



AML and Compliance



The Koger Roundtable on AML and Compliance was held against the background of the implementation of the Third EU Money Laundering Directive into law in Ireland. The EU Directive 2005/60/EC on the 'Prevention of the use of the Financial System for the Purpose of Money Laundering and Terrorist Financing' (the Third Directive) was introduced to prevent abuse of the financial system for money laundering and terrorist financing. The Third Directive also widens the scope of previous anti-money laundering legislation, based on the Financial Action Task Force's (FATF) revised 40 recommendations. The Third Directive aims to update European legislation in line with international law, ensuring the FATF recommendations are applied consistently across the European Union member states.

In Ireland, the Criminal Justice (Money Laundering and Terrorist Financing) Bill 2009 has been published in respect of the of the Third Directive's implementation. The Criminal Justice Bill creates a larger definition of money laundering by:

- Introducing definitions for Politically Exposed Persons (PEP) and Beneficial Owners
- Providing more specific and detailed provisions on customer identification, particularly with trusts, company service providers and non-listed companies.
- Requiring Fund Administrators to perform customer due diligence (Know-Your-Customer or KYC) on a risk-sensitive basis.
- Requiring special procedures where a PEP or a family member/business associate of a PEP of a PEP proposes to invest in a fund.

AML – EU Third Directive

The Criminal Justice (Money Laundering and Terrorist Financing) Bill 2009 ("Bill") was introduced in July 2009 in order to implement the Third EU Money Laundering Directive ("Directive") into law. It has just passed the Committee stage and been sent to the Seanad for approval.

The Roundtable attendees, in general, felt positively about the Directive's implementation. Attendees felt that it gave them more flexibility when requesting KYC documentation. The Directive allows for leniency in certain circumstances (e.g. the case of a fund employee who is known to the fund administrator) while requiring enhanced documentation for perceived high-risk investors.

The new bill requires Fund Administrators to score investors' risk levels based upon investor type, country of origin, and initial subscription amount. There will be three risk levels: low, medium and high. Investor risk levels may change based on investment activity in their account (e.g. churning), or if it is determined that an associated party to the investing entity (e.g. a director) is found to be a Politically Exposed Person ("PEP").

There will then also be three sets of documentation required:

- Simplified (e.g. for a fund employee)
- Standard (e.g. for a vanilla investor)
- Enhanced (e.g. for PEPs/ investors classified as high risk)

Under the Directive, Fund Administrators are required to perform continuous due diligence. Previously, AML checks were performed when an investor entered the fund. Now, administrators must perform checks on a regular basis. AML check frequencies will depend on the risk levels noted previously. For example, an investor classified as low risk will be subject to fewer due diligence checks than a high risk investor over the same period.

An increasing KYC/ AML necessity for fund administrators is the ability to track underlying beneficial owners (UBOs). These underlying beneficial owners are subject to the same rigorous due diligence as the investing entity.

Regulators have yet to provide firm guidelines about Source of Wealth verification. This is now a requirement under the Bill when dealing with PEPs. The information we have received indicates that letters of comfort from banks in non-prescribed countries would not be sufficient to satisfy Source of Wealth verification requirements.

Fund administrators have eagerly awaited global Directive implementation, especially UK based fund managers who have been under Directive guidelines since 2007. Attendees are now simply waiting for full Directive implementation; processes and procedures have been reviewed and changes made, if not implemented, in anticipation of the Bill becoming law.

Suspicious Transactions

The discussion on suspicious transactions highlighted how difficult suspicious activity is to monitor and how this process's steps have to be performed manually. There was a general consensus on the types of transactions/ activities that attendees monitored - three main themes arose from the discussion:

- Suspicious transactions (mostly surrounding transfers and redemptions)
- Irregular account activity
- Static data changes

It was also noted that while some 'rules' about account churning (e.g. two subscriptions and one redemption in a two month period) may identify irregular activity in some funds, as the industry moves towards funds with higher volumes and regular cycles, these 'rules' may become invalid. A further impact of these products is that the time frame within which to identify and report a potential suspicious transaction is shortened.

The roundtable discussion identified several challenges when identifying suspicious transactions:

- Regulators have not provided a definitive list of requirements.
- Training staff to identify and report suspicious transactions to the relevant authority was problematic

- The attendees' consensus that there is sometimes limited input from Gardaí, forcing the fund administrator to make the decision, potentially holding up valid redemption payments as they tend to err on the side of caution.

Current Functionality in Koger's Fund Administration System, NTAS:

- Report Scheduler enables users to automatically generate and broadcast reports at specified regular intervals.
- Reports can be sent via Email or an FTP site.
- Reoccurring report log files are recorded for review and audit purposes.
- DocTrack Reports displaying all the warnings and breaches when booking a transaction/order.
- Risk levels can be set up for investors based on country and entity type.
- Document requests can be set up based on the holders' country, entity, etc

Technology

It was obvious from the tone of the discussions how important it is that technology keeps up in the AML and Compliance space. If fund administrators are going to be able to service their client's requirements effectively they need systems that are flexible, and have enhanced reporting capabilities. NTAS addresses many of these needs, and Koger is always improving its products in order to keep up with changing demands.



Koger, Inc., a leading provider of software and services for the fund administration industry, hosts roundtables on important industry topics, bringing together leaders of top firms in fund administration, as well as fund managers and investors.

Established in 1994, Koger products are used by some of the largest and most respected financial institutions in the world. With offices in United States, Ireland, Slovakia and Australia, Koger provides comprehensive technical 24/5 support.

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