AML Program Effectiveness: Sufficiency of Resources

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When it comes to penalty actions that include insufficient resources, one of the first questions the average AML compliance officer should ask after reading a recent case is: "Is this us?" The usual reaction is somewhere between, "I hope not" and "Gee, I'll have to check that out." And then it goes on the back burner because, really, who has time to read? He/she is already too busy trying to keep up with AML program demands. This article discusses enforcement actions directed at failure to provide sufficient resources for the operation of firms' anti-money laundering programs.

Penalty Actions

Recent enforcement cases have cited insufficient resources, thus bringing an important issue to the forefront, and not for the first time. Allocating adequate resources to critical AML functions is paramount to ensure internal controls are working as designed, contributing to an effective AML program.

In the recent case with a penalty of $8 million against Raymond James,[1] FINRA cited that the firm did not dedicate enough resources to match its growth with reasonable compliance systems and procedures, and relied on a patchwork of written procedures and systems across different departments to detect suspicious activity. Systems and procedures weren't coordinated to effectively link patterns and trends, leaving risk areas and red flags unchecked. The firm failed to conduct due diligence and periodic risk reviews for its foreign financial institutions (FFIs), and failed to maintain an adequate Customer Identification Program (CIP), which is one of the easier functions to manage. Also included in the action was a Section 5 citation, for transactions involving low-priced securities. Many firms and compliance officers don't understand the connection between Section 5 (of the Securities Act of 1933) and AML. Like other higher risk products and services, low-priced securities require effective supervisory controls to ensure compliance, as discussed in SEC risk alert[2] and FINRA Regulatory Notice 09-05.[3]

In another case with a penalty of $16.5 million against Credit Suisse,[4] the bank failed to commit the necessary resources to adequately surveil

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potentially suspicious trading and money movements over a four-year period. The bank relied primarily on its monitoring system without considering that human resources are required to evaluate what the system was flagging for review and, because of its shortage of staff, the firm failed to investigate. In this action, we see the same Section 5 and due diligence issues we saw in the Raymond James case. Where staff actually reviewed the trading activity, it failed to review for AML purposes. The bank also neglected to properly calibrate thresholds that it set for certain scenarios, to ensure quality alerts were raised. The firm also failed to test the AML monitoring system (independent verification and validation audit). As result, the bank failed to investigate trading adequately to determine if SARs should be filed.

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Worth mentioning is that remediation of a penalty action may cost the firm six times the cost of the fine itself. Adding a few full-time employees (FTEs) seems like a no-brainer when you look at it from a monetary standpoint.

How to Determine Sufficiency of Resources

So how should you confirm whether resources in your firm are, in fact, sufficient? If you can keep up with the many tasks required to maintain an effective AML Program, then you likely have sufficient resources. If you find yourself trying to keep up, yet always behind the curve, then take heed. Perform a risk assessment of the AML program, and document your findings. This will serve as an aid to a staffing analysis and a document to bring to the board or to senior executives for review and consideration. Remember, the board owns the AML risk at the firm. Therefore, it is in their best interests to implement a sound and effective program.

Your first resource is your risk assessment. Performing a risk assessment will lead you to know where you need resources and why. If you don't already have a risk assessment, then it's time to create one using the many resources available to you through your AML networks or the internet. If all else fails, engage a third party expert to assist you. Notice I said "assist you." Third parties can't do it without you, as they don't know the specifics of your business model. However, if you work together, you will go a long way toward developing a risk assessment format with metrics that you can update year after year, and align to your policies and procedures.

An important resource for guidance is the Federal Financial Institutions Examination Council (FFIEC) BSA/AML Examination Manual[5] which describes the many aspects of assessing risk. Additionally, a sample Quantity of Risk matrix is available[6] to guide you further.

The risk assessment carves out the many risk factors your firm faces in its day-to-day AML compliance operations. It aides in assessing both the quality and quantity of risk so that you may design proper controls to mitigate your risk and that which you will manage on a day-to-day basis. It can help you to determine where you have shortages in resources – and not just human. For example, firms that don't have automated systems will instead have a set of processes that form a manual system of checks and balances, requiring more human resources to manage the program. Firms with automated systems must also have qualified staff to interpret the outputs from the automated system. Either way, humans are required.

Identify the number of high risk customers in your portfolio, as they all require enhanced due diligence and periodic risk-based reviews, as do correspondents and foreign financial institutions (FFIs). Review the geographic locations where your firm transacts business, particularly countries where there may be heightened risk. And with regard to OFAC – perform an analysis of how many false-positives you clear each month. Determine the man-hours needed to perform clearing of alerts. These functions must be reviewed and validated by qualified personnel. Don't forget your automated systems' alerts – as they may lead to investigations and suspicious activity reports (SARs), all of which take time. You need qualified and skilled personnel to perform these critical tasks. It's endless, which is why it is so important to know where you need resources. Assessing your risk will help you to do that.

Look at your last independent review. If your provider is an industry expert, then the report should cite any violations or deficiencies, and/or include recommendations for improvement. Were there any exceptions in CIP/KYC, enhanced due diligence (EDD) investigations, suspicious activity reports (SARs), and wire transfers? Exceptions typically reveal that additional staff training is needed because personnel don't fully complete their oversight tasks, or personnel are rushed and miss key elements in completing the task correctly because they are covering too many critical tasks.

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If you are having issues such as the ones in the previous paragraph, you likely need to implement a quality assurance/quality control function until you get it right, and that too requires hours to complete. If your reviews and exams cite repeat findings, then you likely have systemic issues – often caused by inadequate human resources and inadequate training of those resources. If your FINRA examination has cited AML items more than once, you will be identified as a recidivist, and FINRA may charge you a larger penalty.

Look at your CIP/KYC. Are you timely collecting all your documentation? How many hours per day are focused on CIP/KYC and what are the quality assurance controls associated with the function? What of transaction monitoring alerts – approximately how many alerts appear per week and how many hours does it take to clear them? How many move to investigation and how many hours does it take to investigate cases, regardless of whether they result in a SAR filing.

If you already have a risk assessment, carve out a section for AML Personnel and identify how many resources are applicable to the critical functions and tasks. Assessing the hours required to effectively complete all BSA/AML/OFAC tasks and calculating that against the number of full time employees ("FTEs") assigned will assist you in assessing staff sufficiency and any shortage. You likely already know who your most valuable personnel are – those who are most efficient and effective. It has been my experience that institutions always have a team that includes staff who are painstakingly effective but not very fast, and those who are productive but maybe not so fussy in getting it perfect every time. This can be a healthy balance in any institution, but always strive for effectiveness. Periodically perform quality control reviews to ensure personnel are adequately trained in their tasks.

Approximate your needs and then compare them to your current personnel. Consider the overall skill-set while you're at it. Do you have a good mix of skills? Do you have all the functions you need, such as CIP/KYC specialists, those who understand your AML monitoring system, investigators who love to dig into transactions until exhaustion, quality assurance and quality control functions to be sure you're doing it right, and good training for each function? Then, create a memorandum document outlining your findings identified in categories. First, list the critical functions (high risk) and assign the approximate number of hours needed to complete the work in each category. Be sure to allow for part timers and floaters supporting your department. Don't forget to account for personal time off, as you need to fill gaps when staff are on holiday.

Finally, what happens when a small firm relies on one person to take on multiple responsibilities? Simply put, you must hire more qualified staff. It's the cost of doing business. And if you're a mid-size firm, with senior management stubbornly not allowing additional hires for compliance? Gone are the days when a firm can say, "...we just don't have the budget." In the AML world, that is not acceptable. AML compliance is here to stay, so make the investment now, before you have to write a check to FINRA.

ENDNOTES

1 http://www.finra.org/sites/default/files/RJFS_AWC_051816_0.pdf
2 https://www.sec.gov/about/offices/ocie/broker-dealer-controls-microcap-securities.pdf
3 https://www.finra.org/file/regulatory-notice-09-05
4 http://www.finra.org/sites/default/files/CreditSuisse_AWC_120516.pdf
5 https://www.ffiec.gov/bsa_aml_infobase/pages_manual/OLM_005.htm
6 https://www.ffiec.gov/bsa_aml_infobase/pages_manual/OLM_110.htm