

WHY IS THE SUPERINTENDENT OF FINANCIAL SERVICES POLICING OUR IRAN SANCTIONS?

NY's Superintendent of Financial Services, Benjamin Lawsky, yesterday dropped the hammer on the UK's Standard Chartered Bank, accusing it of doctoring financial documents to facilitate the laundering of Iranian money through its US banks.

Like Yves, I think one of the most striking details about this story is that SFS—and not Treasury's Office of Foreign Assets Controls—is making the accusation.

But it also appears that Lawsky has ended run, as in embarrassed, the Treasury and the New York Fed. As part of its defense, SCB contends it was already cooperating with Federal regulators:

In January 2010, the Group voluntarily approached all relevant US agencies, including the DFS, and informed them that we had initiated a review of historical US dollar transactions and their compliance with US sanctions...The Group waived its attorney-client and work product privileges to ensure that all the US agencies would receive all relevant information.

The agencies in question are "DFS, the Department of Justice, the Office of Foreign Assets Control, the Federal Reserve Group of New York and the District Attorney of New York."

[snip]

The lack of action by everyone except the lowly New York banking supervisor is mighty troubling. The evidence presented in Lawskey's filing is compelling; he clearly has not gone off half cocked. Why has he pressed forward and announced this on his own? The Treasury Department's Office of Terrorism and Financial Intelligence has supposedly been all over terrorist finance; the consultants to that effort typically have very high level security clearances and top level access (one colleague who worked on this effort in the Paulson Treasury could get the former ECB chief Trichet on the phone). For them not to have pursued it anywhere as aggressively as a vastly less well resourced state banking regulator, particularly when Iran is now the designated Foreign Enemy #1, does not pass the smell test.

Normally, we'd see accusations like SFS released today from Treasury's OFAC, perhaps (for charges as scandalous as these) in conjunction with the NY DA and/or a US Attorney. And yet OFAC has had these materials in hand for 2 years, and has done nothing.

In fact, we have a pretty good idea what OFAC's action would look like, because earlier this year it sanctioned ING for actions that were similar in type, albeit larger in number (20,000 versus 60,000) and far larger in dollar amount (\$1.6 billion involving Cuba versus \$250 billion involving Iran). Both banks were doctoring fields in SWIFT forms to hide the source or destination of their transfers.

ING:

Beginning in 2001, ING Curacao increasingly used MT 202 cover payments to send Cuba-related payments to unaffiliated U.S. banks, which would not

have to include originator or beneficiary information related to Cuban parties. For serial payments, up until the beginning of 2003, NCB populated field 50 of the outgoing SWIFT MT 103 message with its own name or Bank Identifier Code, Beginning in the second quarter of 2003, NCB populated field 50 with its customer's name, but omitted address information. ING Curacao also included its customer's name, but no address information, in field 50 of outgoing SWIFT messages.

SCB:

Rather than institute [a required to ensure the funds didn't come from Iran], SCB instead conspired with Iranian Clients to transmit misinformation to the New York branch by removing and otherwise misrepresenting wire transfer data that could identify Iranian parties. For example, regarding necessary wire transfer documentation, SCB instructed CBI/Markazi to "send in their MT 202"s with a [SCB London"s business identifier code] as this is what we required them to do in the initial set up of the account. Therefore, the payments going to NY do not appear to NY to have come from an Iranian Bank." (emphasis added). SCB also accomplished this subterfuge by: (a) inserting special characters (such as ".") in electronic message fields used to identify transacting parties; (b) inserting phrases such as "NO NAME GIVEN" or "NOT STATED" in lieu of requested information that would identify Iranian Clients; and (c) employing a system known as SCB"s "repair procedure," whereby SCB overseas employees screened payment messages – before they were communicated to its New York branch – in order to ascertain if

any messages contained information that identified Iranian Clients.

And both banks accomplished such fraud by using their global reach to launder the payments indirectly.

I'm most curious about how SFS got this lead. It appears that SCB revealed these violations to SFS and other regulators in 2009. And whatever the other law enforcement agencies are doing, SFS has gone after SCB for ongoing behavior that violates Anti-Money Laundering.

In early 2009, after being contacted by certain law enforcement authorities, SCB conducted an internal investigation into its OFAC procedures. In May 2010, more than a year after it had commenced its own investigation, and notwithstanding its obligation to notify the Department of these matters promptly, SCB finally informed the Department of its review.

▪ *At a meeting in May 2010, SCB assured the Department that it would take immediate corrective action. Notwithstanding that promise, the Department's last regulatory examination of the New York branch in 2011 identified continuing and significant BSA/AML failures, including: An OFAC compliance system that lacked the ability to identify misspellings and*

variations of names on the OFAC sanctioned list.

- *No documented evidence of investigation before release of funds for transactions with parties whose names matched the OFAC-sanctioned list.*
- *Outsourcing of the entire OFAC compliance process for the New York branch to Chennai, India, with no evidence of any oversight or communication between the Chennai and the New York offices.*

A likely explanation is that these unnamed other law enforcement agencies are working up yet another Deferred Prosecution Agreement that claims the companies have cooperated when they really haven't—as Treasury did with ING and even more so with JP Morgan Chase—SFS used its regulatory position to expose the ongoing behavior.

If Yves and I are right, in addition to the outrage at SCB (and Deloitte and Touche, which collaborated in this fraud), SFS' actions should elicit discussions about why Treasury continues to insist banks are cooperating when they really aren't.

My wildarsed guess, in this case, is that we have an understanding with our allies that they'll allow us to require the rest of the world to comply with our sanctions so long as it doesn't affect that country's businesses. That is, I suspect countries like Britain are happy

to comply with our sanctions so long as British banks don't lose competitive advantages as a result. Of course, these sanctions are different that—say—our stupid Cuba sanctions in that the UK is as enthusiastic about sanctioning Iran into docility as the US is, and this scheme is all about retaining lucrative business with Iran.

But we may never learn what reason that is, because that would make things uncomfortable for the entities that claim there is rule of law for banks while they ensure that usually is not the case.

Update: Superintendent spelling error fixed, thanks to joanneleon.