

5 Questions...

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NEW FEATURE!

5 Questions seeks out experts in their respective fields to answer...well, five questions on topics of importance to securities industry professionals in the field of compliance and regulation...

Anti Money Laundering

1) Based on a review of recent rulemaking activity and enforcement actions, what's new and different in the world of AML?

There's been an increase in the numbers of cases involving BDs failing to respond to red flags indicating suspicious activity with regard to unregistered sales of securities or manipulative trading activity. If surveillance systems focus solely on monetary transactions and ignore potentially problematic securities activities, the firm leaves itself open to potentially severe regulatory sanctions.

2) Firms are required to conduct an annual "independent" review of their AML compliance program -- what should they be looking for in an independent examiner?

The examiner must be familiar with and have a working knowledge of all applicable regulations. Ideally the examiner should be completely independent i.e., an individual or entity not employed by or otherwise affiliated with the firm. The results of the review should be reported to an individual at the firm who is senior to the AMLCO. The review may also be conducted internally provided certain conditions are met (see FINRA IM 3011-1).

This edition: Eric Smith on AML

Our guest is Eric Smith. Eric has been a compliance professional for more than 24 years with firms such as Sutro & Co. Inc., RBC Dain Rauscher and, most recently, as Chief Compliance Officer at a San Francisco based investment advisor. He is currently an independent compliance consultant specializing in trading, surveillance and Anti-Money Laundering issues...



5 Questions: Anti Money Laundering (cont.)

3) "Suspicious activity" seems to be such a broad and subjective term -- how does a firm distinguish activity that qualifies as "suspicious" from accepted business practices in a multi-polar global economy?

There is no easy answer and there has been very little regulatory guidance (other than through enforcement) as to precisely what is "suspicious" and what is not. Often an individual transaction – taken alone – may appear on the surface to be legitimate, but when viewed in the context of other activity in the customer's account(s) may be suspicious.

Larger firms generally have sufficient IT resources to develop sophisticated algorithms to detect unusual activity that may be outside the normal pattern for a particular client, or activity that simply seems to lack business sense. Smaller firms typically rely primarily on exception reports provided by their clearing firm, which are often rudimentary, thus a more hands-on approach may be necessary.

A "best practice" would be to have a fully trained AML staff, independent of the firm's business units, with sufficient resources and authority to conduct objective reviews and to take appropriate action where indicated.

4) What is an AML compliance program required to have?

Each firm must designate an individual primarily responsible for AML compliance (the "AMLCO"). An AML plan must also include procedures for compliance with each of the following elements:

- review and response to FinCEN information requests
- sharing information with other financial institutions
- customer identification and verification (including obtaining certain required information for each customer)
- conducting OFAC screening of new and existing clients
- providing written notices to customers regarding the firm's AML program
- detecting and closing certain foreign accounts (foreign "shell banks")

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- obtaining periodic certifications from foreign banking clients
- detecting and monitoring accounts for foreign "private banking" clients and "politically exposed persons"
- the methods to be employed in the firm's ongoing surveillance program
- suspicious activity ("SAR") reporting
- monitoring currency transactions and filing appropriate reports
- recordkeeping
- continuing education for all of the firm's employees
- annual independent testing of the firm's AML practices and procedures

THE SUTRO GROUP LLC

P.O. Box 29025
San Francisco, CA 94129

Phone: 415-888-8055
Fax: 415-380-7964



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www.thesutrogroup.com

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5 Questions: Anti Money Laundering (cont.)

5) Small firms with limited resources are often hard pressed to comply with burgeoning AML regulatory requirements. What do you recommend as far as resources to assist firms in complying with these rules?

Education, education, education!! Consistent and thorough continuing education on these issues should be administered to EVERY employee of the firm (not just the AML folks) and each should be made aware of how to identify and report suspicious activity.

Firms should also ensure that their contractual arrangement with their clearing firm clearly articulates the division of AML responsibilities.

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