

HOW DOES THE NOTION 'ONCE A PEP, ALWAYS A PEP' APPLY IN AML WATCHLIST SCREENING?



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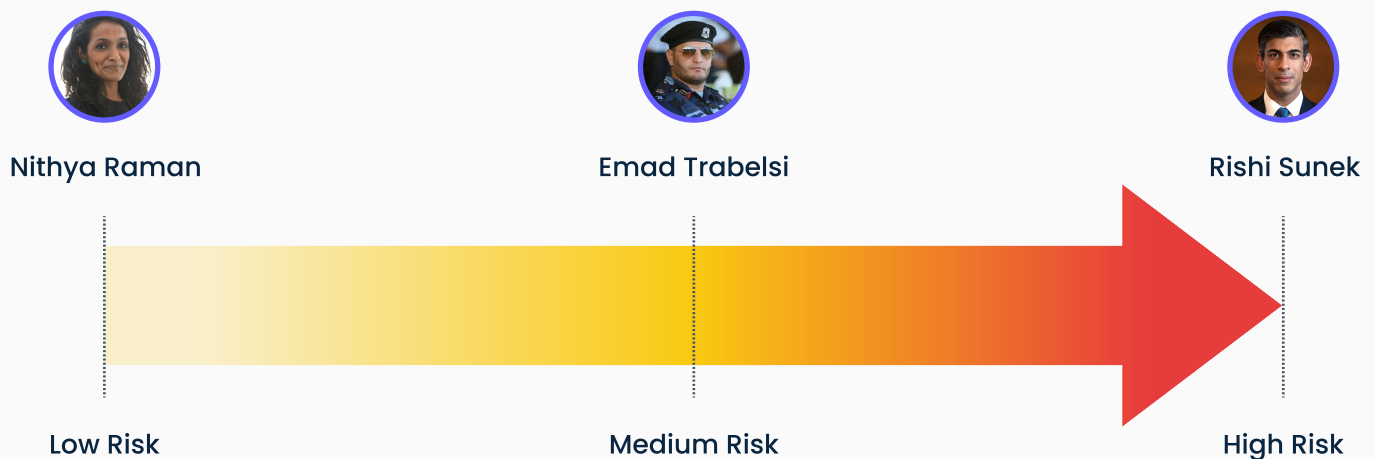
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Introduction

The 2022 revelations of corruption charges against prominent European Parliament member Eva Kaili, implicated in a cash-for-influence scandal with Qatar, underscore the critical need for a comprehensive examination of Politically Exposed Persons and the imperative to enhance regulatory scrutiny.

In the realm of global finance, the term "Politically Exposed Persons" (PEPs) holds substantial weight. PEPs encompass individuals who presently hold or have previously held significant public positions, along with their close associates and family members. Financial institutions closely scrutinize this group due to their elevated risk for corruption and involvement in money laundering. The concern arises from the potential for PEPs to exploit their positions, engaging in corrupt practices such as bribery and misappropriation of funds, and then utilizing financial systems, both domestically and internationally, to legitimize these ill-gotten gains.

Notwithstanding the fact that not all PEPs engage in corrupt activities, the inherent risk of misuse of power remains a persistent concern irrespective of their country of origin, nature of business activities, or seniority of role. The endemic scale of grand corruption and its detrimental impacts on institutions, government revenues, and social welfare underscore the imperative for effective measures to mitigate these risks.



Thus, comprehending the essence of PEPs and their distinct challenges is pivotal to any discourse regarding their persistent classification and the consequential implications.

1. "Wolfsberg Group Publication Statement Guidance on Politically Exposed Persons (PEPs) The Wolfsberg Group is pleased to publish u." AML 30000, <https://www.aml30000.com/wp-content/uploads/2021/06/Wolfsberg-Publication-Statement-on-PEPs-May-2017.pdf>. Accessed 25 September 2023.

Defining PEPs and Regulatory Frameworks

PEPs are individuals who hold or have held prominent public functions, either domestically or in foreign jurisdictions. The Financial Action Task Force classifies PEPs into three main categories: Foreign PEPs, Domestic PEPs, and International Organization PEPs.

▶ Foreign PEPs encompass individuals entrusted with significant public roles in foreign countries, such as heads of state, legislators, senior government officials, or military officers.

▶ Domestic PEPs, on the other hand, hold or have held political or public positions within their own country, mirroring the risk associated with foreign PEPs.

▶ International Organization PEPs refer to those entrusted with prominent functions within international organizations like the United Nations or the International Monetary Fund.



2. "November 2022." Rulers, 2 November 2022, <https://www.rulers.org/2022-11.html>. Accessed 26 December 2023.

3. https://www.gub.uy/secretaria-nacional-lucha-contra-lavado-activos-financiamiento-terrorismo/sites/secretaria-nacional-lucha-contra-lavado-activos-financiamiento-terrorismo/files/documentos/publicaciones/Lista_PEP_V30.pdf. Accessed 26 December 2023.

4. Djankov, Simeon. "World Bank Document." World Bank Document, <https://documents1.worldbank.org/curated/en/611261468155103854/pdf/542500PUB0Expo101Official0Use0Only1.pdf>. Accessed 25 September 2023.

The relatives and close associates of PEPs are also categorized as such because they can be conduits for concealing illicitly gained assets. Understanding these classifications is vital for implementing appropriate Anti-Money Laundering and anti-corruption measures. Precise identification of PEPs is crucial to avoid labeling everyone in public positions and maintain a focused risk assessment.

According to Wolfsberg Group Publication Statement:

“The definition of what constitutes a PEP should not be diluted by the inclusion of persons who may be in public life, but are not in a position to enrich themselves improperly, as this leads to an inefficient allocation of resources, poor customer experience and, in extreme cases, to the denial of financial services to those in public life, their relatives or close associates.”

Global Regulatory Standards and Guidelines for Identifying and Monitoring PEPs:

Financial institutions are mandated to implement effective Customer Due Diligence procedures to identify beneficial owners and ascertain if a customer qualifies as a PEP. These requirements stem from global regulatory standards which necessitate financial entities to maintain risk-management systems ensuring accurate PEP identification. The methods encompass asking pertinent questions, employing database checks, and referencing publicly available information. Notably, the FATF has emphasized the significance of implementing risk management systems for PEP detection in addition to standard CDD measures.

Regulatory authorities across various jurisdictions emphasize the need for banks to determine if a beneficial owner is a PEP, aligning with the FATF's essential criteria. However, disparities exist regarding the explicit requirement to check for PEP status, urging the importance of integrating this aspect into legislation comprehensively. The FATF has established crucial recommendations stipulating that laws or regulations should encompass provisions compelling financial institutions to ascertain if the beneficial owner is a PEP, ensuring a consistent global approach.

5. “Wolfsberg Group Publication Statement Guidance on Politically Exposed Persons (PEPs) The Wolfsberg Group is pleased to publish u.” AML 30000, <https://www.aml30000.com/wp-content/uploads/2021/06/Wolfsberg-Publication-Statement-on-PEPs-May-2017.pdf>. Accessed 25 September 2023.

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Understanding the Evolving Landscape of PEP Regulations:

The evolving landscape of PEP regulations necessitates a comprehensive understanding of when and how to check for PEP status. Financial institutions, particularly banks, are obligated to initiate PEP checks at the outset of a business relationship and periodically for existing customers. This practice ensures that any change in a customer's PEP status is promptly identified and addressed.

Furthermore, many banks incorporate PEP checks when customers request additional products or specific services, particularly for those with a higher risk of money laundering associated with the new offering.

In striving for effectiveness and efficiency, some banks run regular checks against commercial or in-house PEP databases. They employ technology to ensure that customers attaining PEP status after the initial customer onboarding process are promptly identified. The dynamism of the regulatory environment demands that banks adopt proactive measures to stay abreast of PEP status changes and related risks. Additionally, banks are contemplating the feasibility and efficacy of a national or international definitive list of PEPs. While this concept has been advocated for, its practicality and potential limitations in mitigating risks should be carefully assessed before implementation.

By continually adapting and augmenting their risk management systems, banks can effectively navigate the evolving PEP landscape, thereby promoting financial integrity and security in the global banking sector.

Scandals of PEPs' Past:

During the 1990s, Nigeria experienced a dark chapter under the rule of Sani Abacha, a military dictator who embezzled vast sums from the Nigerian Central Bank, diverting these funds to personal accounts in the UK and Switzerland. This illicit episode marked the genesis of the term "Politically Exposed Person". Following Abacha's ousting, the Nigerian government faced significant challenges in repatriating the stolen wealth, prompting the development of a classification system for individuals in such influential positions. Subsequently, many individuals involved in money laundering were identified and designated as PEPs.

In October 2007, a significant case underscored the global prevalence of money laundering. Vladimir Kuznetsov, a former Russian diplomat, was convicted for money laundering, shedding light on the misuse of funds even within international organizations. Further instances like the conviction of Jim Hayes, an Alaska mayor, and his wife in May 2008, emphasized the imperative to address domestic cases of corruption and money laundering affecting social services.

The international sphere was not immune to these issues either. In March 2012, the Royal Bank of Scotland faced consequences for inadequate handling of PEPs, indicating a systemic problem in the banking sector. Subsequently, Barclays Bank's fine in November 2015 illustrated the need for stringent checks and due diligence regarding PEPs to curb financial crime.

Even the UK saw its institutions facing penalties, as in June 2016, when Canara Bank's UK division was fined for anti-money laundering violations. These events emphasized the urgency of implementing and enforcing effective measures for PEP screening to put brakes on money laundering and illicit capital flows.

Case Study:

Donald Trump as a PEP

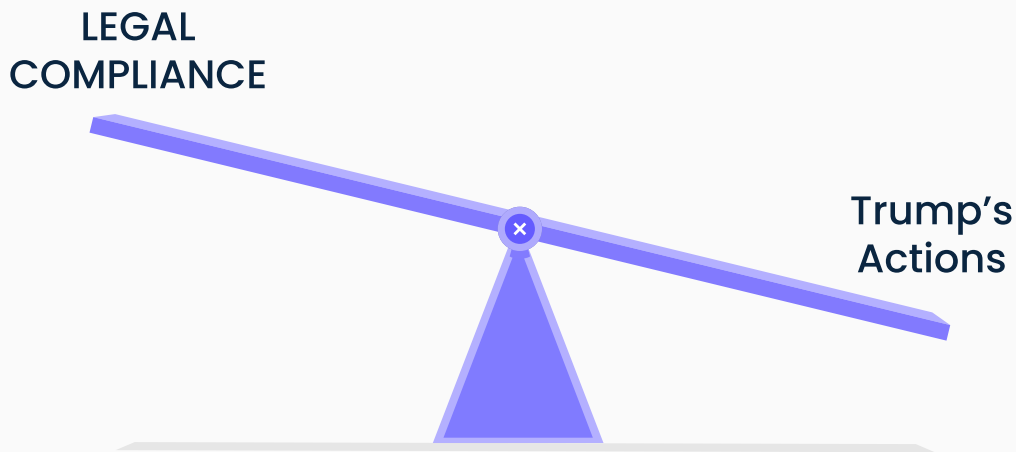
During his presidency, Trump demonstrated a cavalier attitude towards classified information. Notable incidents include sharing classified intelligence with Russian representatives in 2017, which raised concerns about compromising intelligence sources. He also made the unprecedented move of posting a classified satellite image on his Twitter account in 2019, revealing sensitive U.S. surveillance capabilities. These actions not only posed national security risks but also strained intelligence-sharing relationships with U.S. allies.

Trump's approach to government records, particularly those containing classified information, was marked by a lack of adherence to established protocols. He frequently disposed of documents, at times even resorting to flushing them down toilets, which directly contravened legal obligations to preserve official records. This behavior raised concerns about accountability, legal compliance, and the potential loss of valuable historical and security-related information.

The legal implications of Trump's actions are significant. Unauthorized removal and retention of classified information are criminal offenses under U.S. federal law. Furthermore, his handling of classified documents, including potential unauthorized disclosures, could constitute violations of the Espionage Act of 1917 and other related statutes. The indictment against Trump for retaining classified documents illustrates the gravity of these legal implications.

Trump's conduct had substantial national security ramifications. His disregard for established procedures jeopardized intelligence-sharing relationships with allied nations and placed sensitive sources and methods at risk. The potential exposure of critical intelligence information had severe implications for national security, including possible damage to counterterrorism efforts and diplomatic relations.

Moreover, the public exposure of classified information and the nonchalant approach to security procedures set concerning precedents for the handling of sensitive government data, necessitating stringent measures to protect classified materials in any political administration.



Case Study:

Nigel Farage as a PEP

Nigel Farage, a former political leader in the UK, faced account closure by Coutts, allegedly due to his political views. A subject access request revealed that the bank cited his publicly stated views as incompatible with its inclusive organizational stance, posing reputational risks.

Debanking, the practice of terminating services for specific customers, is prevalent in the UK banking sector. The closure of Farage's accounts highlighted the lack of transparent explanations for denying services to politically exposed persons (PEPs), raising questions about the fairness and transparency of the banking sector.

In response to concerns regarding account closures based on political beliefs, the UK government introduced new rules mandating banks to explain and delay closure decisions. The rules aim to provide customers with a 90-day notice period to challenge the decision and foster transparency in the banking sector.

The Farage case underscores the necessity of striking a balance between preventing money laundering risks and upholding the rights of individuals, including PEPs. Regulatory adjustments are crucial to ensuring a transparent and equitable banking environment that respects the rights of all customers.

Examining the Notion of 'Once a PEP, Always a PEP'

The status of a Politically Exposed Person remains in a state of flux, constantly evolving in response to various dynamics, a principle well-captured by the Financial Action Task Force's Recommendation 12. This stance implies that an individual may continue to bear the PEP designation even after their tenure in a prominent public function has concluded. The FATF strongly advocates for a risk-based approach in managing such cases, advocating that the level of risk associated with the individual should guide the actions taken, rather than relying on rigidly prescribed time limits.

Several factors play a significant role in this risk assessment. The extent of informal influence an individual may still possess, the seniority of their prior position, and any continuing connections to their earlier role are pivotal considerations. For instance, a former high-ranking government official might still wield influence or have associations that present risks. Therefore, the approach to handling a PEP post their public function should involve a thorough and comprehensive evaluation of these risk factors.

Furthermore, the United Kingdom has identified fraud as a substantial threat, akin to terrorism, signifying its gravity in the eyes of law and governance. PEPs are particularly susceptible to fraudulent activities owing to their influential positions, underscoring the critical need for rigorous due diligence during customer onboarding. The process of due diligence, especially regarding PEPs, is fundamental in detecting and preventing fraudulent activities.

Moreover, it's important to highlight that PEP and sanction lists are not stagnant databases but living entities that are consistently updated based on personal roles, political factors, and events of global significance. Regulatory authorities, such as the Financial Conduct Authority in the UK, impose strict obligations on businesses to ensure compliance with Anti-Money Laundering regulations. One of these key obligations is effective PEP screening.

The consequences of failing to identify high-risk customers, especially PEPs, can be severe, encompassing both financial losses and legal repercussions. Businesses may inadvertently facilitate money laundering, fraudulent transactions, or other illegal activities, leading to financial penalties and a tarnished reputation. To mitigate these risks effectively, businesses need to be diligent and thorough in their compliance measures, particularly regarding PEPs. This includes staying updated with regulatory changes and dynamically adjusting their screening processes to align with the evolving nature of PEP designations.

Recommendations For Dealing With Sensitive Status of PEPs:

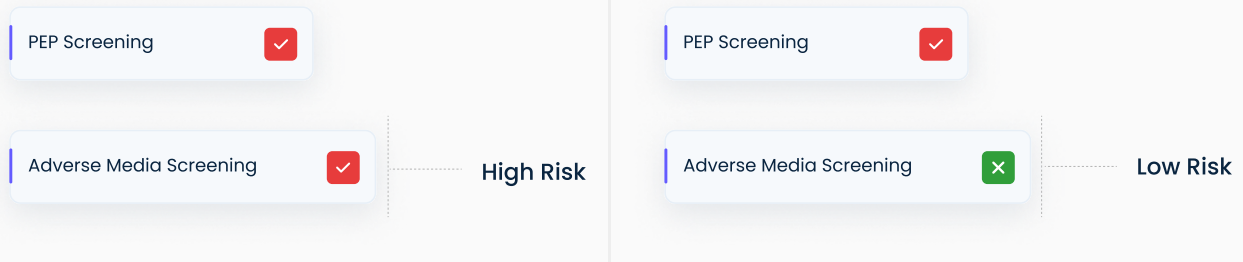
- ▶ Financial institutions should establish robust systems for continuous monitoring and timely updating of PEP and sanction lists. This would ensure that the PEP status of customers is always up-to-date, allowing for appropriate risk assessment.
- ▶ Financial institutions should invest in advanced AI and data analytics tools to enhance their ability to identify and assess PEPs accurately. This investment will aid in real-time monitoring and risk assessment.
- ▶ Encourage collaboration and information sharing among financial institutions and regulatory bodies to collectively address the challenges posed by PEPs. Shared insights and intelligence can significantly improve risk assessments.

- ▶ Regular training programs for employees within financial institutions should be conducted to ensure they are updated with the latest guidelines and techniques for handling PEPs. Knowledgeable staff is essential for effective PEP risk management.
- ▶ Financial institutions should conduct scenario-based preparedness exercises to evaluate their readiness in handling PEP-related challenges. These exercises can help identify gaps and areas for improvement in PEP screening and due diligence processes.
- ▶ Stay vigilant and ensure strict compliance with evolving regulations, especially those related to PEP screening and due diligence. Regularly review and update internal policies to align with the latest regulatory requirements and recommendations.

Recently, the UK Government enacted the Money Laundering and Terrorist Financing (Amendment) Regulations 2023, emphasizing the treatment of domestic PEPs as inherently lower risk than non-domestic PEPs. Regulated firms must apply reduced enhanced due diligence to domestic PEPs unless other risk factors are present.

This regulation introduces a challenge in AML compliance by raising questions about the identification and screening of 'other' risk factors. How do concerned entities effectively screen for these factors, and what if a reduction in due diligence exacerbates issues in this intricately connected global financial system? The potential impacts of this regulation are substantial.

Put differently, an optimal solution is needed. Traditional PEP screening works in some cases, but not in all. To cater to the dynamic needs of today's regulatory landscape, AML watcher provides a platform that incorporates adverse media screening, pinpointing those elusive 'other risks' and ensuring comprehensive compliance prevailing regulations across the board with its extensive data. The platform's innovative approach combines precision with exceptional work flow, making AML compliance not just a requirement but a simplified, accessible process for all.



- ▶ Adhere to the enhanced due diligence measures outlined in FATF Recommendation 12 for foreign, domestic, and international organization PEPs. Implement proactive steps, assess risk criteria, profiles, and conduct thorough verifications to determine a customer's PEP status.



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