

MLROs Conference Two

Steve Lock
Head of Group Financial Crime
Prevention & Security
December 2010



Agenda

- Current issues - recent cases, RBS, Barclays, Lloyds
- Increasing international pressure – Iran
- Background to the new guidance
- What is in the new Part III
- The guidance on sanctions
- The guidance in detail
- Status of the guidance and final thoughts

Recent Cases - OFAC

- April 2006: UBS, €100m, for the transfer of US banknotes to Iran through loans and guarantees. Also violations in respect of Cuba, Libya and Iraq
- Jan 2009: Lloyds, €350m, for helping customers get around US sanctions on Libya, Sudan and Iran. Falsified wire transfers so that transfers would pass undetected through filters at US banks
- Dec 2009: Credit Suisse, €536m, for systematically hiding the identity of its Iranian clients when moving millions of dollars on their behalf and helped Libya, Sudan and Burma evade sanctions
- Aug 2010: Barclays, £190m, violations of the Sudanese sanctions regulations, plus systemic patterns of conduct which gave rise to violations of OFAC sanctions re Burma, Cuba and Iran

Recent Case FSA

- FSA – August 2010, £5.6m fine (30% reduction for early settlement) against Royal Bank of Scotland Group for failing to have adequate systems and controls in place to prevent breaches of UK financial sanctions
- First enforcement action in UK for breach of sanctions
- Case brought by the FSA and not HM Treasury
- Legislation - Money Laundering Regulations 2007 (“the Regulations), which require that firms maintain appropriate policies and procedures in order to prevent funds or financial services being made available to those on the sanctions list.

RBS Findings 1

- Found breach of Regulation 20(1) by failing to establish and maintain appropriate and risk sensitive policies and procedures relating to:
 - Customer due diligence and ongoing monitoring
 - Internal control, and
 - The monitoring and management of compliance with, and the internal communication of, such policies and procedures,
- In order to prevent funds or financial services being made available to designated persons on the list of financial sanctions targets maintained by HMT.

Findings in RBS case II

- RBS were found to have failed to establish and maintain appropriate and risk-sensitive policies and procedures re implementing and overseeing systems to screen customers and payments against the Consolidated List. Did not screen the following payments:
 - Incoming payments to customers
 - Sterling payments by customers (except to US)
 - Euro payments made by customers

- Failed to screen the majority of trade finance SWIFT messages in the international trade transactions it carried out

Findings in RBS case III

- Did not consistently record sufficient information in relation to directors and beneficial owners of its corporate customers. Where information was recorded, failed to screen on an ongoing basis
- Failed to ensure that the design and implementation of 'fuzzy matching' capabilities continued to operate satisfactorily. The results produced by the screening filters were not routinely reviewed or monitored and the parameters became less effective at identifying potential matches.

Implications of RBS case

- RBS case sets new UK regulatory expectation with regard to
 - Linkage between risk policies and 'real life'
 - Importance of knowing your software
 - Fuzzy matching
 - Care needed with interpretation here
 - Screening processes
 - what must be screened (including payment screening), frequency, how to review systems and parameters for matches etc
 - Lessons important but worth thinking that this is for RBS (€16 trillion of payments pa) – where does your firm sit in risk spectrum?

Increasing International Pressure on Iran

- Council Regulation 961/2010
- More comprehensive basis for restricting activity that possibly assists with nuclear proliferation;
- Targets the following sectors:
 - Energy
 - Insurance
 - Financial Services
 - Transport

Financial Services I

- New measures do not prohibit all transactions with Iran, but
 - New authorisation and reporting requirements imposed on financial institutions which transfer funds to and from Iran
 - Under €10,000 no requirements
 - €10-40,000 prior notification
 - Transactions relating to food, medical equipment, healthcare or humanitarian purposes require no prior authorisation but prior notification required if over €40,000
 - Other transactions above €40,000 require prior authorisation
 - Iranian banks with EU branch/subsidiary must notify relevant authority of funds transfers made or received within 5 working days after transaction date
 - All insurance services for the benefit of Iranian entities including the government of Iran are prohibited
- Very broad – important to know what potential impacts for your firm

Financial Services II

- Asset freeze
- UK based entities, Persia International Bank plc, Bank Saderat plc, Irinvestship Ltd, and
 - IRISL UK Ltd has been deleted but other European IRISL subsidiaries are still there
- Plus Bank Mellat (already the subject of the first directions under the Counter-Terrorism Act 2008)
- Existing licences that allowed activity with Mellat frozen, and separate authorisation now needed to receive payments from these entities.

Financial Services III

- What must firms do to comply?

- Decide if you have any exposure to Iran or Iranian entities in any part of the business – if so
 - Do you continue?
 - If you continue with Iranian linked activity, must ensure that not in breach of EU, UK or US sanctions and understand scope of US sanctions.
 - Monitor any transaction that could have an Iranian connection
 - Ensure that the different obligations from the different legislation restricting Iranian linked activity eg companies that are due payments under letters of credit, performance bonds/guarantees or other agreements drawn against Iranian banks

Industry (JMLSG) Guidance

- Background
 - Some existing text in JMLSG Part I
 - Absence of substantive guidance
 - FSA thematic review of compliance with UK financial sanctions regime
 - Number of enforcement actions – principally OFAC and now the FSA
 - Escalation to Board level of sanctions profile in financial firms
 - JMLSG discussions 2009
 - JMLSG Sanctions Editorial Panel established September 2009

Section 4 – Complying with the UK Financial Sanctions Regime I

- General introduction, purpose, compliance, size, who should use the guidance, and how to use it
- What is the financial sanctions regime, penalties for non compliance, other forms of sanctions
- Approach, management responsibilities, risk assessment, procedures and training
- Screening, customers, names and transactions, false positives, audit trails and record keeping
- Reporting matches and breaches

Section 4 – Complying with the UK Financial Sanctions Regime 2

- Annexes
- Relevant legislation
- Regimes currently in place
- Responsibilities for the UK regime
- Licensing regime
- Sources of information

Sanctions Guidance - Detail

4.17 – 4.18: other forms of sanctions, trade sanctions, investment bans etc

4.20: overseas jurisdictions and OFAC need to comply with requirements in jurisdictions where firms operate

4.34 – 4.38: risk assessment in light of business profile, and geographic activity, need to document where most vulnerable to possible matches

4.36 – 4.66: screening customers, transactions, anything else, screening software, fuzzy matching, outsourcing, timing of screening, dormant accounts

4.62 – 4.66: assessing possible matches, false positives, audit trails and record keeping

4.67 – 4.79: reporting of matches and of breaches to HMT and the FSA?

Status of Part III Guidance

- Issued by JMLSG in October 2010
- JMLSG guidance traditionally “approved” by HMT Minister
- Sanctions guidance not approved and appears unlikely to be so (but has been published)
- Read it and determine what impacts your firm

Final thoughts

- Requirements from international bodies are increasing and the US will further increase pressure on Iran if no diplomatic solution
- Further enforcement action for breaches of UK financial sanctions regime now likely
- Sanctions guidance may be imperfect but a significant achievement.

Questions?