

## Operation Bid Rig: Anti-money-laundering lessons to be learned (August 20, 2009)

It could have happened in your backyard. Would you have caught it?

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If Operation Bid Rig, the recent money-laundering investigation unsealed by the United States Attorney in New Jersey, involving state politicians and members of the Syrian Jewish Community, teaches bankers anything, it should be that money laundering is alive and well and that money laundering schemes are limited only by the imagination of the launderers.

The facts of Bid Rig are as follows:

In the political corruption aspect of the case, a cooperating witness (i.e., someone working with law enforcement in an undercover capacity), offered bribes to state politicians to advance his interest in securing government contracts. The monies allegedly accepted by the politicians were used for personal gain and/or to support their reelection efforts. The Rabbis segment of the case is less clear. The allegations appear to involve the use of charities controlled by the Rabbis to serve as the vehicle by which monies were exchanged in the laundering process.

What remains unclear is the funding source of some of the monies laundered from overseas. However, the case brought in Los Angeles in 2007 that recently resulted in a guilty plea by Naftali Tzi Weisz, Grand Rabbi of a Brooklyn-based Orthodox Jewish group, may be instructive. In that case, according to his plea agreement filed in federal court, Rabbi Weisz &ldquo;allow[ed] the charitable entities linked to the Spinka religious group to be used as a vehicle to generate false charitable deductions&rdquo; in a tax evasion/money laundering scheme where checks were exchanged for cash.

These cases elaborate the breadth of the enforcement priorities of federal prosecutors in the anti-money laundering area.

In turn, this is important for financial institutions to understand as they endeavor to perform know-your-customer procedures on new customers and to detect and report suspicious activity within their institution by existing customers (especially known high-risk categories of customers such as politicians and charities).

These cases also should serve as notice to financial institutions that even in these times, when strained compliance budgets are more the norm, there is no room to let down your institution&rsquo;s guard on the AML front.

Action steps to take

What then should be done in light of the N.J. prosecution?

1. **Transaction Monitoring:** The transaction monitoring systems used by financial institutions to detect potential suspicious activities rely upon scenarios or algorithms that look for patterns of behavior inconsistent with expected customer profiles. Often the scenarios come embedded in the systems themselves at the time of purchase and, as a consequence, are relevant at the point in time when installed. As such, if not constantly refined, they can become outdated and can miss new money laundering typologies (as the Rabbi portion of the N.J. case may represent); fail to take account of transactions which go through foreign affiliates; or produce more false positives than true alerts, thereby clogging up the investigative pipeline. By updating the existing scenario set using advanced analytics, experience has shown that false positives may be reduced. With fewer cases needing to be investigated, opportunities for detection of truly suspicious behavior are likely to increase.

[Editor's Note: This point was made at length by practitioner Richard Small of American Express in a session at ABA's 2009 Regulatory Compliance Conference. Read the coverage.]

2. **Financial Intelligence Units:** The FIU is the intelligence nerve center for the financial institution. It tracks the red-flag alerts created by the AML transaction monitoring system and investigates them for suspicious activity reporting (SAR). The private sector FIU is modeled after the government intelligence centers, such as FinCEN in the U.S. or the Israel Money Laundering Prohibition Authority (IMPA).

These FIUs are a critical component of a robust risk and compliance program. Historically, they originated in global financial institutions needing to analyze transactional data from diverse geographic locations. Today, many regional, state, and community banks are implementing FIUs as well, as the technology has become more accessible and consulting organizations have become experienced in helping organizations implement them in a cost-effective manner.

In the current environment, global banks should consider expanding the mandate of FIUs to encompass other risks such as fraud, tax evasion, public corruption, and privacy, while domestic financial institutions that have yet to create a FIU should give thought to doing so. FIUs, whether with a broad or AML-specific mandate, allow for a more holistic view of the compliance risks that institutions face. So, for example, the money-laundering scenarios such as the public corruption and charities (tax) components of the N.J. case each may be more readily observed and acted upon with a robust FIU.

3. **Risk Assessments:** The risk assessment has come to be the foundation of an effective AML program. Once the risks are identified and prioritized, effective transaction monitoring and the SAR analysis process can follow more effectively. (Training; reporting protocols; testing; customer identification program and enhanced due diligence for high risk customers; products and geographies round out the remaining components of an effective AML program.) Financial institutions studying the facts of the N.J. case should ask themselves whether they would have detected and reported this behavior were it to have occurred in their institution.

4. **Testing:** A well trained, fully staffed audit/independent testing team (whether internal or external) complements the compliance function. If the audit staff and compliance testing personnel are trained to understand the specific money laundering risks to their companies, these risks can be mitigated more effectively and senior management may have the benefit of an internal report before receiving the news of a compliance failure from their regulators.

Asking audit/testing staff what protocols are in place that might have detected the behavior exhibited in the N.J. case might be instructive for banks seeking to determine if their programs are adequate to the task. Likewise, asking audit/testing personnel to conduct a targeted look back to determine if any of the actors identified in the complaints were customers is necessary to ascertain whether a SAR should be filed.

The N.J. prosecution is a stark reminder of how difficult it is to detect and report money laundering. So far, no banks have been implicated in the wrongdoing. Whether this is so because of luck or hard work, banks should take the opportunity this case presents to stress test their AML program to avoid problems down the line.

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