Why Can’t We All Just Get Along?

A call for the convergence of AML and ABC compliance functions at financial institutions

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INTRODUCTION

The United States Department of Justice (DOJ) has been known to target corruption inquiries by industry. As a result, companies in the extractives industries, medical devices and pharmaceutical industries over recent years have developed fairly robust and sophisticated anti-bribery and corruption (ABC) compliance programs. According to various experts, including lawyers at Morrison Foerster, it appears that the DOJ has its sights set on the financial services industry.[1] Why now, and why an industry typically more attune with anti-money laundering compliance? Financial institutions, hedge funds and private equity firms can have exposure to the Foreign Corrupt Practices Act (FCPA) risk in a number of ways. Those include dealing with Politically Exposed Persons (PEPs), high level employees of state-owned enterprises who are considered to be foreign officials under the FCPA, sovereign wealth funds, employees of publicly traded companies (issuers) acting abroad, foreign companies in which they invest by acquiring risk, as well as laundering suspicious proceeds through their accounts. Quite simply, the United States has an interest in assuring that its financial institutions are not abused to launder the proceeds of corruption. Integrating ABC compliance into existing AML compliance programs makes sense not only financially, but also practically, because where there is corruption, there are proceeds to be laundered.

[1] http://www.mofo.com/files/Uploads/Images/130515-DOJ-Turns-FCPA-Spotlight.pdf

BACKGROUND

In late 2010, the Department of Justice introduced the Kleptocracy Asset Recovery Initiative, an effort to "target and recover the proceeds of foreign official corruption that have been laundered into or through the United States[2]." The DOJ is so dedicated to this endeavor that the initiative involves three sections of the DOJ's Criminal Division: the Asset Forfeiture and Money Laundering Section, the Office of International Affairs, as well as the Fraud Section. The DOJ has brought several high profile cases under this initiative in the past several years, most famously, the case of Teodoro Nguema Obiang Mangue, son of the then president of Equatorial Guinea. Obiang engaged various intermediaries including U.S.-based lawyers, real estate agents and banks to move more than $110 million of illicit funds into the United States via the bank account of a company called Sweet Pink, Inc. Obiang was not a signatory on the account. [3] According to the DOJ,

> *The most high-profile of our Kleptocracy cases to date involves two civil actions we have brought against approximately $70 million in assets allegedly belonging to a government minister in Equatorial Guinea who is also the son of that country's president. According to court papers, despite an official government salary of less than $100,000 per year, this minister amassed wealth of over $100 million. Among the items we are seeking to forfeit are nearly $2 million worth of Michael Jackson memorabilia (including the white glove), a Gulfstream G-V jet worth $38.5 million, and a $30 million house in Malibu. These are hard, and hard-fought, cases, but we believe strongly that*

[2] http://www.justice.gov/criminal/pr/speeches/2010/crm-speech-101019.html
[3] http://issuu.com/world.bank.publications/docs/9780821388945/1?e=1107022/2698080

foreign officials who amass wealth through corruption should not be permitted to use the United States as a haven for their ill-gotten gains[4].

According to the DOJ's FCPA Resource Guide,[5] "companies with ineffective internal controls often face risks of embezzlement and self-dealing by employees, commercial bribery, export control problems, and violations of other U.S. and local laws." Having the proper policies, procedures and internal controls in place is one of the four pillars of an effective AML Compliance program. AML and ABC compliance, as well as risk go hand in hand, as do the related crimes. Proceeds of corruption need to be laundered to hide their illicit origin. In fact by definition, according to 18 USC §1956[6], bribery is a predicate offense (specified unlawful activity) to money laundering.

[4] http://www.justice.gov/criminal/pr/speeches/2013/crm-speech-1305091.html
[5] DOJ FCPA Resource Guide at 40.
[6] Also known as the Money Laundering Control Act or MLCA

Take the case of the Greens[7] for example. In 2009, the Hollywood producers were both convicted of bribery and money laundering, as well as tax evasion. They had paid bribes to the former governor of the Tourism Authority of Thailand in exchange for tourism contracts for a film festival. The payments originated in US banks and were wired to offshore accounts. The Greens also "used different business entities, some with dummy business addresses and telephone numbers, in their dealings with the TAT in order to hide the large amount of money the Greens were being paid under the contracts.[8]" Both served six months jail time and ordered to pay $250,000 restitution. Their attempt to appeal the order to pay restitution was denied[9]. In addition to the Greens, Siriwan, the government official who accepted the bribes and her daughter were charged by the DOJ under the Money Laundering Control Act (MLCA) for money laundering[10].

[7] http://www.jdsupra.com/legalnews/second-superceding-indictment-in-us-v-g-01381/

[8] http://www.justice.gov/opa/pr/2009/September/09-crm-952.html

[9] http://cdn.ca9.uscourts.gov/datastore/opinions/2013/07/11/10-50519.pdf

[10] http://www.fcpaprofessor.com/from-siriwan-to-gonzalez-why-the-doj-altered-the-way-it-charges-alleged-corrupt-foreign-officials

CONVERGANCE

In an environment of increased scrutiny by regulators and law enforcement in spite of financial constraints, it no longer makes sense to have entirely separate siloed compliance functions in today's modern framework. Technology providers have taken notice of the need as well. According to Oracle, for example, "the market has matured to a state where financial institutions have been going through the process of consolidating these systems to reduce overhead and gain operational efficiencies[11]." An effective compliance program is one that is an integrated model that considers enterprise-wide risk management and coordination across business units to ensure that nothing falls through the cracks.

ROBUST COMPLIANCE

Compliance departments focused only on AML/BSA requirements may result in tunnel vision and only monitoring transactions just enough to be able to file a suspicious activity report. Moreover, not only is it too narrow a focus that ignores ABC and corruption risk, it is costly and ineffective to run separate programs. This can also be problematic because it may only scratch the surface of a deeper underlying issue and fail to detect a broader pattern of suspicious activity. There is no fool proof way to guarantee that violations never occur, but having an effective and comprehensive compliance program in place can be invaluable. Such was the case with Morgan Stanley when the DOJ declined to bring an enforcement action against the company in spite of uncovering a criminal violation. The DOJ's reasoning was based on the fact that:

[11] http://www.oracle.com/us/industries/financial-services/oracle-fccm-wp-522840.pdf

According to court documents, Morgan Stanley maintained a system of internal controls meant to ensure accountability for its assets and to prevent employees from offering, promising or paying anything of value to foreign government officials. Morgan Stanley's internal policies, which were updated regularly to reflect regulatory developments and specific risks, prohibited bribery and addressed corruption risks associated with the giving of gifts, business entertainment, travel, lodging, meals, charitable contributions and employment. Morgan Stanley frequently trained its employees on its internal policies, the FCPA and other anti-corruption laws. Between 2002 and 2008, Morgan Stanley trained various groups of Asia-based personnel on anti-corruption policies 54 times. During the same period, Morgan Stanley trained Garth Peterson on the FCPA seven times and reminded him to comply with the FCPA at least 35 times. Morgan Stanley's compliance personnel regularly monitored transactions, randomly audited particular employees, transactions and business units, and tested to identify illicit payments. Moreover, Morgan Stanley conducted extensive due diligence on all new business partners and imposed stringent controls on payments made to business partners[12].

The audit procedure and pillars for both programs are remarkably similar and overlapping as demonstrated in the following discussion.

[12] http://www.justice.gov/opa/pr/2012/April/12-crm-534.html

RISK ASSESSMENT

As with any compliance program whether it is AML or ABC, the first step would be to evaluate the institution's risks including customer risk, geographic risk, product risk, etc. Compliance risk, regulatory risk and operational risk should all be considered. "A company needs to carry out a risk assessment and to consider applicable risk mitigation strategies. To this end, a company should evaluate how FCPA risk fits into its overall approach to risk, and, most importantly, how to leverage existing risk assessment and control processes[13]."

> *"A single data model covering all aspects of crime and compliance for a financial institution is the natural first step in consolidating data to ensure accurate data used in the various monitoring and detection engines. Resulting alerts and investigation decisions are fed to and from this single data model to continue the reliance on accurate data[14]."*

The institution should then collectively evaluate those risks and draft risk-based policies and procedures.

IMPLEMENTATION AND INTEGRATION

When looking at an existing AML compliance program, one can easily tailor requirements to include FCPA and bribery/corruption-related issues in written policies and procedures and training of employees. Transaction monitoring and testing should also incorporate FCPA scenarios and closer monitoring of suspicious activity such as wire transfers to offshore

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[13] Id.
[14] Id.

accounts or shell companies, payments of consulting fees, unusual political or charitable contributions, and enhanced scrutiny for payments related to government contracts. Other existing staples of AML compliance can also be further scrutinized to uncover FCPA risks:

Know Your Customer (KYC)

Financial institutions already have in place customer due diligence protocols as part of their existing AML programs. This process can be further enhanced by closer scrutiny of third parties. For example, KYC questionnaires can be expanded and targeted toward third parties such as vendors, sales agents, and distributors. Information gleaned from this first step can be used to determine the need for enhanced due diligence, which is arguably required for intermediaries. Due diligence should be ongoing and not be limited to account opening (when beneficial ownership is determined) to ensure that potentially risky transactions (such as international wire transfers) are closely monitored and appropriately flagged. For example, additional questions may include those:

- Relating to awareness of the FCPA/UK Bribery Act and related consequences
- Relating to whether the customer regularly has or anticipates dealings with government officials
- Regarding whether principals of a company have ties to government officials
- Regarding the existence of joint ventures or business partners that may have close ties to government officials

PEPs

Finance institutions have long been screening for PEPs in the context of putting the institution at risk for potentially laundering the proceeds of corruption. According to the Federal Financial Institution Examination Council[15], a basic definition of a PEP is:

- A "senior foreign political figure" is a high-level official in the executive, legislative, administrative, military or judicial branches of a foreign government (whether elected or not), a senior official of a major foreign political party, or a senior executive of a foreign government-owned corporation. In addition, a senior foreign political figure includes any corporation, business, or other entity that has been formed by, or for the benefit of, a senior foreign political figure.

- The "immediate family" of a senior foreign political figure typically includes the figure's parents, siblings, spouse, children, and in-laws.

- A "close associate" of a senior foreign political figure is a person who is widely and publicly known to maintain an unusually close relationship with the senior foreign political figure, and includes a person who is in a position to conduct substantial domestic and international financial transactions on behalf of the senior foreign political figure.

For ABC purposes, this definition should be expanded to include instrumentalities of the government, State Owned Enterprises (SOEs), and high level employees of SOEs. As a matter of

[15] http://www.ffiec.gov/bsa_aml_infobase/pages_manual/OLM_087.htm

best practices, domestic PEPs and gatekeepers (such as accountants and attorneys) should also be scrutinized.

INTERNAL AUDIT/INDEPENDENT REVIEW

The fourth pillar to an AML compliance program is periodic independent testing. Just as with an AML audit, the audit process to evaluate FCPA controls is similar, but some enhancement is necessary. For example, compliance with US Generally Accepted Accounting Principles does not guarantee the absence of fraud or compliance with the accounting (books and records and internal controls) provisions of the FCPA. As such, tidy, transparent, record-keeping, even in the case of corrupt payments is a must and should also be addressed via audit in addition to:

Policies and Procedures

- *Are there clearly articulated written policies and procedures in place that speak to methods to identify and mitigate or prevent suspicious activity?*
- *Are they clearly communicated to all relevant personnel and business partners?*
- *Does it reflect tone at the top and does it trickle down?*
- *Is there a designated individual in charge of governance?*
    - *Is that individual well trained and independent, meaning compliance decisions need not necessarily compete with business decisions, reports directly to the board or board committee?*

Training of Employees

- *Is there mandatory ABC training for all relevant personnel and business partners? Is the training ongoing? Is there a whistleblower line in place or a means to escalate a red flag?*

Testing of Controls

- *Are there metrics and systems in place to screen for suspicious activity or potential violations/transactions? Are these risk-based?*

Continued Monitoring and Auditing

- *Are existing systems still relevant? Are they effective? Is there proper analysis on the back end to detect larger schemes?*

CONCLUSION

With financial institutions experiencing more and more pressure from regulators, it only makes sense to have a cross-practice comprehensive enterprise risk management program that incorporates both AML and ABC policies into one seamless program. With so much overlap to approach, due diligence, training and auditing, it naturally follows that an integrated approach will save time and money in the long run.