

Executive Briefing – AFC Audits

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Effective senior management oversight and governance relies on effective anti-financial crime (AFC) audits. This briefing explains your responsibilities as senior management, and the questions you should consider about your organization and its audit function.

What are the responsibilities of senior management?

According to the Financial Action Task Force's *Risk-Based Approach Guidance for the Banking Sector* (October 2014):

“Senior management should not only know about the money-laundering/terrorist-financing risks to which the bank is exposed but also understand how its anti-money laundering (AML)/countering-the financing of terrorism (CFT) control framework operates to mitigate those risks. This would require that senior management:

- receives sufficient, regular and objective information to get an accurate picture of the ML/TF risk to which the bank is exposed through its activities and individual business relationships;
- receives sufficient and objective information to understand whether the bank's AML/CFT controls are effective (for example information from the Chief Compliance Officer on the effectiveness of controls, or audit reports);
- and that processes are in place to escalate important decisions that directly impact the ability of the bank to address and control risks.”

The FATF's guidance, although specific here to the banking sector, is also relevant for the non-bank financial sector, designated non-financial businesses and professions (DNFBPs) and virtual assets service providers.

What are the potential consequences when senior management does not discharge its responsibility?

Consequences for senior management include enforcement action against the organization for breaches of AFC regulations and weak AFC controls – from hefty fines to the loss of license.

“ Increasingly, consequences for certain violations of AFC regulations include personal and individual accountability of the board members and senior management. ”

What should an effective AFC audit program do?

A meaningful and effective AFC audit program:

- provides independent assurance to senior management;
- challenges the organization's AFC controls through testing;
- provides confidence and confirmation that the organization's AFC controls are effective, by:
 - confirming the controls are adequate and compliant;
 - identifying areas and opportunities for enhancement of controls.

AFC audits present an opportunity to establish a (more) effective AFC compliance program for the organization.

How effective are your AFC auditors?

Both internal and external audits are subject to increasing scrutiny by the regulators. The audit team themselves are assessed by the regulatory examiners on the following basis:

“Did the auditor or audit team involved in the review of this area have the necessary skills, experience, and knowledge required for the review?” Q.43, US Office of the Comptroller of the Currency’s (OCC) handbook *Internal and External Audits* (Version 1.0, December 2016)

During a regulatory examination, the assessment of an audit function is two-fold.



Did audit identify and raise the issue? If no, why not? This speaks to **competency**.



Did the audit report include the identified issue? If no, why not? This speaks to **culture**.

Regulatory examiners are now including their assessment of the audit function in their inspection reports. Increasingly, there is comment on audit in published enforcement actions against an organization for AFC regulatory breaches and/or weak AFC controls.

Is your organization’s AFC audit team competent?

Competent AFC auditors will:

- demonstrate a keen awareness of the financial crime risk of the organization or the line of business that is audited;
- appreciate that the organization will deploy an AFC compliance program which is risk-based, and one which is commensurate with the risk of the organization or line of business;
- keep pace with the changes in the organization’s business strategy and priorities, and the consequent changes to the management’s risk tolerance and risk appetite;
- review the methodology and outcome of the organization’s enterprise-wide AFC risk assessment and use this to inform areas of focus;
- articulate the risk when they identify deficiencies, and offer reasonable solutions to remediate and or enhance.

Competent AFC audit teams are:

- agile – they embrace technology and deploy new and diverse skill sets;
- collaborative with the auditable entities, and in particular, compliance, in looking for opportunities to enhance AFC controls, not just identifying deficiencies.

In the case of AFC technology related audits, the audit team should also bring to the audit a specialized skillset of technology to be audited in their review of implemented AFC related systems and solutions.

“ For audits to be successful, they should receive strong support from senior management for issues raised and remedial actions to be taken. ”

Is your organization's culture right for effective audits?

In organizations with poor risk culture, the voice of audit is likely to be overridden. Where an audit team does not have a strong voice, issues raised by audit may not be documented in the audit report due to the challenge from the business. Or, when they are included, there is often a weak and ineffectual commitment in the audit report's management response (e.g. "management agrees to review" or "we will issue a reminder").

In cases where internal key performance indicators (KPIs) are tied to the number of issues raised in an audit, a tense and adversarial face-off between compliance and audit may result. In this case:

- audit may feel they have to find exceptions and issues for the audit to be deemed successful, or for the audit team is to be adjudged as competent and thorough;
- AFC compliance may resist any potential observation or finding because their performance appraisal may be at stake.

Wrong KPIs, unfortunately, may not drive the right behaviors or results for compliance or audit, and can lead to a loss of credibility. In such cases:

- compliance loses its objectivity when it resists the opportunity identified by audit to enhance the organization's AFC controls (this may also extend to the business and other functions responsible for the certain AFC controls and processes);
- audit loses its credibility when it raises issues which are perceived to be spurious and trivial.

Recommendations

A strong audit function enables senior management to discharge their responsibility of effective oversight and governance over the organization's AFC program. It is therefore in the interest of senior management that they support the auditors.

- Encourage auditors to improve their competency by upskilling themselves on AFC risk awareness, effective AFC risk management and AFC related technology issues and solutions.
- Create a culture within the organization to enable a confident audit team that works collaboratively with the business and compliance stakeholders.
- Review KPIs and other performance measures for audit, compliance, and business, to ensure that these drive the right behaviors and outcomes.

What AFC audit is responsible for

Ensuring AFC policies and procedures are fully compliant with local AFC regulations

Assessing if relevant functions and units (including compliance) are complying with policies and procedures

Assessing if the controls implemented effectively mitigate or manage the organization's ML/TF risks, including new and emerging risks

Identifying deficiencies in AFC controls, following root cause analysis (people, process or system)

Ensuring that committed actions by the relevant stakeholders and management are validated and reviewed for soundness and sustainability

Acting as a partner to the business and compliance to support strategic objectives, as well as to combat financial crime

What AFC audit is not responsible for

Checking if compliance is doing its job

Looking for case-by-case exceptions and issues

Rendering own opinion as to – (a) interpretation and application of local AFC regulations (unless compliance got it wrong); or (b) compliance's exercise of an AFC risk decision (e.g. whether STR/SAR or exit is warranted)

Proposing new/different ways of avoiding ML/TF risk, which may no longer be risk based

Taking a 'tick box' approach to an audit (i.e. complete the testing and move onto the next audit)

Acting as a "troublemaker" or "the enemy"

For more information on the ACAMS programs available for upskilling AFC compliance and audit professionals, please contact us: acams.org/en/contact-us.

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