and systematic due diligence across the entire supply chain and monitor all customers and transactions using a risk based approach.
- v. Maintain up to date supply chain documentation
- vi. Conduct on-going training for all employees involved in the Precious Metals supply chain.

Senior management's mission is to continually update and strengthen its compliance policy particularly with respect to the supply, transport and trade in Gold and other Precious Metals, and for the policy to be in line with the Practical Supply Chain Guidance issued by the Dubai Multi Commodity Centre (DMCC), which is based on the OECD Due Diligence Guidance for Responsible Supply Chains of Minerals from Conflict-Affected and High-Risk Areas

**b. Has the refiner assigned a dedicated compliance or risk officer?**

Compliance Statement: **We are fully compliant.**

- o We have established a robust risk management and compliance system under the direction of a Chief Compliance Officer (CCO).
- o The CCO leads a Compliance team of six that is responsible for the implementation and enforcement of the company's Compliance Policy with the full support of Senior Management.

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- o The CCO and all other Compliance Officers possess the necessary competence, knowledge and experience to oversee the supply chain due diligence process.
  - o The main duties of the Compliance Officers are fully in line with the requirements set by our regulator, the DMCC.
  - o Our Compliance team works closely with the Compliance and Inspection Departments of our regulator, the DMCC, calling on their expertise and assistance to assist us in ensuring full and complete implementation of the DMCC due diligence guidelines on responsible supply chain.
  - o The Compliance Department utilizes a wide range of available resources including World-Check, online/Govt. verification etc. in order to determine the authenticity and verification of all documents.
  - o Our Compliance Department has established its own independent processes and shares the Compliance Policy and other relevant information with employees and suppliers.
  - o Our Compliance Department has developed KYC forms and informative notes to support clients and suppliers in the due diligence process.
  - o Our Compliance team conducts on-site visit to our suppliers' business premises to review their procedures, due diligence process and for compliance discussion and awareness.
- c. **Has the Refiner developed internal documentation and records of supply chain due diligence to cover internal inventory and transactional documentation?**

Compliance Statement: **We are fully compliant** following the implementation of our corrective action plan

- o The company maintains full documentation and client files with respect to the client on-boarding KYC due diligence process.
  - o All transaction related documents are kept on the clients' files with this information including invoices, customs papers and full details of the gold supplied by clients including the form, weight and purity.
  - o A new system was installed called the FACTS Compliance system during 2013; this has improved the compliance team's ability to keep track of required and expired documentation. It provides accuracy for dates on documentation and an alert system before the document is expired.
  - o With respect to our production we keep detailed records of all gold bars produced at the refinery with each bar having a unique serial number that allows us to track and trace the bars.
- d. **Has the refiner strengthened company engagement with gold supplying counterparties, and where possible, assisted gold supplying counterparties in building due diligence capabilities?**

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Compliance Statement: **We are fully compliant** following the implementation of our corrective action plan

We have taken practical steps aimed at strengthening our engagement with gold supplying counterparties to assist them in building their own due diligence capabilities.

- We have communicated our Responsible Supply Chain policy to suppliers by electronic email and conducting on-sites visits.
- We follow an on-going process of Compliance and Due Diligence awareness email communication with suppliers.
- We have shared the DMCC practical guidance with all existing clients and this is included as a standard part of the new client on-boarding process.
- Our Compliance Department has developed KYC forms and informative notes to train and support clients and suppliers in the due diligence process.
- Our Compliance team conducts on-site visit to our suppliers' business premises to review their procedures, due diligence process and for compliance discussion and awareness.
- We have sponsored the Turkish language version of the DMCC Guidance on Responsible Supply Chain.
- We sponsored the DMCC's Responsible Sourcing Workshop held on 2 April 2013.

e. **Has the refiner developed adequate security requirements?**

Compliance Statement: **We are fully compliant.**

We have established and maintain the highest standards of security at our Refinery with key features including:

All material received from clients is segregated on receipt and recorded by origin and type of supply, i.e. mine supply Dore bars or scrap jewellery Dore bars to assist our track and trace procedures.

The material remains segregated and held securely during the first stage assay with the initial purity and weight results verified against the original documents and transmitted to the clients. Then we proceed with the melting process at which point the material is co-mingled with other clients' material as a batch for efficient refining purposes. We are always able to track and trace all client supplies back to the date of the original melt batch.

Our Refinery's process requires all material received to be melted into grains with the grains being refined on a daily basis into kilo bars, large bars (12.5 kg); ten tola, 100 gram cast bars, and minted bars. Every kilo bar and large bar (12.5kg) produced by the refinery has its own unique serial number. This enables us to track and trace each of these Kaloti bars back to the original date of production.

On premises security features:

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- Security gates with monitoring cameras and sensors.
- Physical access to high security areas is controlled with strong identification and authentication technique. Access rights to secure areas are regularly revised and updates.
- All members of staff enter and exit the refinery using sensor finger print technology with photos at every Access Point.
- Workers entry is allowed only their own departments.
- All main doors and safe doors controlled and monitoring with Police Department.

f. **Has the refiner conducted necessary training for persons involved in supply chain due diligence?**

Compliance Statement: **We are fully compliant.**

We conduct the necessary due diligence and KYC training for all persons involved in the supply chain. There is an ongoing process of compliance training and awareness of all risks, especially red flags, through the following:

- i. Internal Compliance training to front office employees (Customer Relationship Managers, Dealers, Finance Department). We regard this group as the first line of "Red Flag Defence".
- ii. Compliance awareness communication with suppliers.
- iii. Compliance awareness email communication with all staff.
- iv. Compliance awareness articles in internal newsletter.
- v. Sponsoring Responsible Sourcing Workshops held by DMCC on 02-04-2013
- vi. Participation of compliance personnel on the following compliance seminars:
  - a. Due Diligence for Responsible Sourcing of Precious Metals and Ensuring Responsible Supply Chain Management held by DMCC held on 11-07-2012
  - b. "Compliance & Anti Money Laundering Seminar" held by Thomson & Reuters and DMCC on 24-09-2012
  - c. "Anti Money Laundering briefing" held by DMCC and ICT (International Compliance Training Middle East) on 7-10 -2013

During the initial review period we had deviations with regards to sub step (c) relating to KYC and due diligence documentation in respect of a small number of clients representing in aggregate less than 1% of our overall business and of suppliers of mined gold ; and to step (d) relating to helping clients build their due diligence capabilities. Subsequently we have now implemented a corrective action plan and **we are now fully compliant.**

**Step 2. Identify and assessing the risks in the supply chain**

Compliance Statement: **We are fully compliant** following the implementation of our corrective action plan



**a. Does the Refiner take into account geographical, counterparty and transactional risk?**

Compliance Statement: **We are fully compliant** following the implementation of our corrective action plan

Our policy is to "Know Your Geography (KYG)", "Know Your Customer (KYC)", and "Know Your Transaction (KYT)". We have modified and upgraded our procedures and policies with the aim of ensuring that we take into account all geographical, counterparty and transactional risks.

**"Know Your Geography (KYG)"**

We conduct enhanced due diligence on supplies from countries assessed as high risk (Red Flag) and countries bordering Red Flag areas.

**"Know Your Customer (KYC)"**

The customer risk classification is determined at the on-boarding stage by reference to the content and quality of documentation provided by the client, and the geographic location where the customer is based, taking into account the country's financial and regulatory system, records on human rights abuse, and whether sanctions exist or have existed. For example we do not accept over the counter (or walk in) customers.

**"Know Your Transaction (KYT)"**

Prior to each and any transaction the risk of the deal is assessed taking into account the form and quality of the precious metal, the original source of the precious metal, the nature of the customers' business, and the customers' historical trading activity. The risk assessment process includes actionable points to mitigate any risks identified. By way of example we have adopted a zero tolerance approach to cash transactions which means that we will not accept cash in payment for physical gold bars, nor will we pay cash for the supply of scrap or dore gold bars.

**b. Has the Refiner conducted enhanced research on red flagged customers with respect to locations?**

Compliance Statement: **We are fully compliant** following the implementation of our corrective action plan

We now conduct enhanced due diligence on red flagged customers with respect to geographic location. This includes:

- o Organizing site visits to high-risk clients, taking pictures and issuing visit reports to be kept on the clients' files.

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- o We have appointed a Compliance Officer to oversee the transactions originated from key clients, associates and, or subsidiaries to coordinate, train, guide and monitor the source of supply and the measures in place for responsible sourcing.
- o We perform in depth due diligence on medium and high risk as per DMCC requirements by enhanced investigation into gold supply chain in order to identify the actual source of gold and mitigate identified risks.

**c. Has the refiner conducted enhanced research on red flagged supplier prior to engaging with them?**

Compliance Statement: **We are fully compliant** following the implementation of our corrective action plan

Our standard client on-boarding process requires us to conduct a "Know Your Customer" risk analysis on all potential suppliers prior to engaging with them. If we classify a potential supplier as high risk we conduct enhanced due diligence on all aspects of the client so that we fully understand the actual source of gold to be supplied and the nature of the client. Unless we are fully satisfied that risks can be mitigated so as to comply with the DMCC guidance we will reject such clients and supplies

During the initial review period we had deviations in sub steps (a), (b) and (c) in which KJI did not identify risks in cash settlement transactions which was the typical modus operandi in the Dubai wholesale gold market. We took steps during 2013 to assist our suppliers in moving away from cash settlement and are fully remediated from November 2013. There was also a lack of documentation in identifying risk in the supply chain for a small number of transactions although they were in accordance with Dubai Customs import regulations, there were no such items following the implementation of our corrective action plan. **We have now remediated all these points and are fully compliant.**

**Step 3. Has the refiner developed and implemented a risk mitigation/control plan?**

Compliance Statement: **We are fully compliant.**

- o We have designed and implemented a strategy for risk management of any identified by either:
  - i. Mitigation of the risk while continuing to trade with the customer, or
  - ii. Mitigation of the risk while suspending trade with the customer until the risk has been resolved, or
  - iii. Disengagement from the risk.
- o We have taken steps in 2013 to further strengthen our policies and procedures as part of the on-going strategy to mitigate geographical, counterparty and transactional risks. These steps include:
  - The Internal Quality Team conducts periodic internal audits.



- We have implemented the "FACT" system in the Compliance Department to automatically monitor client files with respect the expiration of essential documents allowing us to request updates from the clients.
- Our Physical Department reports to Compliance Department for review any cases where inconsistency has been observed, for example purity, contents, type or form of material and documentation.

**Step 4. Carrying out independent third party audits of gold and precious metals company's due diligence practices.**

Compliance Statement: **We are fully compliant.**

We have arranged for annual independent third party audit of our gold and precious metals compliance and due diligence practices by engaging Ernst & Young, Dubai. They have completed a reasonable assurance audit of our due diligence practices and a follow up review in line with the guidance and protocols provided by the DMCC. Both the original review and the subsequent follow up review were conducted on both KJI and KJF in accordance with the International Standard in Assurance Engagements ISAE 3000 Assurance Engagements Other than Audits or Reviews of Historical Financial Information.

**Step 5. Reporting annually on responsible supply chain due diligence**

Compliance Statement: We will be fully compliant upon the release of this report.

The first review and follow up on our supply chain due diligence has been completed and this report will be made public upon receipt of the associated auditors assurance report.

**Management Conclusion**

We have fully implemented all aspects of the Practical Supply Chain Guidance issued by the Dubai Multi Commodity Centre (DMCC) which is based on the OECD Due Diligence Guidance for Responsible Supply Chains of Minerals from Conflict-Affected and High-Risk Areas. We are fully committed to adopting any future guidelines, rules or regulations with respect to the responsible supply of gold and precious metals and all other international rules relating to anti-money laundering and the fighting of terrorist financing. We will continue to strive to upgrade and improve our risk classification and risk mitigation processes and educate our staff and our suppliers on an on-going basis to ensure that the highest possible standards of responsible supply chains are maintained. If users of this report wish to provide feedback to Kaloti International DMCC or have any questions they can contact our Compliance Department by sending an email to [dubai.compliance@kalotico.com](mailto:dubai.compliance@kalotico.com)

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*AREEK ELMAJARA  
27/11/2013*