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By email: fatf.consultation@fatf-gafi.org

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Dear Luis,

The Wolfsberg Group¹ appreciates the opportunity to comment on the Revision of the FATF 40+9 Recommendations. The consultation process is a testament to the progress made in effective engagement between the public and private sectors in recent years and provides a unique opportunity to enhance the efficacy of AML/CTF efforts as envisaged by the FATF Standards, as well as by the various sets of Wolfsberg Principles and Statements issued since 2000.

Our comments are structured as per the format used in the consultation paper. We note that there are to be two phases of consultation and therefore our comments below apply to the first consultation phase only; we look forward to participating in the future phase also.

SECTION 1: THE RISK-BASED APPROACH

The Wolfsberg Group strongly supports FATF's proposal to develop a single comprehensive statement on the risk based approach (RBA) and commends FATF for continuing its work on the RBA.² An effective RBA brings focused attention to areas of higher risk necessary to facilitate identification of customers and activities that merit additional scrutiny or that are truly suspicious. We welcome FATF's support of this approach by recognising the importance of the RBA in broadening the scope of its applicability to AML.

The comprehensive RBA statement should make clear that the application of the RBA expressly endorses the use of the full range of measures from the most simplified to enhanced controls that reflects risk more accurately. This would help to dispel the confusion that is frequently encountered in this area; a confusion which misguidedly prompts some financial institutions (FIs) to implement procedures designed more to demonstrate the performance of controls to satisfy regulatory mandates but which are largely divorced from effective risk mitigation. Prescriptive check the box requirements should not be the goal of any CDD exercise; the purpose is to manage potential AML risk, using the

¹ The Wolfsberg Group members are Banco Santander, Bank of Tokyo-Mitsubishi-UFJ, Barclays, Citigroup, Credit Suisse, Deutsche Bank, Goldman Sachs, HSBC, JP Morgan Chase, Société Générale and UBS.

² The Wolfsberg Guidance on a Risk Based Approach to managing Money Laundering Risks: <http://www.wolfsberg-principles.com/pdf/risk-based-approach.pdf>

RBA. Policy makers and supervisors, including regulators, should find greater comfort in an appropriate CDD structured on the RBA, as opposed to false comfort derived from simply assessing compliance with prescriptive documentary requirements.

We would, in the same vein, caution FATF not to make recommendations or issue guidance that is too prescriptive with regard to any of the various risk indicators. The power of the RBA rests with its specific application within the unique context of each FI's business. In various parts of the Consultation Paper, we see suggestions that imply prescriptive responses. We believe these would only serve to undermine the effectiveness of the RBA. For example, we see this in the suggestion that all foreign Politically Exposed Persons (PEPs) present a heightened risk. Automatic risk ranking is unhelpful in the identification of risk and inconsistent with the application of a robust RBA as it embeds rote requirements unrelated to any active consideration of the risks that are actually present and leads to an inappropriate allocation of resources. Even with PEPs, discussed more fully below, the risks depend on many factors, such as the type of account, seniority of the PEP and specific country risks.

Again, to the same point, FATF R8 identifies new technology and non-face-to-face relationships as two specific risks demanding special attention. While we agree with FATF's suggestion to separate these two distinct issues and to refocus R8 on new technologies, we ask that FATF nonetheless clarify that the risks of new technology and non-face-to-face relationships are different in different circumstances and emphasise that there is no single process appropriate for all conditions.

Our fundamental observation, of course, is that for every broad, blanket assertion, there is an exception, and, therefore, we strongly support FATF's work to help ensure the adoption of the RBA which recognises the distinctions and allows for targeted, meaningful controls. While the RBA is the best approach to detection of matters that need to be brought to the attention of the authorities, it is understood that no approach will assure a 100 per cent success rate in the detection of all questionable matters and that, if some matters are undetected, that does not invalidate the RBA.

SECTION 2: R5 & ITS INTERPRETATIVE NOTE

Section 2.1 General Comments

The Wolfsberg Group supports changes to R5 and INR5 that endorse a strong RBA focused on "risk variables," allowing for a flexible and non-prescriptive approach to CDD. We further note that an effective RBA recognises that the controls adopted to address risk factors will vary greatly across the wide diversity of financial businesses, products and services. The approach to controlling a common risk factor should not lead to "across the board" requirements mandated throughout the breadth of the industry sector. We support FATF's characterisation of risk factors as just that – factors that should be considered but by themselves, and in isolation, lead to no particular conclusion or mandated process. This explicitly recognises that no single factor necessitates a common response. As the paper says, "ML/TF risks can vary and . . . a 'one-size-fits-all' approach is not necessary." Indeed, we

encourage FATF to go a step further and discourage, with explicit language, a categorical approach as not only unnecessary but fundamentally counterproductive due to its consequence of misallocating resource and focus, which undermines the effectiveness of the effort.

We are committed to the robust application of the RBA as the most effective approach to a thoughtful and productive set of controls within any particular institution. We believe the applicability of the RBA is conceptually and practically the most effective mechanism for creating meaningful and effective controls and that this is true across all risk factors, including how to identify and assess risks related to beneficial ownership.

Section 2.2 Beneficial Ownership

The RBA should be applied to the question of when, whether, in what circumstances and to what level of diligence beneficial ownership should be ascertained. Paragraph 21 of the Consultation Paper strikes us as too prescriptive and too narrowly conceived, and, therefore, would not necessarily add significant value to a range of relationships. We endorse the application of the RBA for relevant beneficial ownership. This would entail a risk analysis that sets out the circumstances and conditions leading to a range of vetting options with respect to the level of ownership, shareholding and managerial control to be investigated, depending on all the risk factors set out within the RBA.

The proposed changes seem to place a specific emphasis on the term “mind and management,” which is a vague concept with different meaning and implications in different contexts and, therefore, difficult to implement across the spectrum of financial services with any semblance of consistency. The concept of “mind and management” will mean different things to different parties in a relationship, causing confusion within and between regulatory expectations and requirements.

We strongly encourage FATF to provide context and descriptive information about the range of risks inherent in the broad concepts of beneficial ownership and relevant control over a relationship in INR5 and to set out in R5 the principle that beneficial ownership and control are factors relevant to certain customer relationships based on the application of the RBA. As the meaning of “beneficial ownership” is dependent on the circumstances, it is not feasible to define this term in the abstract, nor would it be helpful to create new terms that would introduce new definitional issues.

Nonetheless, it is noteworthy that we encounter very different definitions of what is understood by beneficial ownership between regions. This prevents the global application of consistent, institution-wide controls. In particular, we would highlight the example of US legislation FATCA (Foreign Account Tax Compliance Act contained in the Hiring Incentives to Restore Employment Act of 2010), which is scheduled to come into force in 2013 and will have direct effect on FIs globally. The consequences of this legislation, as it is currently enacted, is at variance with the RBA as proposed by FATF in its consultation paper, as it requires far more in-depth and prescriptive KYC and beneficial ownership requirements. In order to be FATCA compliant such a process will, over time, have to be applied to all clients (with the exception of a small threshold of USD 50’000).

In this context, while we fully support FATF proposals moving further towards taking a RBA, including in the area of establishing beneficial ownership, we cannot reconcile this approach for AML with the approach that FATCA takes and the implications for a de facto new global minimum standard for beneficial ownership, which is very prescriptive. Banks are likely to experience significant issues in reconciling the prescriptive provisions of FATCA with the RBA. Therefore, FATF needs to be aware that standards being developed outside of AML, e.g. in the tax area, will have the effect of imposing new global CDD standards (including the identification of beneficial ownership) on banks.

With regard to paragraph 24, we would note that any requirement to take the name of the beneficiaries should exclusively apply to the life insurance company itself. FIs maintaining accounts for life insurance companies should not be subject to such a requirement. "Beneficiaries" and "Beneficial Owners" should not be conflated. When an FI is involved in making a payment to a beneficiary, applicable sanctions screening should be performed, but the beneficiary is not the customer of the FI by virtue of its beneficiary status, and, by definition, Customer Due Diligence would not be appropriate in the context of a non-customer beneficiary.

SECTION 3: PEPs

We believe that the RBA should be applied to PEPs. We disagree with the assertion that all PEPs (whether foreign or domestic) are high risk and note that even PEPs presenting increased risks may not create a high risk relationship if the products and services are inherently low risk. We would refer to the statement made in the Wolfsberg 2008 PEP FAQs, where it was noted that "the greatest risks appear to be present where a PEP seeks to establish a relationship with a Financial Institution beyond the jurisdiction in which they hold the public position that gave rise to the categorisation."³ Generally, though, the majority of PEPs do not abuse their position and will not represent any undue additional risk to an FI solely by virtue of that categorisation.

We would also point out that the categorisation of a client as higher risk is usually not solely due to one criterion but rather tends to be derived from several factors. The 2008 Wolfsberg PEP FAQs indicate that "Financial Institutions should consider a range of factors when determining whether a particular holder of a public function has the requisite seniority, prominence or importance to be categorised as a PEP. Relevant factors could include examining the official responsibilities of the individual's function, the nature of the title (honorary or salaried political function), the level of authority the individual has over governmental activities and over other officials, and whether the function affords the individual access to significant government assets and funds or the ability to direct the awards of government tenders or contracts."⁴

We also note that there remains to this day no universally agreed definition of a PEP, which means that local or regional regulations may differ in respect of particular elements of the PEP definition. The

³ Wolfsberg PEP FAQ's: <http://www.wolfsberg-principles.com/pdf/PEP-FAQ-052008.pdf>

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need for global FIs to consider these differences when determining PEP categorisation standards and relationship management procedures lead us to recommend, once again, that a universally accepted definition be established, reiterating that the notions of the seniority of the politician, the type of account being requested and who controls the purse strings are essential criteria to be taken into consideration.

With respect to paragraph 30, while we support the underlying rationale for reconsidering the standard with regard to family members and close associates, we would nonetheless recommend the application of the RBA to both rather than trying to address this by changing the definition.

SECTION 4: RELIANCE

The Wolfsberg Group strongly supports FATF's proposal to extend the concept of reliance beyond the banking, securities and insurance sectors to include other types of institutions, businesses or professions. This proposal is not only logical and consistent with a robust RBA, but it will also help to increase operational efficiency without increasing risk. We advocate going further and specifically encouraging countries to authorise reliance on entities outside their own jurisdiction where there is supervision and transparency over AML requirements commensurate with their own.

We would refer FATF to our response letter of 9-Nov-09 for a broader discussion of the concepts of reliance. However, in order to delineate better what constitutes third party reliance, we would encourage FATF to adopt the basic premise that for reliance to exist there must be a shared customer between the relying party and the relied-upon party. We would add that a shared customer relationship in this sense does not arise merely because an FI, in acting on behalf of its customers, transacts with another FI.⁵

The Wolfsberg Group supports FATF's proposal to endorse the concept of reliance across branches, majority-owned subsidiaries and affiliates within a financial group, to the extent permissible by the laws and regulations prevailing in the jurisdictions relevant to the relying group party and the relied upon group party.

SECTION 5: TAX CRIMES AS A PREDICATE OFFENCE TO MONEY LAUNDERING

The Wolfsberg Group acknowledges and supports the various international initiatives regarding tax compliance as highlighted at the G20 Summit in Seoul, Korea in November 2010. These include the signing of hundreds of information exchange agreements and the peer reviews conducted under the auspices of the OECD. The Wolfsberg Group encourages FATF members to coordinate and communicate with their national counterparts involved in these initiatives to monitor developments and prevent duplicative or conflicting efforts. As these initiatives reflect, countries are uniquely

⁵ See Q&A 4 of FAQs on Selected Anti-Money Laundering Issues in the Context of Investment and Commercial Banking: http://www.wolfsberg-principles.com/pdf/ibcb_faqs.pdf and Section 4 of Anti-Money Laundering Guidance for Mutual Funds and Other Pooled Investment Vehicles: <http://www.wolfsberg-principles.com/pdf/mutual-funds.pdf>

positioned to address tax compliance, as a cross border matter, on a government to government basis.

Tax compliance is the responsibility of customers. Although FIs should not deliberately market products or services to customers specifically structured to facilitate tax non-compliance, FIs are not (and should not be viewed as being) in a position to confirm the tax compliant status of customers. The role of what FIs can do in this regard, as an AML matter, is limited by the nature of AML programmes: such programmes are intended to identify unusual activity, which, upon further inquiry, could lead to a suspicion of money laundering. In the context of a tax crime predicate -- where the sources of funds may well be legitimate and where the tax laws that apply to customers are varied, extensive, and complex -- FIs will generally not be in a position to identify the tax non-compliance of their customers. Expectations as to what FIs can do should take these realities into account and should not be unduly raised.

When suspicious activity is detected, it should be reported to the governmental agency charged with receiving suspicious activity reports. It would be inconsistent with the obligation to report suspicious activity to require reporting to different agencies on the basis of the FI's assessment of what possible underlying crimes might be generating that activity.

SECTION 6: SRVII AND ITS INTERPRETATIVE NOTE

We are somewhat surprised that a considerable revision to SR VII is being considered as part of the consultation process. The global payments system is a complex structured system created over several decades to ensure consistency, certainty and speed of global payments necessary to the effective operation of multinational businesses. The issues raised in the consultation paper should be considered carefully as to their implications on changes to the payments system that would jeopardise the efficiency of the system.

Current payment industry standards require that, at a minimum, the beneficiary name, Bank Identifier Code (BIC) or other identifier, bank and where available, account number, are required to execute a transfer. The inclusion of additional beneficiary information would be impractical at the point of initiation of a wire transfer, as the originator of a transfer would not usually have information beyond the name, account number and bank. In some instances the originator may be able to provide the address of the beneficiary; however, since this is not usually required, the information may or may not be available. Given the fact that the originator of the transfer usually does not have additional information beyond the minimum required for the transfer, it would not be feasible to require such additional information, nor there any basis for the originating FI to assess the reliability or accuracy of the information.

Requiring any additional information may have differing implications in relation to domestic and international payment systems. Indeed, the addition of national identity number or dates of birth may also have implications with regard to privacy and/or data protection standards, which vary dramatically

between jurisdictions and the requirement to include such information may create significant legal conflicts.

For these reasons, we do not believe that a requirement for additional beneficiary information would be feasible and the requirement for any additional information, while it may be of some limited usefulness, would conversely create significant delays and disruption to the global payments system.

We are generally supportive of a standard that requires institutions to screen all international transfers, even when acting as an intermediary bank. Banks have specific policies and procedures in place for resolving screening hits in conjunction with their risk based approach. Should additional beneficiary information be present or required in a transfer, the methodology for screening or resolving hits would not change from the present approach. As a group, the members of the Wolfsberg Group currently screen information as intermediary banks; however, this may not be the case for all banks.

It should be noted that there is also a differentiation in the requirement for screening in many jurisdictions between domestic and international transfers. In those jurisdictions that require screening, UN sanctions may be included in the screening process. The result of that screening, if positive results are found, would vary based on local law or regulation. Were additional beneficiary information to be required in a transfer, that information would also be screened; however, the screening of this additional information could have a significant effect on compliance and efficiency. It is generally acknowledged that, with the implementation of the MT 202 COV messages, false hit rates increased by about 30 per cent. Furthermore, additional beneficiary information provided by the originator may be unreliable and the originating bank does not have any means to validate that information or ensure that it is complete.

Regardless of the information contained in a transfer, it is difficult to determine if incomplete information is contained in specific data fields. Screening systems scan the information that is present and compare that information to the lists being screened against. Whether information is incomplete cannot be ascertained from the screening process. For mandatory information, systems can determine if information is missing and a transfer would simply not be executed until the required information is obtained.

Should FATF make changes to SR VII, we strongly feel that it is important to provide guidance that is clear and lends itself to uniform adoption. The original implementation of SR VII has, in the past, varied greatly where differing requirements exist between and within jurisdictions creating substantial confusion and disruption to global payments. It would be highly desirable to avoid this confusion in the future by providing more specific guidance related to implementation.

SECTION 7: OTHER ISSUES

While the Wolfsberg Group notes that the revisions in this section pertain largely to financial intelligence units, we would be interested in seeing the final wording of the proposed revisions,

particularly the means by which FATF will seek to make R27 and R28 more effective (paragraph 51) as well as whatever recommendations are issued with respect to the exchange of information between competent authorities as per any future revisions to R40, although we understand that this is at a preliminary stage.

Similarly, although this section relates to international cooperation (mutual legal assistance, extradition, cooperation/exchange of information), we would like to highlight an issue that is particularly relevant to the management of the legal and regulatory risks associated with ML/TF on a global level, i.e. that some jurisdictions do not foresee the possibility of being able to exchange information across a group of FIs (in particular sharing information on SARs, PEPs, etc. with the parent company/headquarters of such a group).

SECTION 8: USEFULNESS OF MUTUAL EVALUATION REPORTS

We appreciate the opportunity to provide feedback on the usefulness of the mutual evaluation reports to the private sector. We are very conscious of the amount of work that goes into the preparation of these reports and appreciate the fact that, once agreed at a FATF Plenary, they are then made available to FIs and indeed the wider public. We applaud the process, which, while taking time, is intended to ensure a level playing field amongst countries and to ensure a satisfactory implementation of the FATF 40+9 recommendations. Indeed we note also that FATF is the sole body producing AML/CTF relevant reports and, as such, these are seen by the public sector as a reference point for the industry, especially in terms of the quality of a country's AML/CTF regime. That being said, however, while the reports provide an interesting commentary on the status and development of a country's compliance with FATF 40+9, their practical usefulness for FIs in terms of incorporating these reports into their operational processes is limited.

The challenge for FIs rests in how to interpret the content of these reports, what weight to place on them and how best to incorporate the information and/or the overall results into FI risk ratings, particularly country risk ratings, when the reports have not been produced or designed for this specific purpose. Furthermore, it should be noted that, while Country Risk is a significant component of an FI's overall RBA, particularly as it relates to, and interacts with, customer risk, the information in the Mutual Evaluation Reports cannot have the same utility as indices ranking countries such as, for example, a publicly available country corruption index. Moreover, unless MERs include focused money laundering risk assessments for that country (which go beyond an assessment of the country's compliance with 40+9), preferably with clear ratings and a transparent methodology, issued in a timely fashion and regularly updated (e.g. annually), and unless this process is carried out for all countries (not just FATF/FSRB members), then the reports, as currently issued, can only be used for more general educational and background purposes.

In addition to the release of MERs, it has become a practice for FATF to name (and shame) a limited set of countries which are deemed to demonstrate strategic AML/CTF deficiencies. There appears to

be a specific approach as to why countries are listed, but we are not aware of any methodology that is available by which the rating can be validated or understood beyond the short commentary accompanying the release. While the regularity with which these lists are published falls more in line with FI requirements for timeliness in regard to country assessments, it remains the case that there is no consistency as to how to interpret the ratings (due to lack of clarity around the criteria resulting in their being assessed in the first place) or what the consequences on country risk assessment should in fact be. As already suggested at the FATF Consultation Forum in September 2009, it would be beneficial to issue some guidance around how these countries come to be assessed and what actually qualifies them as being deficient.

Financial Inclusion

As private FIs competing globally for customers, we welcome this initiative which recognises that a substantial number of persons find some difficulty in gaining access to bank services. One reason for this includes the challenges for some prospective customers in providing acceptable identification documentation and the inability of firms to verify such information in accordance with FATF standards. In trying to reconcile these competing public aspirations (financial inclusion and rigorous AML standards) we would be concerned if the standards to be applied to those currently operating outside the formal regulated sector were unduly weakened for the sole purpose of bringing them into the formal regulated sector. Should the current framework be adjusted in line with the proposed changes with respect to the RBA and R5, this should be sufficient to address and satisfy both aspirations.

We are grateful to have had the opportunity to comment on the proposed revisions to the recommendations and remain at FATF's disposal should any clarification with respect to the above be required. We also note that there are some issues under consideration which may require some highly technical or specialised input, which, if we are able to do so, we would be happy to provide more targeted support on, as FATF pursues its review process.

Yours sincerely,

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