

## Regional perspectives: Central and South America and the Caribbean



### In the shadow of the U.S.A.

Banks in Central and South America and the Caribbean are, through trade and financial links, closely bound to the U.S. and have been impacted by the extra-territorial effects of U.S. legislation. Banks in the region reported greater AML investment than ever before in order to meet the higher standards expected of them.

#### The role of senior management

The results of our survey indicate that senior management considers AML to be a high priority in this region, with 88% of respondents confirming that this is the case within their own institutions. This represents virtually no change from the response in 2004. This sustained interest in AML issues affecting banks in the region may well be a consequence of recent regulatory enforcement actions in which a lack of senior management oversight has been specifically singled out as a weakness within the institution. In some instances, the entire board of directors of some institutions have been replaced as a result of regulatory action related to AML, and this has helped to focus senior management's attention on the issue.

#### Cost of compliance

Banks in the Central and South America and Caribbean region anticipate high growth in future AML costs, with an average expected growth rate of 42% over the next three years. This is despite

already strong growth since our last survey. Banks in the region attributed the rise in costs to increased expenditure on transaction monitoring and training, perhaps in response to increased pressure from U.S. regulators. A third of our respondents had responsibility for global or North American operations, and many other banks in the region have correspondent banking relationships with the U.S.. These links to the U.S. are believed to have been influential in increasing focus on AML training in the region. This is reflected elsewhere in our survey, with banks in this region rating OFAC rules as the most significant impact on their institution with the exception of local legislation and regulations. The banks currently face increased burden not only to indirectly "comply" with U.S. but also with EU legislation and regulations. While this in the short term increases the cost of compliance, in the long term, financial institutions in this region will be well suited to preserve their global competitiveness, while satisfying

regulatory demands not only in their home countries, but within other world financial markets as well.

#### AML policies and procedures

Banks in the region showed a slight increase in the number of banks seeking to use a global AML policy across their entire organization. The number of banks reporting that they develop policies and procedures at a global level and implement them consistently worldwide, increased by 18 percentage points, and now account for 38% of all banks in the region. This is likely to reflect the U.S. influence, as well as the fact that banks in the region are in an early stage of the development and implementation of AML policies and procedures. The percentage increase can most likely be attributed to a number of enforcement actions in the U.S. and EU that are being used by banks in the region as guidelines in order to avoid similar costly enforcement actions.

### Formal monitoring of AML systems and controls

All banks in the region reported that they had a formal program for testing the effectiveness of their AML systems and controls (the only other region to report this was Russia & CIS). However, several banks have voiced concerns about regulatory expectations regarding the requirements for testing the effectiveness of their automated AML monitoring systems, and the lack of regulatory guidance in this area.

### Risk-based approach to Know Your Customer activity

Along with the majority of respondents to our survey, many banks in this region say that they use a risk-based approach at account-opening and that they consider the two most important factors for risk assessment to be the nature of the customer's business and whether the individual is a PEP.

A relatively high percentage of banks in the region have a remediation program in place to fill in gaps in their KYC information for existing customers (83% of respondents). This has increased by 10 percentage points from the 2004 survey, although the key change since this time is a growing emphasis on the use of a risk-based approach to remediation. In our last survey, 100% of respondents with a remediation program said that they were doing so across their entire customer base. This year, only 40% of respondents were in this situation, with the majority of the remaining banks using a risk-based approach.

### Politically Exposed Persons

Most respondents in this region, 83% of those surveyed, said that they had a

procedure in place for identifying and monitoring PEPs. Regional factors, such as a history of political corruption, are likely to have influenced the high profile that this issue has in the region. The majority of jurisdictions in the region require banks to identify both foreign and domestic PEPs, which exceeds the requirement in the U.S.A. PATRIOT Act 2001 to identify foreign PEPs only.

### Transaction monitoring

Respondents in the region noted transaction monitoring as one of their two most significant areas of investment, although the majority of banks in the region said that they were satisfied with the systems that they had in place (more so than any of the regions surveyed except Russia and the CIS).

Banks in the region also said that improved transaction monitoring was the most significant driver of increased numbers of SARs and claimed a relatively high degree of functionality for their IT, with 38% of internationally active banks in the region saying that they could monitor a single customer's transactions and account status across multiple jurisdictions (only the North American banks did better than this, with 42% of banks making the same claim).

The high results for this region and the U.S. is not surprising given the high degree of U.S. regulatory influence in the region and the banks' ability to adapt and mirror their processes in line with U.S. regulatory expectations. However, transaction monitoring cannot be viewed in isolation, and many respondents commented that their transaction monitoring efforts could be improved by

conducting and continuously updating:

- a comprehensive assessment of the banks' products and product groups in order to determine the risks certain products and product groups pose for money laundering and terrorist financing;
- a full analysis to understand the universe of all transaction-types that the institution uses;
- a comprehensive assessment to determine the risk the customer base poses for money laundering and terrorist financing.

### Training

The proportion of staff at banks in this region that are given AML training was relatively high, with 71% of banks saying they had trained 81-100% of their staff in the past two years. This emphasis on AML training may be attributable to the impact of U.S. legislation, specifically the U.S.A. PATRIOT Act 2001. However, rather than conduct tailored training courses, many institutions choose to give every relevant member of staff the same level of basic AML training so as to satisfy both local and U.S. regulators. With some of the large banks having tens of thousands of employees, this is a pragmatic approach to meeting compliance needs, but is only the first step toward implementing a robust and comprehensive AML training program that takes into account the different lines of businesses and AML risks across the bank.

### Attitudes towards regulation

Banks in the region, in common with those across the survey, say that the biggest influence on their AML policy and procedures is their domestic legislation and regulation. However, U.S. legislation is the next most commonly cited influence on AML



policy, reflecting the close commercial and financial ties between the U.S. and Latin America, and the correspondent banking relationships that underpin these relationships. Banks in this region are currently experiencing a certain level of “double” regulation, both by domestic regulatory bodies and indirectly by U.S. legislation. One of the most commonly cited concerns of banks in this region is the lack of overall harmonization of regulations between the U.S. and domestic regulations. Banks have cited numerous efforts being conducted by trade associations in order to achieve a greater level of harmonization between domestic and U.S. regulators, while preserving the integrity and soundness of the entire Americas financial markets.

### **Sanctions**

In the area of sanctions compliance, the extra-territorial effects of U.S. law have been particularly prominent, because of the close trade and financing links between the region and the U.S., banks reported particular vigilance in updating their information on principals for the purposes of sanctions screening and monitoring (83% of banks reported they did so on an annual basis). Similar to the challenges banks are experiencing in the area of transaction monitoring, the U.S. influence is significant, leading to amendment of AML compliance programs to take account of this.

### **Outlook**

With ongoing U.S. and international pressure, banks in the region are likely to continue to enhance their AML processes in line with the evolution of practices in the U.S. and elsewhere. Whilst this can raise operational issues and costs, it will make it easier for banks in the region to carry on business internationally and access overseas markets, and this is increasingly important at a time that the majority of emerging markets are going through unprecedented economic growth and internationalization of capital flows.