

Financial Services and Markets

First FSA Enforcement Action Against MLRO

FSA fines corporate advisory firm and its MLRO for failures in anti-money laundering systems and controls.

Background

The Financial Services Authority ("FSA") has fined Sindicatum Holdings Limited ("SHL") £49,000 and its money laundering reporting officer ("MLRO"), Michael Wheelhouse, £17,500 for failing to have adequate anti-money laundering controls in place. It is the first time the FSA has fined a money laundering officer.

SHL is a London based corporate advisory firm which, during the relevant period (October 2003 to September 2007) was engaged in investment business with only 26 clients (predominantly small and medium corporate firms based overseas). Mr Wheelhouse jointly founded SHL and, as the firm's MLRO, is an approved person.

Comments

The FSA said that the "nature, extent and potential implications" of SHL's failures merited the financial penalty. However, what is notable about this enforcement action is that SHL had comparatively few clients (26) and half of those were identified adequately. The remaining 13 clients were in higher risk jurisdictions and the customer due diligence failures obviously breached clear guidance given in the JMLSG Guidance Notes - in percentage terms, therefore, the failures related to a significant number of the firm's small client base. As with previous AML enforcement actions, the FSA found no evidence that money laundering had actually taken place - the issue related to the failure to implement adequate systems and controls.

The action against Mr Wheelhouse serves as a warning to a large number of MLROs in small to medium sized firms - the failure to implement adequate controls is unlikely to be tolerated by the FSA in any circumstances but the regulator was undoubtedly even less tolerant given the relatively small number of clients needing identification and the long period of time over which the failures persisted.

One passing comment in the Final Notice against Mr Wheelhouse is of particular concern. As outlined below, Mr Wheelhouse had erroneously applied an exemption in relation to a Lithuanian bank. The FSA notes that on this occasion Mr Wheelhouse acted as the account executive collecting the identification evidence and also as the officer reviewing and signing off the account (a practice which must surely be necessary in many small firms with limited personnel). The FSA comments that "such an arrangement decreased the likelihood of this failure being identified". While this point was not central to the FSA's findings, it is worrying to see the regulator impliedly suggesting some kind of "four eyes" principle in this context - after all, Mr Wheelhouse was the MLRO, who had oversight responsibility, and it was he who made the mistake. Although a firm must have effective systems and controls for countering the risk of financial crime and the MLRO must have a level of independence, there is no explicit requirement in SYSC or in the JMLSG Guidance Notes to ensure that the activity of data collection and the activity of review and sign off must be performed by different individuals.

What is clear from the two cases is that the FSA is prepared, in its pursuance of its policy of "credible deterrence", to make examples of small firms and individuals as a warning to the industry as a whole.

FSA's findings

- **Failure to implement adequate AML and client identification procedures**
 - Although SHL had anti-money laundering and client identification procedures set out in AML Handbooks produced by an external consultant (which were presumably considered to be adequate by the FSA) there was no process to ensure that the procedures were followed in practice and they were consequently not fully implemented (see below).
 - SHL had also failed to follow up on issues raised by the external consultant in its quarterly reviews of SHL's procedures.

- **Failure to verify identification of a significant number of clients**

- Of the 26 clients, 13 were low risk and SHL's identification of these was appropriate. The remaining 13 clients were higher risk, being incorporated in "less transparent jurisdictions" (Lithuania, Slovenia, Russia and Hungary are mentioned in the Final Notice). In relation to these 13 clients SHL had not obtained sufficient evidence to verify their identity. The FSA highlighted the following failures:
 - In the case of 3 clients identification evidence was not obtained at the time of client take on - in one case evidence of an individual's address was not obtained until 4 years later;
 - SHL accepted information concerning directors, beneficial owners or controllers from the individuals themselves, rather than obtaining evidence of those matters from independent sources;
 - Company and personal documents obtained by SHL were, in some cases, in foreign languages and there was inadequate evidence to demonstrate that these documents, or translations, of them had been adequately reviewed by the MLRO in order to confirm their contents; and
 - SHL accepted photocopies of identification documentation which were not certified as being true copies of the originals.

- **Failure to keep adequate records**

- In a small number of cases, SHL's records indicated that verification checks had been carried out on clients but the relevant documentation was missing from the client files; and
- Client acceptance checklists (required by SHL's procedures) were not fully completed by account executives or the MLRO for some considerable time or, in some cases, were not completed at all.

- **MLRO's failures**

- As MLRO Mr Wheelhouse was responsible for implementing and monitoring the effectiveness of SHL's AML procedures and controls. The FSA found that he should have been aware of the firm's failings as outlined above and in particular:
 - He failed to ensure that client checklists were fully completed - and he did not report this failure in any of the MLRO reports he made to the SHL board;
 - He failed to ensure that all client acceptance checklists were completed; and
 - He failed to comply with his obligations as MLRO and with the firm's procedures - an example the FSA gives is that of Mr Wheelhouse applying an exemption from identification in relation to a deposit-taking bank in Lithuania, despite Lithuania not appearing on the "equivalence" list for regulated entities.

Further information

The FSA's enforcement notices in relation to both SHL and Michael Wheelhouse can be found at the following web links:

<http://www.fsa.gov.uk/pubs/final/sindicatum.pdf>

<http://www.fsa.gov.uk/pubs/final/m-wheelhouse.pdf>

If you would like further advice on this issue please contact Margaret Chamberlain in the Financial Services and Markets Department or your usual contact at Travers Smith.

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