



**THE PANDORA PAPERS: HOW ANTI-MONEY
LAUNDERING PROCEDURES AND CONTROLS SHOULD
HAVE FLAGGED \$300 MILLION EARLIER**

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ABSTRACT

PURPOSE – This paper aims to discuss the risk-based policies, procedures, and controls reasonably designed to identify and minimize money laundering and other illicit financing risks associated with Non-profit Organizations.

DESIGN/METHODOLOGY/APPROACH – This paper uses the “Pandora Papers” to illustrate the vulnerability of the banking system to money laundering and other illicit financing risks associated with Non-Profit Organizations, and to solidify the hypothesis that effective implementation of risk-based policies, procedures, and controls can help flag illicit funds before a lengthy asset recovery process becomes necessary.

FINDINGS – This paper determined that adequate policies, procedures, and controls, if implemented, could help manage the money laundering and other illicit financing risks associated with Non-Profit Organizations, and ensure monitoring systems are set up to adequately detect suspicious transactions.

ORIGINALITY/VALUE – This paper uses the “Pandora Papers” to help build awareness with the regulatory, enforcement and customs authorities as well as reporting entities about the risks and vulnerabilities of Non-Profit Organizations, and how to mitigate them. This is the only Article to adopt this kind of approach.

KEYWORDS: Money Laundering, Offshore Structures, Banks, Transaction Monitoring system, Manual-Monitoring Process, Filtering Criteria, Thresholds, Training, Independent Testing

1. INTRODUCTION

A trove of leaked documents reviewed by the International Consortium of Investigative Journalists and 150 media partners provide an unprecedented view of how millions of dollars are secretly moved around the world by individuals and entities under investigation by law enforcement agencies or other designated authorities. Those records are part of the Pandora Papers, a cache of more than 11.9 million documents obtained by the International Consortium of Investigative Journalists. The investors revealed in the leaked documents include offshore trusts holding three hundred million dollars for the Legion of Christ in the wake of the Vatican investigation. The trusts holding money for the Legion in New Zealand maintained four Swiss bank accounts, including one at a Geneva-based bank, Lombard Odier, that the U.S. Justice Department later found had helped American clients conceal assets from U.S. tax authorities. In statements to International Consortium of Investigative Journalists, the Legion acknowledged it had set up one of the three trusts, but distanced itself from the other two, which held the majority of the funds designated for the Legion. The Legion said it had no knowledge of the other two trusts' operations. The two trusts were funded by scions of a prominent industrialist family in Mexico, including Father Luis Garza Medina, one of the Legion's top leaders. In civil litigation that began in 2011, Luis Garza and other Legion members were accused of defrauding an elderly Catholic woman out of \$60 million in charitable donations to the order.

While attention has been on offshore structures who hide and move millions of funds around the world, little attention is paid to the banks that willingly transferred these funds from the bank accounts domiciled with them to the bank accounts of offshore structures, especially at a time when those Bank customers were under investigation. This act runs contrary to anti-money laundering (AML) laws and regulations which require Banks to implement an effective system of internal controls reasonably designed to ensure compliance with AML laws and regulations.

While details of the banks' compliance efforts remain unknown, what institutions should do when handling such high-risk clients is clear. What follows is guidance on how a bank could've prevented the movement of funds to the bank accounts of offshore structures.

2. ASSESSING RISKS AND APPLYING A RISK-BASED APPROACH

Banks should have adequate processes and procedures to identify and address high-risk customers. The Bank's customer risk-rating program should review customer relationships in their entirety — i.e., across the Bank's different business lines — in order to obtain an enterprise-wide view of customer risk. In addition, the Bank should include important information about its clients in its risk-rating analysis, such as the nature of the customers' businesses, verification of owner/operator identities, and anticipated account activity. The exclusion of this information may result in high-risk customers being risk-rated based on incomplete information. As a result, customers whom the Bank identified or should have identified as high-risk may be free to conduct transactions through the Bank with insufficient oversight. Banks should therefore ensure that their policies, procedures and controls should gather and review sufficient information on foreign and domestic account customers to adequately assess risk and potential for money laundering and other illicit financing risks.

Banks should connect certain customer information to their risk rating system, which should rate customers based on their overall risk for money laundering by generating a score for each customer.

Non-profit Organizations like the Legion of Christ should have been rated by the Bank in accordance with their location, size and services offered, the anti-money laundering (AML) and supervisory regime of the jurisdiction that registered the Legion of Christ, nature and duration of the bank's relationship with the Legion, the type, purpose, and anticipated activity of the account, public information in standard industry guides, periodicals, and major publications. The customer scores should be used to determine the frequency for regular AML reviews, including semi-annual and annual

high-risk customer reviews which should focus on identifying if the customer has negative news on them, assessing account activity, comparing the historic dollar volume to the current dollar volume to assess the reasonableness of the customer's transaction activity, and sampling checks within the customer's account to fully enable the Bank to understand the nature and legitimacy of their customers' activity and patterns therein. **AML Analysts who became aware of the investigation of the Legion by the Vatican in 2010 along with the civil litigation in 2011 where Luis Garza and other Legion members were accused of defrauding an elderly Catholic woman out of \$60 million in charitable donations to the order, should have reviewed such information with the account activities of the Legion to determine whether there is a deviation in their account activity from the anticipated activity identified at account opening. Where the AML Analysts detect a deviation in the legion's account activity, they should change the legion's risk ratings. For example, if the legion was rated as medium risk, the Bank should have changed this to High Risk.**

Banks should Incorporate information about customers' business purposes, anticipated activity, anti-money laundering supervision, host country anti-money laundering vulnerabilities, and history of anti-money laundering compliance into the Bank's monitoring of customer transactions. Failure to incorporate these elements into the suspicious activity monitoring program may lead to multiple failures to identify suspicious activity and file Suspicious Activity Reports (SARs).

3. SUPPLEMENTING THE TRANSACTION MONITORING SYSTEM WITH A MANUAL-MONITORING PROCESS

Banks dealing with Non-profit Organizations like the Legion of Christ should supplement their transaction monitoring system with a manual-monitoring process that includes a quarterly review of high-risk customers. Moderate-risk customers should be reviewed semi-annually and low-risk customers should be reviewed annually.

Where the Bank learns through its semi-annual and annual high risk customer review that a customer had been indicted, on charges relating to its business that included conspiracies to commit money laundering, the Bank should accurately and timely file SARs. **For example, Where AML analysts learnt of the investigation of the Legion of Christ by the Vatican in 2010 and of the civil litigation in 2011 where Luis Garza and other Legion members were accused of defrauding an elderly Catholic woman out of \$60 million in charitable donations to the order, they should have implemented enhanced monitoring on the bank accounts of the Legion of Christ to adequately monitor for and detect suspicious activity. Failure to do this will expose the financial system to serious risks of money laundering.**

Banks should also review the account activity of each personal account of individuals managing or controlling Non-profit Organizations like the Legion of Christ that has at least two cash transactions per month of \$3,000 or more occurring during any three months within the period from January 1, through June 31, to determine whether the pattern of account activity may suggest that the account is being used for business purposes. Thereafter, the Bank should conduct semi-annual reviews for three years of the account activity of each personal account that has at least two cash transactions per month of \$3,000 or more occurring during any three months within a six-month period (i.e., July-December) to determine whether the pattern of account activity may suggest that the account is being used for business purposes. If the Bank determines that an account is being used for business purposes, the Bank should document the name of the business, the nature of the business, the individual member's relationship to the business and the Bank, and the nature of the activity in the account and any related accounts. The Bank also will code the account in its internal system as a business account, and it will monitor the account for AML purposes.

Banks should continue to use and maintain its enhanced automated and manual systems to identify possible suspicious currency, wire transfer, and other transactions through member accounts, both personal accounts and business accounts. Special attention should be given to transactions through

business accounts and personal accounts used by members for business purposes, especially accounts used by businesses that are themselves financial institutions subject to AML Laws and Regulations, e.g., funds transmitters.

4. DOCUMENTING OR EXPLAINING FILTERING CRITERIA, THRESHOLDS

Banks should conduct risk-based transaction monitoring which can identify significant amounts of suspicious activity in the bank accounts of Non-profit Organizations like the Legion of Christ. Banks should document or explain filtering criteria, thresholds, and how both are appropriate for the Bank's risks. Management should periodically review and update the filtering criteria and thresholds established for continued effectiveness. In other words, where a Bank decides to configure its automated transaction monitoring system to generate a certain number of alerts each month, the Bank should conduct "below-threshold" testing to evaluate the extent to which the limits placed on alerts for Queries has caused the Bank to fail to investigate and file SARs on suspicious activity. The below-threshold test should involve selecting a sample of alerts that occurred immediately below the alert limits to determine whether the limits should be adjusted to capture suspicious activity that occurred below the threshold. Where the below-threshold testing reveals a significant amount of suspicious activity occurring below the alert limits that the Bank employed, the Bank should lower the alert thresholds to increase the number of alerts reviewed and ensure that the Bank properly investigated and reported suspicious activity. Banks may also need to substantially increase their number of investigators and where necessary, increase salaries of certain AML employees to ensure that the Bank effectively manages its monitoring programs.

5. MAINTAINING ADEQUATE STAFFING AND CONTINUITY TO REVIEW SUSPICIOUS ACTIVITY ALERTS AND INITIATE AND COMPLETE INVESTIGATIONS

Banks must recognize the risks inherent within its international business line and provide adequate staffing to mitigate such risks. **Where the Bank determined at the Enhanced Due Diligence stage that Non-profit Organizations like the Legion of Christ qualify as high-risk customers, they should provide adequate staffing to mitigate such risks.**

Banks must employ sufficient staff to review suspicious activity alerts resulting from the Bank's monitoring processes. The Bank's compliance staff should be able to initiate and complete investigations and file complete and timely suspicious activity reports. Failure of the Bank to provide adequate designated personnel will limit its ability to initiate and complete investigations and file complete, accurate, and timely suspicious activity reports.

6. TRAINING

The Bank's AML training program should be commensurate with the Bank's customer risk profile and services offered. The Bank's AML program must provide for education and training of personnel regarding its responsibilities under the program, including gathering customer identification information, performing customer verification through the use of external databases, reviewing accounts for suspicious transactions, reviewing and/or approving wire transfers, and maintaining records in accordance with AML requirements. **The Bank's training program should provide AML staff with adequate job-specific training on red flags associated with the type, size, and frequency of the various transactions made by Non-profit Organizations like the Legion of Christ through the Bank.**

The Bank's training program should focus on general AML requirements and also include topics on risks specific to the Bank.

7. CONCLUSION

Banks must implement an effective system of internal controls to ensure compliance with the relevant anti-money laundering laws and regulations and manage the risks of money laundering primarily in the bank accounts of Non-profit Organizations like the Legion of Christ. The mechanisms/measures which have been extensively discussed in this paper will ensure monitoring systems are set up to adequately detect suspicious transactions.

Banks should implement an effective independent audit function, in terms of both scope and frequency, to manage the risk of money laundering and compliance with anti-money laundering laws and regulations. The internal audit function should adequately evaluate and test the Bank's suspicious activity monitoring and reporting systems, the Bank's domestic and foreign customer due diligence program, or other aspects of its AML program. Specifically, internal audit should adequately evaluate and test bulk cash, cash letter, Remote Deposit Capture (RDC), pouch activities, and the enhanced due diligence process relative to foreign correspondent financial institution accounts.

The Bank's independent audit program repeatedly should effectively evaluate money laundering vulnerabilities and to detect anti-money laundering compliance failures in a timely fashion. In particular, the scope of its independent audits should be sufficient to effectively assess the Bank's exposure to the risk of money laundering activities and its ability to comply with anti-money laundering programs and suspicious activity reporting obligations.

With such steps, AML Analysts would have readily identified suspicious elements, "Red Flags" or suspicious activity associated with the Legion's transactions totalling \$300 million.

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Ehi's skill and knowledge in the field of the financial crime space are drawn from his many years of experience as a researcher in anti-money laundering laws and policies, counter-fraud measures, and anti-corruption strategies. So far, Ehi has authored more than 50 publications, including eight books on money laundering law/banking law. Ehi's second book titled "The Risk-Based Approach to Combating Money Laundering and Terrorist Financing" was rated as the #5 best money laundering book of all time by Financial Expert in its 2021 refresh of the rankings. The book also became a bestseller on Amazon for banking law. Ehi's fourth book titled "Deterring and Detecting Money Laundering and Terrorist Financing: A Comparative Analysis of Anti-Money Laundering and Counterterrorism Financing Strategies" has received many commendations from both academic researchers and anti-money laundering professionals.

Ehi received a bachelor's degree in law from the University of Lagos and holds a master's degree in International Commercial Law with specialization in international banking law and anti-money laundering compliance from Cardiff University.

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