

INTERNATIONAL BANKING

Expert Analysis

New Recommendations on Combating Money Laundering, Terrorist Financing

For over 20 years, the Financial Action Task Force (FATF) has developed international standards to fight anti-money laundering (AML) and terrorist financing.¹ One of its signature works has been its Forty Recommendations, first released in 1990, on fighting money laundering. The Recommendations later were expanded to encompass the financing of terrorism and the proliferation of weapons of mass destruction (WMD).

After an extensive review, in February the task force released the latest revisions of the Recommendations, the “International Standards on Combating Money Laundering and the Financing of Terrorism & Proliferation.” This month’s column will review the history of the Recommendations and discuss the significant aspects of the 2012 version. Banks operating internationally should be aware of the revised Recommendations and be ready for possible operational adjustments that might be necessary in order to meet the new and revised standards contained therein.

A Little History

The Financial Action Task Force was established in 1989 in Paris by the G-7 countries, the European Commission and eight other countries to develop proposals on a global basis to fight money laundering. From this original membership of 16 in 1989, the task force has grown to 36 members (34 member countries, the European Commission, the Gulf Co-operation Council) representing countries around the globe, and its standards are used by more than 180 countries.

Original Recommendations

The first set of Forty Recommendations was issued in 1990 and in addition to periodic revisions, detailed interpretive notes on the Recommendations have been developed to accompany many of the individual Recommendations, which have been of great assistance to those charged with implementing them. The original Forty Recommendations dealt solely with anti-money laundering issues and broke down into general categories covering measures to be taken at the international level, the individual country level and the individual financial institution level.

By
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Special Recommendations

After the terrorist attacks in the United States on Sept. 11, 2001, the FATF expanded its mandate to include measures to fight terrorist financing and issued Eight Special Recommendations on Oct. 31, 2001, adapting many of the AML Recommendations to the issue of terrorist financing, such as criminalizing the financing of terrorism. In addition, the task force recommended the licensing or registration of persons providing money transmission services. The FATF also drew attention to the potential vulnerability of non-profit organizations to terrorist organizations posing as legitimate entities seemingly devoted to the same cause as the non-profit organization.

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On Oct. 22, 2004, the FATF adopted a Ninth Special Recommendation for countries to more closely monitor cash couriers operating across international borders. Countries should enact measures to detect and stop at the border currency and bearer negotiable instruments that are suspected to be related to terrorist financing or money laundering and adopt measures to address currency or bearer negotiable instruments that are falsely declared or disclosed to authorities.

2012 Recommendations

After a two-year review, the task force issued revised Forty Recommendations on Feb. 16, 2012, into which the Nine Special Recommendations have been incorporated. In its press release announcing the issuance of the revised Recommendations (and Interpretive Notes as necessary),

the FATF stated in part that the “revisions, made with inputs from governments, the private sector, and civil society, provide authorities with a stronger framework to act against criminals and address new threats to the international financial system.”²

The 2012 Recommendations have been reorganized into seven general categories. A discussion of the new categories and the significant additions and revisions of the Recommendations follows below.

Policies and Coordination

An explanation of the general framework of the Recommendations has been moved into a section on AML/Terrorist Financing Policies and Coordination. This section includes a new recommendation that urges countries to take a “risk-based approach” to addressing AML and terrorist financing in a particular jurisdiction. Countries need to thoroughly understand the AML and terrorist financing risks posed in the country, in order to take actions and expend resources that address those risks effectively. For higher risks, more preventive and enforcement measures may be necessary in meeting the intent of the Recommendations. For lower risks, taking a simpler approach to implementing the Recommendations may be warranted. Countries in turn should require financial institutions under their jurisdiction to take a similar risk-based approach.

Confiscation

The Money Laundering and Confiscation section contains and restates the existing Recommendations on criminalizing money laundering and urges passage of legislation that would make it easier to identify, track, freeze, and confiscate the laundered proceeds of crime.

Terrorism and Proliferation

The Terrorist Financing and Financing of Proliferation Section contains all the Recommendations that specifically relate to the financing of terrorists and WMD proliferation. A new recommendation has been added urging countries to implement the targeted financial sanctions passed by the United Nations Security Council resolutions relating to the prevention, suspension and disruption of WMD proliferation.

Preventive Measures

The Preventive Measures Section should be of the most interest to financial institutions. This section consolidates the Recommendations regarding preventive measures that financial institutions (and certain designated non-financial institutions) should take to avoid being conduits for, and being used by people engaged in, money laundering or terrorist or WMD proliferation financing.

The FATF has strengthened the Recommendations in many ways in order to emphasize that countries must take all possible measures to be able to more effectively combat money laundering, terrorist financing and financing of WMD proliferation.

The FATF has strengthened the language in many of the preventive measure recommendations from recommending what the financial institution "should do" to what the financial institution "should be required to do," which appears to raise the Recommendations to a status that would require it being enacted into law or regulation, rather than just being left as regulatory guidance or a best practice. For some countries, such as the United States, many of the actions contained in the Recommendations have long been made mandatory through law or regulation.

Recommendations in which the revised language appears include the following:

- Prohibiting the maintenance of anonymous accounts or accounts held by clearly fictitious persons;
- Undertaking customer due diligence (CDD) in the normal course of establishing or maintaining customer relationships, including verification of identity, and also setting out the circumstances when a financial institution should conduct enhanced CDD of a customer or account such as with international correspondent accounts and foreign politically exposed persons (PEPs);
- Prohibiting a financial institution from having shell banks as correspondents and requiring it to make sure that its correspondents are not using the account at the financial institution to provide services to shell banks;
- Establishing formal programs by financial institutions against money laundering and terrorist financing, both at the financial institution level as well as group-wide for those financial institutions that are part of a group, including foreign branches and subsidiaries of the financial institution.

At the same time, several of these recommendations urge a risk-based approach in taking some of these preventive measures. For example, the requirement to apply customer due diligence measures is tempered by the suggestion that certain elements of the CDD program be applied "as appropriate" after a risk-based analysis.

In addition, the Recommendations address the issue of domestic politically exposed persons and recommend that financial institutions should be required to take "reasonable measures" to identify

customers or beneficial owners who are domestic PEPs or have a prominent function with an international organization and, after appropriate analysis, to decide as to which domestic PEPs enhanced CDD should be applied.

With respect to funds transfers, the Recommendations urge that all agents of money transmitters be included in the money transmitter's AML/terrorist financing compliance programs. In addition, the Recommendations include a requirement that all affected institutions abide by UN Security Council resolutions in freezing and prohibiting transactions designated by the UN Security Council relating to the prevention and suppression of terrorism and terrorist financing.

Transparency

The Transparency and Beneficial Ownership of Legal Persons and Arrangements Section groups together the Recommendations on transparency and accuracy of information maintained by financial institutions, or designated non-financial institutions such as attorneys and accountants, on the beneficial ownership and control of legal persons to avoid their misuse by money launderers or those engaged in terrorist financing.

Powers of Authorities

The Powers and Responsibilities of Competent Authorities and Other Institutional Measures Section consolidates the Recommendations that deal with ensuring that countries have sufficient authority to take effective measures to combat money laundering, terrorist financing and WMD proliferation financing. There are a few new recommendations that are aimed at strengthening the power of the regulatory supervisors and filling in some gaps. These include:

- Urging enactment of legislation to prohibit the establishment or continued operation of shell banks;
- Ensuring that comprehensive supervision on a consolidated basis also applies to group supervision for compliance with AML/terrorist financing purposes;
- In monitoring financial institutions for compliance with AML/terrorist financing, ensuring that the supervisors have the necessary enforcement powers, including the power to withdraw, restrict or suspend a financial institution's license as applicable;
- Ensuring that supervisors have the appropriate powers to impose effective sanctions for failure to comply with AML/terrorist financing requirements;
- Ensuring that supervisors utilize more effective techniques in investigating money laundering and its predicate offenses, and terrorist financing;
- Ensuring that countries maintain effective mechanisms to identify, in a timely manner, and without prior notification to the owner, whether natural or legal persons hold or control accounts and identify assets of interest in an investigation;
- Ensuring that sanctions on financial institutions and other nonfinancial institutions subject to these Recommendations for failing to comply with AML/terrorist financing include the ability to

sanction not only a business but also its directors and senior management.

International Cooperation

The final Section on International Cooperation groups together the Recommendations dealing with international mutual legal assistance, extradition and other forms of legal assistance. The language has been strengthened in the Recommendations to urge that countries have:

- More rapid, constructive and effective measures for dealing with requests for mutual legal assistance, extradition and other international cooperation in relation to money laundering, associated predicate offenses and terrorist financing;
- An adequate legal framework for mutual legal assistance, extradition and other international cooperation;
- Competent financial, human and technical resources, with staff that maintains high professional standards, including confidentiality;
- Authority to take expeditious action in response to requests by foreign countries to identify, freeze, seize and confiscate property that represents the proceeds from money laundering and its predicate offenses, or terrorist financing;
- Effective mechanisms for managing such frozen or seized property and coordinating seizure and confiscation proceedings.

Conclusion

While emphasizing in several places the need for a risk-based analysis, the FATF nonetheless has strengthened the Recommendations in many ways in order to emphasize that countries must take all possible measures to be able to more effectively combat money laundering, terrorist financing and financing of WMD proliferation, whether in the area of closer international cooperation, on the legislative level by tightening the laws on money laundering, at the regulatory supervision level by making sure that supervisors have all tools necessary for effective supervision and enforcement, or at the financial institution level by mandating that they undertake all appropriate due diligence with regard to monitoring customers and transactions. Non-U.S. banks operating in the United States will not only have to comply with any changes in home country law, its U.S. operations also will have to comply with any applicable changes in U.S. laws, regulations or guidance.

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1. All documents referred to in this column are available on the FATF's website at <http://www.fatf-gafi.org>.
2. See http://www.fatf-gafi.org/document/17/0,3746,en_32250379_32236920_49656209_1_1_1_1,00.html.