FURTHER FSA ENFORCEMENT ACTION AGAINST AN MLRO, WHAT NEXT FOR THOSE RESPONSIBLE FOR FINANCIAL CRIME ISSUES?

On 15 May 2012, the FSA announced the imposition of a fine of £525,000 on Habib Bank and a fine of £17,500 on its Money Laundering Reporting Officer ("MLRO") for failing to take reasonable care to establish and maintain adequate anti-money laundering systems and controls.

The decision exacerbates a number of concerns amongst those discharging CF10 and CF11 positions regarding the personal exposure they are taking on, since when one looks back at the FSA's enforcement action to date holding senior management and their firm responsible for regulatory failures, almost all action has been against those in the financial crime space. Frequently those MLRO's who hold only the CF11 function are not "senior management" from a common sense perspective, reporting as they frequently do to others more senior in the organisation. All too often they are having to fight for further resources and there is a growing perception that they are becoming the soft target for FSA enforcement action. The FSA's failed enforcement action against John Pottage demonstrates the difficulties which the FSA has in holding more senior management accountable. We are not suggesting that Mr Pottage did anything wrong, on the contrary. But the case against him was a rare example of the FSA pursuing the head of a business unit for alleged compliance failings. The Tribunal's rightful rejection of that case will cause the FSA to pause before embarking on similar action against another member of senior management. What should not happen, in our view, is for even more focus to fall on those discharging the CF11 function.

However, while MLRO's are in the firing line, we thought it may be helpful to look back over the enforcement actions brought against individuals involved in financial crime prevention and summarise the apparent triggers for that action and the lessons to be learnt. We hope in so doing that this understanding may help to reduce the risks going forward.

In this bulletin we summarise the findings and we recommend referring to the relevant Final Decision Notice for particular issues.

Sindicatum Holdings and Michael Wheelhouse (29 October 2008)

Sindicatum had 35 clients. Its procedures required the MLRO to sign off due diligence checklists. The FSA concluded that the firm and it's MLRO failed to ensure that procedures were followed. Checklists were not fully completed for up to three years, or at all, and the MLRO wrongly gave an exemption for one client.

Whilst the MLRO took advice from outside consultants and took some steps to improve the processes, the findings and recommendations were not followed up adequately. He failed to refer to deficiencies in his MLRO report.

As a consequence, the FSA found that the MLRO had not ensured that the firm complied with the relevant standards and requirements of the regulatory system and was therefore in breach of Principle 7.

Alpari and MLRO (5 May 2010) (Sudipto Chattopadhayay)

The FSA concluded that the following failures occurred:

- the firm failed to carry out risk assessments between 2006 and 2008 and as a result put itself at risk of being used in financial crime;
- the firm failed to carry out satisfactory due diligence and monitor accounts, and failed to implement systems to screen against sanctions lists to determine if customers were PEPs. It had a higher risk model as contact with customers was not face-to-face and the customers were from higher risk jurisdictions;
- the firm expanded the business but did not expand the compliance department;
- the MLRO delegated responsibility to another experienced person and relied upon them;
- the MLRO, despite being aware of growth in the business and potential problems with the AML processes, did not recruit additional staff quickly enough, it took 7 months;
- the MLRO thought the firm was checking for sanctions matches when the firm was not, and when asked the MLRO was confused about the difference between sanctions and PEP risks;
- the MLRO had no input into the MLRO report despite signing off on it;
- the MLRO failed to ensure their instructions regarding training were followed and failed to keep themselves up to date by attending more training.

The FSA concluded that the MLRO was responsible for compliance and oversight and therefore was accountable for the breaches.

Dr Sandradee Joseph and Dynamic Decisions Capital Management Limited ("DDCM") (18 November 2011)

The FSA concluded that the MLRO failed, on becoming aware of facts which suggested that the fund was not complying with its regulatory requirements, to take steps to investigate those concerns. She failed to investigate the reasons why the prime broker terminated its relationship with DDCM or to investigate the concerns raised by investors regarding a bond in which DDCM had invested funds.

Greenlight (27 January 2012)

Alex Ten-Holter, a compliance officer at Greenlight, failed to take steps to satisfy himself that an order to sell was not based on inside information when he was aware that, inter alia:

1. a call with Punch had taken place minutes earlier;
2. he had been told Punch would have told them "secret bad things" if they had agreed to a confidentiality agreement; and
3. after the event, Punch's shares fell, and he did not go back and question it.

As a consequence, it was held that he failed to act with due care and skill in carrying out his CF10 controlled function in breach of Principle 6. He had sufficient information such that he was "on notice" of possible market abuse. He relied on his view that the firm had high standards of compliance and a strict market abuse policy. The FSA concluded that it was inappropriate to assess the risks on that basis as mistakes can be made.

John Pottage (20 April 2012)

John Pottage, former head of the bank's UK wealth division, was found to have failed to properly oversee the business. The FSA concluded that he became aware in the first quarter of 2007 of serious problems in the wealth management business which he inherited. He took steps to improve the position in July 2007, but did not discover a fraud. He failed to instigate a root and branch review sooner. The Tribunal overturned that decision, holding that he had acted reasonably in the steps he had taken. The Tribunal concluded that it was reasonable to delegate to senior staff, i.e., legal/ risk/compliance and provide oversight and challenge only as long as this is evidenced in minutes of relevant formal and informal meetings and any action points are followed up promptly.

Habib Bank and Syed Itrat Hussain (15 May 2012)

Approximately 45% of Habib's customers were based outside the UK and about half of its deposits came from jurisdictions which had less stringent AML requirements, or were perceived to have higher levels of corruption, than the UK. The FSA concluded that Habib failed to establish and maintain adequate controls for assessing the level of money laundering risk posed by its customers, in particular, the high-risk countries with which it dealt. In particular, Habib's high-risk country list excluded certain countries, including Pakistan and Kenya, on the basis that the Bank had offices there. In the FSA's view this did not negate the higher risk of money laundering these countries presented. As MLRO, the FSA held Syed Itrat Hussain held personally responsible for these inadequacies.

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If you have any questions regarding this memorandum, please contact Peter Burrell (+44 207 153 1206, pburrell@willkie.com) or the Willkie attorney with whom you regularly work.

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