

Regulatory enforcement trends

The Cayman Islands Bankers' Association recently welcomed Michael Shepard, Principal with Deloitte Transactions and Business Analytics LLP, who gave an overview of global and US AML regulatory enforcement trends and spoke of the renewed sense of urgency associated with them, at a gathering of CIBA members at the George Town Yacht Club.

Anti-money laundering was still a hot topic, Shepard said, and reinforced the view that an effective AML compliance programme helped to mitigate risks associated with money laundering and terrorist financing.

Noting that AML regulation was working, Shepard said AML statutes and compliance were still important tools the US government has in combating financial crimes and terrorist financing. As a result, financial institutions continued to face AML enforcement actions; however, in

the wake of the financial crisis, some banks had reduced staff and spending on AML compliance as part of their austerity measures.

"As large banks improve AML compliance and exit higher risk businesses, money launderers could migrate to mid-sized and smaller banks," he warned, adding that regulatory enforcement actions were on the rise.

With the US Department of Justice's focus on compliance and criminal prosecution for non-compliance, Shepard said that an effective compliance programme could advance three significant objectives, to: prevent and detect unlawful conduct and mitigate criminal fine and sentencing consequences.

Regulators can hold individuals personally liable for compliance deficiencies, he said, and quoted recent actions brought about by the likes of FINRA, the SEC and the OCC.

In the UK the Financial Conduct Authority had been busy, opening 109 Inquiries in 2014, compared with 90 in 2013. 60 inquiries were opened in 2014 into individual employees. As an example, in January 2015 a former group treasurer and head of tax at a British retailer was sentenced to 12



Mike McWatt, past President Cayman Islands Bankers' Association, left, with Michael Shepard, Principal with Deloitte Transactions and Business Analytics LLP

- **In the last 5 years, the Federal Reserve has issued 113 enforcement actions related to BSA and OFAC compliance, including 25 public cease and desist orders and written agreements**
- **With these recent actions, the Federal Reserve has assessed hundreds of millions of dollars in penalties –large, small, US and non-US FIs**

What is the role of a Corporate Monitor?

When a corporation accused of wrongdoing agrees to settle charges or is sentenced to probation, it is sometimes required to pay for a monitor to ensure compliance with the law and appropriate AML controls enhancement

months in jail for insider trading and February 2015 the FCA had opened 67 investigations on people or firms it had previously approved to manage investments under the Alternative Investments Fund Managers Directive.

Benjamin Lawksy, New York Department of Financial Services Superintendent, appeared to be increasing scrutiny of financial institutions operating in New York and the use of corporate monitors, Shepard advised.

In addition, regulators could reopen cases and find broken promises and willful violations, resulting in additional penalties, he warned. The NY Department of Financial Services was reportedly taking a fresh look at old cases, reopening settlements, and in some cases could seek to impose a larger penalty than the previous one.

Recent Cayman Islands AML Enforcement Trends International Cooperation

While Shepard noted that CIMA has agree-

Latest enforcement trends

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ments with leading authorities, such as the SEC, the US Commodity Futures Trading Commission, the UK's FCA and IOSCO, there were increasing expectations of financial institutions. These included the training of key staff, procedures established for determination and confirmation of the true identity of the customer, ongoing monitoring of business relationships, recognition and reporting of suspicious activities to the reporting authority, among others.

Enhanced US scrutiny on non-US financial institutions required improving compliance capabilities, he warned, outlining where common weaknesses could lie further to regulatory enforcement actions.

These weaknesses included insufficient resources dedicated to compliance, risk assessments lack quantitative analysis and support, inadequate KYC procedures, including limited view of entire customer relationship (inadequate "feedback loop") and employees, Board and management having not received relevant and targeted AML compliance training.

Having three independent, well-resourced, effective lines of defence – oversight functions, internal audits and business operations - helped to manage and mitigate ML / TF risk, Shepard confirmed. A culture of compliance and sufficient training for all employees were critical steps to elevating AML compliance programmes, he said.

Five key expectations could be made regarding AML compliance programmes:

1. Leadership should set the tone from the top. Leaders of the organisation should always remain informed of the state of the institution's AML compliance and FI's leaders commitment should be visible as it influences the attitudes of others within the organisation.
2. Compliance should not be compromised by revenue interests
3. Information should be shared throughout the organisation
4. Compliance programme should be effective and tested by an independent



Michael Shepard, Principal with Deloitte Transactions and Business Analytics LLP

and competent party

5. Leadership and staff should understand how their AML reports were used

"Changing the culture of compliance at your institution may be the biggest challenge you face. Start small and think long-term," Shepard advised, giving the following pointers to improve the compliance culture:

- Maintain open communication with regulators;
- Understand the generation GAP.

Messages must reach and resonate with a multi-generational workforce;

- Be proactive vs. reactive. The advantages to a reactive approach would be a lower upfront cost and simplicity. The disadvantages would be higher incremental costs, incompleteness and increased risk. The advantage to a proactive approach is demonstrably better compliance.
- Leadership should make the whole organisation understand the importance of AML. Compliance is the responsibility of all.

Heightened expectations were driving significant change, Shepard said.

Proposed beneficial ownership rules

Common themes that ran through recent regulatory pushes by FinCEN, the EU and the FATF included:

Definition - natural person(s) who directly or indirectly hold a minimum percentage of ownership interest in legal entity customers in addition to individuals with a certain level of control over the entity (including those on whose behalf transactions are conducted)

Threshold Approach - Proposed minimum standard of 25% and, for the purposes of assessing ownership, suggest financial institutions "may" want to use a lower (10%) threshold under certain circumstances

CIP Practices - Collect name, date of birth, address and US social security number or equivalent for non-U.S. persons and verify consistent with existing risk-based CIP practices

Standardisation - Information must be collected in a standardised format.

Key Questions

Managing different threshold expectations -what do you implement and when?

Minimum CDD requirements -does missing information lead to an expectation to deny services?

Obtaining "accurate" beneficial ownership information – Will institutions be held accountable for entities that provide false information?