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COMPLIANCE IRELAND BRIEFING NOTE UK FSA FINES FIRM AND MLRO FOR INADEQUATE AML SYSTEMS AND CONTROLS

This briefing note is on-line at
http://www.complianceireland.com/documents/UK_FSA_fines_MLRO_20081029_Final.pdf
and www.antimoneylaundering.ie

United Kingdom Financial Services Authority (FSA) fines Money Laundering Reporting Officer and his employer for failing to have adequate AML systems and controls in place for verifying and recording clients' identities.

On 29 October 2008, the UK FSA fined both Sindicatum Holdings Limited (SHL) £49,000 (Euro 62,450 / USD 80,650 / AUD 118,400) and its money laundering reporting officer (MLRO), Michael Wheelhouse, £17,500 (Euro 22,300 / USD 28800/ AUD 42,300) for not having adequate anti-money laundering systems and controls in place for verifying and recording clients' identities. This is the first time the FSA has fined a money laundering reporting officer.

The FSA found a number of failings including:

- the firm failed to implement adequate procedures for verifying the identity of its clients;
- it failed to verify adequately the identity of a significant number of its clients;
- it failed to keep adequate records with regard to the verification of the identity of its clients; and
- Mr Wheelhouse failed to take reasonable steps to implement adequate procedures for controlling money laundering risk.

The head of retail enforcement at the FSA, William Amos, said:

"It is vital to the integrity of the UK's financial markets that regulated firms are not used by criminals to launder money. Senior management must implement and follow procedures that meet our requirements so that the risks their firms face are properly managed.

"This fine is a warning to firms and individuals about the importance of complying with our rules in this area and we will not hesitate to clamp down on failures, where necessary."

Although the significance of the fact that the MLRO was fined should not be lost on compliance and AML professionals, it is also interesting to read that the FSA took into account the limited financial resources of the firm in deciding the amount of the penalty. The FSA stated that had the firm the ability to pay a larger fine, then a significantly larger fine would have been imposed. This is an important point especially noting that no evidence of money laundering was identified by the FSA. Firms, and their MLROs, should note that regardless that a firm might consider itself to represent a low AML risk, this does not translate into not implementing adequate systems and controls for the risks posed. The 3rd EU AML Directive, now implemented in the UK by the Money Laundering Regulations 2007 and soon to be implemented in Ireland by the Criminal Justice (Money Laundering) Act – supplemented by relevant guidance notes – requires covered firms to undertake and document a risk assessment at (i) firm, (ii) client/transaction, (iii) product/service, and (iv) geographical levels. Further, covered firms must adopt a written AML/CFT Policy supplemented by adequate and sufficient AML/CFT procedures, including on-going due diligence, monitoring (at all levels) and effective training.

The FSA has a statutory responsibility to reduce the extent to which it is possible for a business carried on by a regulated person to be used for a purpose connected with financial crime. Sindicatum Holdings Limited

is a corporate advisory firm based in London with small and medium sized corporate clients in countries including Lithuania, Slovenia, Russia, Hungary, the Czech Republic and the UK.

The FSA concludes its press release confirming that SHL and Mr Wheelhouse have taken robust steps to review and improve the firm's systems and controls in relation to financial crime.

Readers of our regular Newsletter will recall in Newsletter 3/2008 (available at http://www.complianceireland.com/documents/CI_Newsletter_July08.pdf) we reported on the FSA withdrawing its approval of Irene Hall, Compliance Officer at PMSG Insurance Services Limited (fined £35,000), for lacking the competence and capability to ensure that her firm complied with FSA regulations including those aimed at ensuring the fair treatment of customers. Again, this was a case where senior management did not organise the regulatory affairs of the business to responsibly assess and adopt adequate risk management systems.

While it is true that other compliance and risk officers have faced regulatory actions, including one senior in-house compliance lawyer being jailed for insider dealing (UK) and others charged with money laundering (US), the regulatory sanctions imposed on Mr Wheelhouse and Ms Hall will certainly cause compliance professionals great concern. Regardless of the specific facts in the matters of Michael Wheelhouse and Irene Hall, the FSA's message is clear – *if you hold a senior position, including that of compliance officer or MLRO, and your firm fails to meet its regulatory obligations which can be attributable to either the fitness or probity of the compliance officer/MLRO, that person is likely to be disciplined by the FSA.* In such cases the failure to implement adequate systems and procedures calls into question the fitness of the approved person and may lead to regulatory sanctions.

There are a number of issues in the FSA's Final Notice that will strike (and perhaps perplex) readers:

- A. Mr Wheelhouse set up a New Business Committee in November 2006. This committee was established to monitor the introduction of new business and took advice from independent consultants. However the FSA considers that this action was insufficient to ensure or improve compliance with the firm's procedures and the FSA's requirements.
- B. the FSA states that the Money Laundering Reporting Officer failed to ensure that client checklists were fully completed and he made no reference to any such matters in the MLRO reports that he presented to the board of his employer.
- C. it is plausible to opine that a few readers might consider Mr Wheelhouse's actions in setting up the New Business Committee to be above and beyond what is implemented in their own firms. Equally the concept of regular MLRO reports to the board, which SHL's MLRO prepared (albeit not to the satisfaction of the FSA), is something which many firms do not implement.
- D. the FSA decided that the MLRO was a cause of the failure by SHL to take reasonable care to establish and maintain effective systems and controls for countering the risk that SHL might be used to further money laundering or other financial crime.
- E. Mr Wheelhouse failed to comply with his obligations as MLRO and with the Firm's procedures on the basis that, on one occasion, he applied an exemption from identification to a deposit-taking bank in Lithuania, despite Lithuania not appearing on the "equivalence" list for regulated entities. In Ireland, many MLROs would simply decide that as Lithuania is part of the EU (since 2004), then a client bank based in that country meets the 'short form of identification' test under section 32 of the Criminal Justice Act 1994 and the guidance notes. Many would resolve the identification issue by downloading an extract from the Lithuanian bank's regulator's website, placing it on the client file and moving on (assuming the bank was acting as a principal). It is also likely that some MLROs might disregard the fact that the bank was acting on behalf on third parties and not even move to obtaining a letter of assurance.

- F. MLROs should not themselves be involved in the collecting of identification evidence and signing off accounts as such arrangements, in the view of the FSA, decreases the likelihood of failures in the account opening process being identified.
- G. the FSA's decision recognises that the MLRO attempted to reduce the risk of SHL being used to further financial crime by employing independent compliance consultants to draft manuals, give training and conduct quarterly reviews of SHL's adherence to its systems. However, the FSA was critical of the fact that this process was often informal and that no adequate process for using feedback and advice existed for ensuring improvements in SHL's systems.

NOTE: Our Briefing Notes and Newsletters are read by compliance and risk professionals in Europe, Australia, South Africa and the Americas. However the majority of our subscribers are based in Ireland. The common consensus in Ireland is, no doubt, that the Irish Financial Services Regulatory Authority (the local equivalent of the FSA) will not likely sanction a compliance professional. Our experience is that individuals confuse the 'principles-based' approach of regulation in Ireland as equating to light-touch regulation. However the Irish Financial Regulator has the power to sanction individuals, including compliance professionals, if not now under the CB&FSAI Act 2004 and/or the Fitness & Probity Code, then (from an AML/CFT systems and controls failure perspective) it will have so under its proposed new AML/CFT powers once the 2008 law is passed. Recent fines imposed (or settled) by the Financial Regulator on firms and senior management have surprised many of us. The question is 'Are there more surprises in store as the regulator continues to develop its strategy?'.

- Read this Briefing Note in pdf at http://www.complianceireland.com/documents/FSA_fines_MLRO_20081029_Final.pdf
- Read the Final Notice in respect of Michael Wheelhouse at http://www.complianceireland.com/documents/michael_wheelhouse_MLRO_fine_20081029.pdf
- Read the Final Notice in respect of SHL at http://www.complianceireland.com/documents/sindicatum_fine_20081029.pdf
- Read the FSA press release at http://www.complianceireland.com/documents/FSA_Library_Communication_PR_2008_125.pdf
- Visit our Anti-Money Laundering website at www.antimoneylaundering.ie

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