



The Secretary to Parliament
C/O Mr. Bradley Viljoen
Committee Section
Parliament of the RSA
P.O. Box 15
CAPE TOWN
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30 April 2008

Dear Sir

FINANCIAL INTELLIGENCE CENTRE AMENDMENT BILL, 2008

I refer to the invitation to submit written representation on Financial Intelligence Centre Amendment Bill, 2008 (the Bill) to the Secretary to Parliament.

It is noted that the commentary set out below is focussed on the compliance implications of the Bill and on considerations relating to compliance officers in particular. This is based on the writer's compliance experience and on the broad understanding he has gained through the provision of consulting services to a wide range of accountable institutions.

We acknowledge the important contribution that the Financial Intelligence Centre Act makes in the control of money laundering and terrorist financing. South Africa cannot afford to lose the fight against crime and enhancements to the regulatory requirements will play a pivotal role in this regard.

1. Introduction

The impact of the Amendment Bill on Compliance Officers should be seen in the light of the existing Financial Intelligence Centre Act requirements contained in section 43. These will become increasingly important from a compliance officer responsibility viewpoint in the light of the introduction of administrative sanction.

2. Compliance Requirements – Section 43

The following is stated in section 43 (training and monitoring of compliance) of the Financial Intelligence Centre Act:

“An accountable institution must-

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- (a) *provide training to its employees to enable them to comply with the provisions of this Act and the internal rules applicable to them;*
- (b) *appoint a person with the responsibility to ensure compliance by-*
 - (i) *the employees of the accountable institution with the provisions of this Act and the internal rules applicable to them; and*
 - (ii) *the accountable institution with its obligations under this Act.”*

The aforementioned provisions specifically require that accountable institutions must “appoint a person with the responsibility to ensure compliance”. This provision raises a number of significant concerns in view of the requirements contained in section 45C, most importantly from a compliance officer responsibility perspective.

It is general practice for accountable institutions to appoint a compliance officer often termed the Money Laundering Control Officer (MLCO). However, one of the cornerstones of establishing an appropriate compliance officer responsibility profile within an organisation is to recognise that compliance officers are not responsible for “ensuring compliance”, i.e. management is responsible for conducting all business activities in compliance with laws, rules and standards (management is in a position to ensure compliance) and the compliance officer’s role is to assist management in this regard.

This responsibility profile is reflected in the guidance that has been published by the Basel Committee on Banking Supervision in a publication entitled Compliance and the Compliance Function in Banks, April 2005.

“Principle 7: Compliance function responsibilities

The responsibilities of the bank’s compliance function should be to assist senior management in managing effectively the compliance risks faced by the bank. Its specific responsibilities are set out below. If some of these responsibilities are carried out by staff in different departments, the allocation of responsibilities to each department should be clear.

34. Not all compliance responsibilities are necessarily carried out by a “compliance department” or “compliance unit”. Compliance responsibilities may be exercised by staff in different departments. In some banks, for example, legal and compliance may be separate departments; the legal department may be responsible for advising management on the compliance laws, rules and standards and for preparing guidance to staff, while the compliance department may be responsible for monitoring compliance with the policies and procedures and reporting to management. In other banks, parts of the compliance function may be located within the operational risk group or within a more general risk management group. If there is a division of responsibilities between departments, the allocation of responsibilities to each department should be clear. There should also be appropriate mechanisms for co-operation among each department and with the head of compliance (e.g. with respect to the provision and exchange of relevant advice and information). These mechanisms should be sufficient to ensure that the head of compliance can perform his or her responsibilities effectively¹.”

¹ Basel Committee on Banking Supervision - Compliance and the Compliance Function in Banks; April 2005; page 13.

The above is aimed at banks. However, the principles contained therein will be applicable to other organisations. This is supported by the following specifications which are contained in the Compliance Institute of South Africa's Generally Accepted Compliance Principles, Codes, Standards and Guidelines:

"The primary role of the compliance function is to assist Management in discharging their responsibility to comply with applicable Regulatory Requirements, through the provision of Compliance Risk Management services.²".

It is noted that section 43 does not address the compliance contributions that can be made by other role players. By way of illustration, the wording contained in section 43 is framed in a manner which is fundamentally different to the compliance responsibility requirements contained in regulation 49 of the Banks Act, 1990, which specifically recognises important governance dynamics relating to the role played by management and other stakeholders.

Although section 43 is headed "training and monitoring of compliance" no reference is made to compliance monitoring in the provisions contained therein. This is not, in itself, a significant concern in that compliance officers would, in terms of generally accepted standards be expected to monitor compliance. However, the inclusion of the word "monitoring" may be an indication of the intention behind the drafting of the said section.

3. Administrative Sanction

The introduction of "administrative sanction" in terms of section 45C will have a significant impact on the regulatory exposure of accountable institution and reporting institution stakeholders.

The contents of section 45C(1) are set out below for ease of reference:

"The Centre or a supervisory body, despite the provisions of sections 46 to 66 and irrespective of whether criminal proceedings in terms of this Act have been or may be instituted, may impose an administrative sanction on any accountable institution, reporting institution or other person to whom this Act applies pursuant to an inspection or when satisfied on available facts and information that the institution or person –

- (a) has failed to comply with a provision of the Act;*
- (b) has failed to comply with a condition of a licence, registration, approval or authority imposed in accordance with section 45(1A)(f);*
- (c) has failed to comply with a directive issued in terms of this Act; or*
- (d) has failed to comply with a non-financial administrative sanction imposed in terms of this section."*

² Compliance Institute of South Africa - Generally Accepted Compliance Principles, Codes, Standards and Guidelines; August 2007; Principle 7.

The need for administrative sanction is understood in that the criminal sanction route (the option contained in the Financial Intelligence Centre Act) is time consuming, costly and not always practical.

However, in view of the significant impact of the Amendment Bill's administrative sanction specifications on accountable institutions, reporting institutions and other persons, it is essential that there is clarity relating to important sections of the Financial Intelligence Centre Act, the regulations thereto, guidance notes and directives. Importantly, this is needed in the light of the rules based approach that has been adopted in the drafting of the Financial Intelligence Centre Act regulations, which provides for limited discretion in the application of internal rules in meeting the regulatory requirements, notably in respect of client identification and verification.

4. Impact of Administrative Sanction

The comments set out below are focussed on the impact of the requirements on compliance officer's responsibility profile.

As specified in section 45C(3):

"The Centre or supervisory body may impose any one or more of the following administrative sanctions –

- (a) a caution not to repeat the conduct which led to the non-compliance referred to in subsection (1);*
- (b) a reprimand;*
- (c) a directive to take remedial action or to make specific arrangements;*
- (d) the restriction or suspension of certain specified business activities; or*
- (e) a financial penalty not exceeding R 10 000 000 in respect of natural persons and R 50 000 000 in respect of any other legal person."*

The aforementioned provisions will apply to any:

- *Accountable institution;*
- *Reporting institution, or*
- *Other person to whom this Act applies."*

Although, in practice, the focus of any caution, reprimand, directive, restriction, suspension, or financial penalty will typically be on the accountable institution or reporting institution itself, these will also apply to management and employees.

Specifically, compliance officers will be directly impacted. In terms of section 43 of the Financial Intelligence Centre Act, accountable institutions must "appoint a person with the responsibility to ensure compliance".

It is argued that, if a compliance officer is responsible for compliance, moreover management's compliance, then when management does not ensure compliance, regardless of the responsibilities discharged by the compliance officer, the

compliance officer will, in the light of the requirements of section 53, be held to account for management's compliance.

This logic, if applied, would be fundamentally flawed and out of line with international standards.

It is submitted that the encouragement of a so-called "scapegoat" approach to complying with the Financial Intelligence Centre Act requirements, as highlighted above, will not serve the interests of counter money laundering and terrorist financing.

It is conceivable that a compliance officer that has appropriately advised management on the compliance with laws, rules and standards and has prepared guidance to staff, monitored compliance with the policies and procedures and undertaken reporting to management and substantially discharged all applicable responsibilities, could be exposed to administrative sanction.

Where there exposure to compliance officers is raised to the level that good candidates are no longer prepared to accept the responsibility imposed, this will be counterproductive.

5. Suggested Changes to Section 43

In view of the commentary set out above, the following suggested changes are, in good faith, put forward for consideration.

An accountable institution must-

- (a) provide training to its employees to enable them to comply with the provisions of this Act and the internal rules applicable to them;*
- (b) appoint a person with the responsibility to assist management in discharging their responsibility to ensure compliance by the accountable institution with its obligations under this Act through the provision of monitoring and other compliance services.*

The above suggestion specifically refers to the monitoring aspect of the compliance process, which, in terms of the Compliance Institute of South Africa guidance is made up of four phases, i.e. compliance risk identification, compliance risk assessment, compliance risk management and compliance monitoring.

If needed, the governance considerations relating to the aforementioned could be addressed in the regulations. It is critical that any specification in this regard should be appropriate from a good corporate governance perspective, i.e. taking into account leading practice in view of the South African circumstances. The consideration of specific requirements that may be appropriate for different types or size of organisation may add value in this regard.

6. Clarity Relating to Certain Regulatory Requirements

Based on the writer's experience, there are a number challenges in the interpretation of various Financial Intelligence Centre Act requirements, i.e. from a practical application perspective.

It is submitted that, in view of the significant costs relating to compliance with the Financial Intelligence Centre Act requirements, this is an extremely important consideration. These costs are, to a significant extent, driven by the volume of accounts and transactions. It is evident that a relatively small increase in unit costs (relating to accounts and transactions) could, in a high volume environment, result in relatively high global costs.

Examples of provisions that require clarification, which have a potential high cost impact, include the retention of documents used for customer identification and verification purposes and the documentation standards relating thereto, for instance in respect of the status of copies (most importantly in respect of accountable institutions not impacted by Guidance Note 3).

In an environment of regulatory uncertainty, a compliance officer's regulatory exposure will be significantly increased where administrative sanctions are introduced – Amounting to R10m plus non-financial sanction.

Clearly, the exposure of other stakeholders will also be increased.

The cost of compliance could be significantly increased through the application of the new enforcement and other measures. The Amendment Bill does not specify governance considerations that will be applied in this regard.

7. Review Mechanism

In view of the impact that the Financial Intelligence Centre Act has on accountable institutions, it is suggested that there should be a robust mechanism to review the effectiveness of the requirements that are imposed and to determine whether the regulatory objectives are being efficiently achieved.

The the addition of the paragraph 4(e) refers. Where this is effectively implemented with input from public and private sector stakeholders, it will add value to the South African counter money laundering and terrorist financing framework.

8. Conclusion

Compliance officers play a key role in assisting organisations to comply with the requirements of the Financial Intelligence Centre Act. The introduction of the Amendment Bill will significantly impact the level of regulatory exposure faced by them, which would be counterproductive in the South African commitment to combat money laundering and terrorist financing.

Changes to section 43 of the Financial Intelligence Centre Act, as suggested above, will go some way to addressing concerns that are evident. It is also important to address challenges relating to clarification of certain Financial Intelligence Centre Act requirements as well as the responsibility profile of stakeholders.

Yours sincerely

John Symington
Director