Anti-Money Laundering (AML) Practices at Bank Sohar, Sultanate of Oman

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Abstract: Integrity related practices are assuming great significance in the corporate governance of any financial institution today. This case looks at the Anti-money laundering (AML) practices at Bank Sohar, Sultanate of Oman. After a brief description of the company, the policy related to AML at Bank Sohar is described followed by the discussion of the process for embedding the policy within the organization. The mechanism for identifying and reporting the issues pertaining to the practice within the organization is explored and the mechanism for enforcing the practice is studied. Findings of the study suggest that the entire organization has to work together in order to create fool-proof policies leading to better acceptance and implementation. The practices follow the recommendations of Financial Action Task Force on Money Laundering (FATF) and other international studies in an effort to keep Bank Sohar free from any AML concerned potential threats.

Key words: Anti-money Laundering, Anti-money Laundering Practices, Bank Sohar, Oman, Money Laundering

1. Introduction

Money laundering has been called the world's third largest industry and is associated with all manner of crime (Baily, 2000). Money laundering is defined as the processes of making illegally-gained proceeds (i.e. "dirty money") appear legal (i.e. "clean"). Money laundering facilitates crimes such as drug trafficking and terrorism and can adversely impact the global economy (History of Anti-Money Laundering Laws, FinCEN). The rise of electronic banking is exposing vulnerabilities facilitating the movement of billions of dollars in illicit funds. They stem from the speed of money movements, secrecy surrounding financial dealings, jurisdictional issues

due to large number of agencies involved and the failure of government mandated measures and the need for private sector actors to take more responsibility.

2. Literature review

Banking encompasses a wide spectrum of activities, thus, providing large possibilities in this domain to carry out various abuses related to money laundering. Financial Action Task Force on Money Laundering (FATF) is one of the leading international organizations for the prevention and fight against money laundering. This working group cooperates closely with World Bank and International Monetary Fund for the establishment of financial and regulatory measures against money laundering. The group prescribes twenty-five criteria that a country should consider. These include:

- Establishment of strict procedures of “know your customer” in order to be fully acquainted with legitimate activities of each client;

With an intention of identifying and controlling various potential illicit practices, banks are introducing Know-Your-Customer (KYC) provision. However, banks need to take care of the implementation, as there is no obvious end point to the information that would be useful to a bank manager in seeking to prevent money laundering in KYC. Also, it is hard to deal with third-party introducers (where the main beneficiaries wish to remain anonymous) and it can be hard to balance KYC with customer’s right to privacy (Jackson, 2000);

- Refusal to establish a corresponding banking relation with a respondent in jurisdiction, or to continue the relation in the jurisdiction in which he is not physically present;

This provision is taken care of by requiring depositors to sign a document stating that the deposit by any non-citizen, whether individual or a company, is dealing with money legally earned and legally transferred (Baker, 1999);

- Training of employees who work with corresponding accounts to recognize high risk circumstances or irregular activities;
- Conduct sporadic control of all the relations of the corresponding accounts with foreign banks in order to identify higher risk respondents and close the accounts with problematic banks;
- Report to supervising bodies and units of financial inquiry all the problems they have been facing in working with foreign responding banks.

To deal with the money laundering practices associated with electronic money transfer, following measures have been suggested in Bjelajac (2011):

- Implementation of current requests of clients’ identification in order to avoid opening “anonymous” accounts;
- Development of new procedures that should facilitate financial institutions’ ability to meet their clients during their business relations;

- Cooperation among jurisdictions on the basis of unified standards;
- Development of the new information technology capacity that would enable detection of suspicious on-line transactions and confirmation of clients' identity;
- Restriction of the number and type of on-line services or the value of such transactions etc;
- Impediment of non-licensed financial institutions in certain jurisdiction to provide their on-line services in that jurisdiction etc.

Methods and measures for preventing criminal act of money laundering involve numerous actions and procedures in the domain of prevention, conducted by the competent authorities to suppress money laundering and its consequences for the society.

Inspection is a primary supervision method in the implementation of money laundering prevention measures. The global nature of the money laundering phenomenon makes the geographical borders irrelevant. Money launderers tend to shift their activities in jurisdictions with few or ineffective measures against money laundering (Claessens, 2006). In line with the argument, the document "Forty recommendations of the Group for financial actions" which prescribes the minimum internal control measures recommends the following:

- Development of internal policies, procedures and control, including placement of professional employees on the management level and adequate supervision procedure that ensures high employment standards;
- Continuous staff training;
- Revision functions for testing the system of measures against money laundering.

The above review considered the available literature on the recommended practices to identify and prevent AML activities.

3. Case study on Bank Sohar

3.1 Anti-money laundering practice (Company description)

Bank Sohar is Oman's youngest state sponsored commercial bank which was established in 2007. It has 26 conventional branches and 5 Islamic windows. Its key shareholders are the Royal Court Affairs with 14.6% and Oman Investment and Finance Co. SAOG with 13.5% of the holding respectively. Bank Sohar offers a wide array of products and services which include retail banking, corporate banking and Islamic banking among others (Bank Sohar SAOG, 2014).

In its seven years of journey, Bank Sohar has exhibited substantial growth and performance. Bank Sohar has managed to grow to become the fourth largest and one of the most profitable banks in Oman. In spite of increasing competition, Bank Sohar registered a net profit of RO26.871mln for the financial year of 2013 compared to RO23.011mln of the previous year entailing a year-on-year increase of 16.77 per cent (Muscat Daily, 2014). It has the highest ROE (Return on Equity) amongst all the listed Commercial Banks in Oman. This is a result of higher asset leverage. Non-Performing Loans are at an acceptable level of 1.6% of Gross

loans at the end of Q2'13. The bank has succeeded in achieving Fitch's long term rating of BBB+ on account of its prudent provisioning and its coverage of questionable advance (Kathiwalla, 2009).

In reflection of its excellent performance, Bank Sohar has received 11 foreign, regional and local awards over the past year. These encompass the "Best Corporate Social Responsibility Bank Oman 2013" award by renowned UK-based Global Banking and Finance Review, the "The Golden Award for Quality and Business Prestige" by Otherways Management and Consulting Association in Rome, the distinguished Tatweej Academy's "Golden Order of Merit" in the field of "Prudent Management and the Best Supportive Bank for Tourism Projects in the Arab World", "Fastest Growing Bank in Oman" by UAE-based CPI Financial, the "Majestic Five Continents Award for Quality and Excellence" by Otherways International Research and Consultants; the "Golden Excellence Award for Corporate Social Responsibility" for the second year in a row by Arab Organisation for Social Responsibility in Dubai and the "Best Enterprise" and "Best Manager of the Year" for Bank Sohar and Dr Mohamed Abdulaziz Kalmoor respectively by the Europe Business Assembly (EBA) (Muscat Daily, 2014).

In addition, Dr Kalmoor was also honoured as the "CEO of the Year 2013" while the bank was awarded as one of the "Top Five Large Corporate Enterprises in Oman" by Alam Al Iktisad Wal Amaal. Bank Sohar was also recognised by a leading English economic and business publication as one of the top 20 corporate performers listed on the Muscat Securities Market (MSM) at the OER Top 20 Awards (Muscat Daily, 2014). One of the cornerstones of Bank Sohar's performance has been its strong corporate governance culture. It focuses on the set of processes, customs, policies, laws and practices affecting the manner in which the organization is directed, administered and controlled. The emphasis is also on relationships between various stakeholders inside and outside the organization. Shareholders welfare which is a vital aspect of corporate governance is incorporated by achieving economic efficiency to optimize economic results (Corporate Governance Report, 2014).

The basic framework of the bank's corporate governance requires that the Board of Directors, Sharia Supervisory Board (SSB) for its Islamic Banking Window (Sohar Islamic) and managers should (Corporate Governance Report, 2014):

- Maintain the highest standard of corporate governance and regulatory compliance;
- Promote transparency, accountability, responsiveness and social responsibility;
- Conduct its affairs with its stakeholders, customers, employees, investors, vendors, government and the society at large in all fairness and in an open manner;
- Create an image of the bank as a legally and ethically compliant entity;

An important tenet in the corporate governance at Bank Sohar is the emphasis on Anti-Money laundering (AML).

3.2 Bank Sohar integrity-related practice

To cater to AML practices towards superior Corporate Governance, the bank's role is to establish and maintain procedures to ensure and monitor compliance with the reporting and recordkeeping requirements.

To cater to the AML and other risk management requirements, Bank Sohar has developed a Corporate Governance Philosophy within the directives and guidelines of the Central Bank of Oman (CBO), the Capital Market Authority (CMA) and the Commercial Companies law of Oman (CCL). The policy integrates four universal values synonymous with corporate governance, namely, – accountability, fairness, responsibility and transparency (Corporate Governance Report, 2014).

Bank Sohar maintains specific focus on AML practice due to two driving forces – firstly, the compliance requirements from the authorities and secondly, its core value of maintaining “integrity”. When interviewed on 28th April, 2014, Mr. Amran al Balushi, Chief Manager of Bank Sohar confirmed the components of the AML practice at Bank Sohar. They include;

- Formation of clear policies and procedures in the form of clear documentation, internal audit for all the branches of the bank and its subsidiaries in home country and outside. These policies are specific to the relationships with shell banks (a bank incorporated in a jurisdiction in which it has no physical presence and which is unaffiliated with a regulated financial group), Potentially Exposed Persons (PEPs) or their affiliates.
- Risk assessment with appropriate due diligence processes to evaluate various categories of customers, their account details along with the transaction types. Incorporation of a system that not only maintains a record for each new customer with required details but also identifies and maps high risk clients.
- Identify and report suspected information obtained by screening customers and transactions against list of persons, entities or countries issued by government-competent authorities.
- Monitoring program for unusual and potentially suspicious transaction activity that covers fund transfers and monetary instruments such as travelers’ checks, money orders, etc.

3.3 Policy development

As per the guidelines of CBO, the development of the policy is carried out by various subcommittees created by the Board of Directors. The committees’ responsibility is to ensure focused and specialized attention to specific issues related to governance. As per the Corporate Governance Report of Bank Sohar in 2014, the subcommittees and their primary responsibilities are as follows:

Figure 3-1 Organizational Chart

The role of Audit Committee is to assess and review the financial reporting system of the bank to ensure that the financial statements are correct, sufficient and credible. The committee reviews the adequacy of regulatory compliance, regulatory reporting, internal control systems, structure of internal audit departments, and compliance of their staffing and holds discussions with the internal/external auditors on significant findings and control environment. The Head of Internal Audit and Head of Compliance report to the Audit Committee.

The Head of Internal Audit is responsible for the operational control as per the framework. The Head of Compliance ensures that the bank complies with all the Laws, rules and regulations as applicable in Oman and internationally. The Executive Committee at Bank Sohar plays a significant role to ensure implementation of the business Strategy, policies and procedures of the Bank. The committee ensures implementation of appropriate codes of business conduct to nurture ethical behavior to protect the bank's integrity and that of its shareholders. The responsibilities of Credit Approvals Committee include oversight and governance in relation to the credit performance of the Bank. The Risk Management Committee's role is to assist the Directors to discharge the responsibilities of oversight and governance in the risk performance sector. The committee ensures implementation of risk strategy and ensures that a robust risk framework is in place. The Committee also provides guidance and direction on all credit, market, interest rate, liquidity and operational risk policy matters. The Head Office Project committee functions as an Audit committee for headquarters project in the areas of risk management, project scope, budget, resource allocation, procurement strategies and the resolution of significant issues on management of the headquarters project. Each of the committees forms the policies pertaining to their area in line with the directives of CBO and international banking requirements.

3.4 Process for embedding the practice within the organization

"The training centre has a vital role in embedding the practice within Bank Sohar" says Mr. Amran al Balushi. AML policies are first oriented to employees at various levels using a series of methods. Firstly, AML policies are posted online on the intranet and all employees are required to sign in and read the policy. Then, they are made to answer 15 questions that reflect the level of understanding of the employees to ensure practice at the workplace. For other policies, employees are selected and sent for in-house training sessions conducted in classrooms. Bank Sohar has a well-established learning center consisting of several senior trainers who carry out these trainings. In-house programs last from half a day to sometimes a full day. The Centre is also responsible for designing and documentation of new training materials. Further, some employees are sent to College of Banking and Financial Studies (CBFS) to attend additional courses about topics like Information Security Awareness (ISA) etc. In the process of implementation, the primary obstacles identified include budget and the time allocation for such activities. However, with the support from the higher levels, these issues are resolved. Many employees have undergone the phased training sessions and have been found to actively use these skills and knowledge at the workplace.

4. Identification, reporting of issues and enforcement

Issues that fail to comply with the regulatory and AML framework are identified by the employees in the concerned department and reported to their immediate line manager as per Mr. Amran al Balushi. Depending on the sensitivity and seriousness of the issue and the person suspected in the malpractice, the line manager escalates the issue to the Internal Audit and Compliance department. If the immediate manager is the suspect, the employee is required to approach the manager within the department. Whistle blowing is also encouraged which either can be through writing or by calling a telephone number dedicated to whistle blowing. The Internal Audit and Compliance department takes it up with the appropriate sub-committee at the higher level. The respective committees present their reports to the Board of Directors.

During the interview Mr. Amran al Balushi confirmed that external auditors, internal auditors, and compliance officers are responsible for enforcement at Bank Sohar. During this enforcement process, compliance officers review all the departments and ensure that all policies and procedures are complied without any failure. If not, then, they report to the management. Internal Auditors do the same job and try to dig out any lapses in existing policies and procedures that may need development. Sometimes, they find old policies which had not been developed, and the same is reported to the management. External Auditors assess the financial details and try to unearth any misreporting or miscalculation of facts and figures. In addition, the fraud auditors check for frauds by ensuring compliance to the established policies and procedures. It can be said that enforcement is carried out jointly by different teams who at the end of the day make sure that the practices are enforced for better governance. The following lessons were learned as a result of this study:

- a) Effectiveness of any process depends on the degree of inclusion. The process of inclusion makes sure that the whole organization works as a team to design fool-proof policies leading to better acceptance and implementation;
- b) Following best practices ensure effectiveness and profitability of any organization;
- c) Quality at source in terms of sound practices is paramount to total quality, thereby, ensuring creation of customer loyalty and equity. This is a path to sustainability, finally, culminating in enriched stakeholder value.

5. Conclusion

Money laundering or the financial means of organized crime are extremely difficult to tackle due to various reasons. Hence, it becomes joint responsibility of the central bank of the country along with the individual financial institution itself to formulate policies towards identification, enforcement and reporting of any malpractices. This case study reviewed the structural framework adopted by Bank Sohar to keep updating with the changing environmental conditions. A brief assessment of policies, process and practices for embedding and enforcing AML practices undertaken at Bank Sohar was conducted. It was found that the

practices follow the recommendations of FATF and other international studies in an effort to keep Bank Sohar free from any AML concerned potential threats.

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