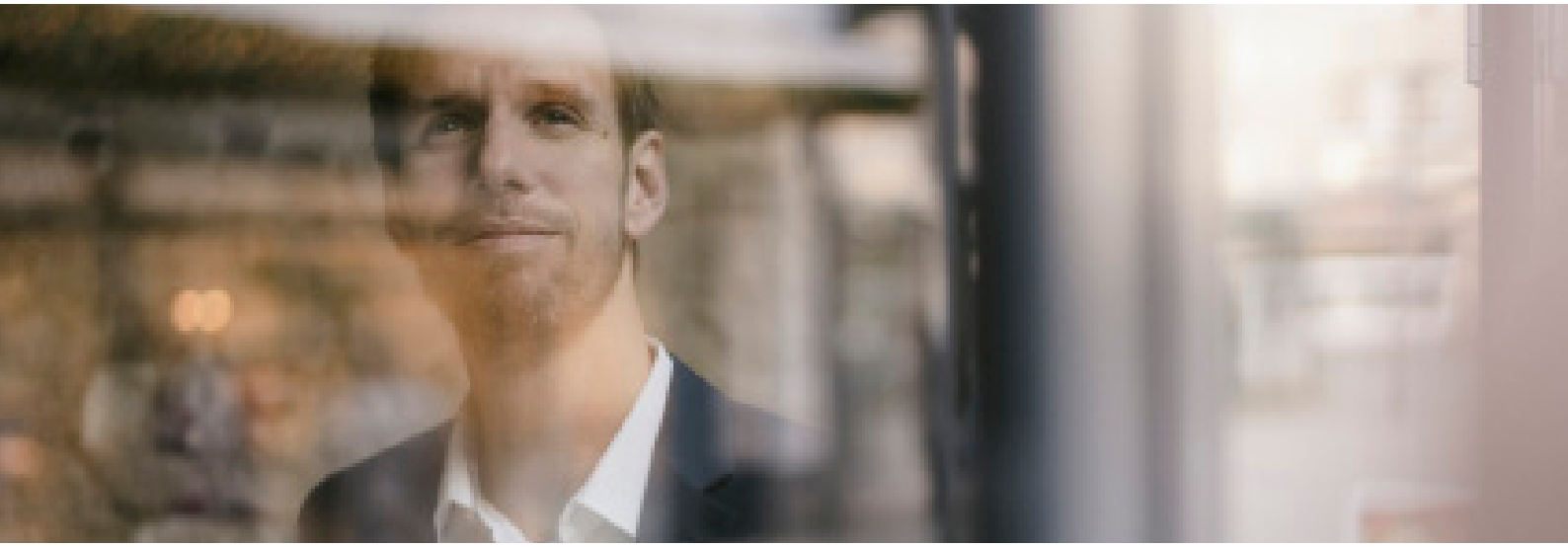
Will you get caught out by dirty laundry?

What are the personal liabilities for directors and officers under Australian anti-money laundering laws and regulations, how can the risks be mitigated and what part can insurance play?



The anti-money laundering (AML) regulatory framework is constantly evolving, particularly in Australia. With an increasing volume of global transactions and creative money laundering schemes, there can be concerning personal liability consequences for senior executives and individuals for instances of non-compliance.

Over the past decade, total fines and penalties paid by the global banking industry to prudential regulators for conduct-related matters is estimated to be up to US$470 billion. Intended to drive desirable conduct and culture within financial institutions, the implementation and scope of accountability regimes vary by country.

Enforcement, which has ramped up considerably across the globe in the last three years, generally involves fines, penalties or pecuniary sanctions (civil and/or criminal) levied against the institution and the individuals responsible for oversight of the transaction monitoring framework.

There are several well-publicised examples of recent Australian enforcement actions:

- Westpac was fined AU$1.3 billion for failing to submit reports that would assist the Australian Transaction Reports and Analysis Centre (AUSTRAC) in detecting money laundering and terrorist financing activity.
- The Commonwealth Bank was fined AU$700 million for late filing thousands of transactions and failing to properly monitor transactions on 778,380 accounts to check for money laundering red flags.
- An investigation into Crown Resorts found that, between 2012 and 2016, millions of dollars were transferred by customers through Crown hotels for ‘services’ in contravention of AML laws.

No individuals were fined in these cases however the situation is different in other jurisdictions. In the UK, the Financial Conduct Authority (FCA) published a decision relating to the CEO of a UK Authorised Bank for failings in relation to AML systems and controls, imposing personal fines.

AUSTRAC continues to be active in its investigations. It recently ordered an external audit into Australian stockbroking group, Bell Potter, following findings of compliance weaknesses in the group’s systems, controls and record keeping.

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There has also been a call to widen the current Australian AML legislation, with an inquiry referred to the Senate's Legal and Constitutional Affairs References Committee into the adequacy and efficiency of the current regime. The Committee's report and recommendations are expected at the end of March 2022.

What part does insurance play?

In Australia, a company cannot indemnify its directors and officers for civil penalties under the Corporations Act 2001 (Cth) and Competition and Consumer Act 2010 (Cth). D&O policies can provide an important financial backstop for individual insured persons in such instances, as long as the policy is specifically structured to contemplate the level of exposure.

Insurance cover is determined on a case-by-case basis. Policies may provide cover for civil fines and pecuniary penalties unless the insurer is legally prohibited from paying such fines or penalties in the jurisdiction where the claim is determined. In the UK, the FCA expressly prohibits insurance for fines, whereas in Australia, civil fines and penalties are generally insurable at law. Accordingly, D&O policies usually include cover for these fines, subject to the usual exclusions for deliberately dishonest or fraudulent conduct or conduct which involves a wilful breach of duty owed to the company.

In addition, PI and D&O policies will typically provide cover for the legal costs incurred by a director and/or senior executive where they are being investigated by a regulator such as AUSTRAC and have received a notice to attend an interview or produce documents, for example. Whether the PI or D&O policy responds in this scenario will depend on the nature of the investigation but cover for regulatory investigations is typically only available to individuals and not the costs of the entity responding to the investigation.

Amendments to the AML/CTF Act came into effect on 17 June 2021, which introduced a raft of measures aimed at further strengthening Australia's AML framework, largely relating to the reporting entity's liability. Senior executives should be aware of these amendments and work towards integrating compliance into their organisation's internal AML programs, to manage risk and minimise potential insurance policy coverage issues.

The Australian regulatory framework

In Australia, AML regimes have been introduced via the Anti-Money Laundering and Counter-Terrorism Financing Act 2006 (the AML/CTF Act) which applies to the financial services, bullion, gambling and digital currency exchange sectors. Part 10.2 of the Federal Criminal Code Act 1995 (Cth) provides the definition of money laundering offences. Asset recovery provisions that allow law enforcement to pursue the recovery of assets linked to offences after a conviction are contained in the Proceeds of Crime Act 2002 (Cth).

AUSTRAC is Australia's financial intelligence agency with regulatory responsibility for enforcement of the AML and counter-terrorism regime. Australia's criminal money laundering laws also have extraterritorial application under the Code.

Key regulatory changes introduced in 2021

1. Customer identification procedures: entities can rely on third party identification procedures if certain criteria are met
2. Correspondent banking relationships: more stringent obligations on these involve prohibitions on relations with financial institutions that permit their accounts to be used by a shell bank and new requirements for due diligence assessments
3. Tipping-off offences: entities remain prohibited from disclosing the making of suspicious matter reports, with new exceptions to address some of the complexities the regime and enhance collaboration between various agencies
4. Access to information: greater information sharing between the public sector, private sector and foreign agencies/governments to enhance investigation capabilities
5. Cross-border movements of money: new streamlined provisions on cross-border movement of physical currency, including a requirement that travellers report all such movements of "monetary instruments" over $10,000 and an expansion of the offence provisions.

FAQs

The following FAQ may be helpful for executives and individuals in key functional roles, including those responsible for implementing and maintaining adequate AML programs.

Q. Is an insurance policy available that provides coverage for individuals and executives responsible for carrying out key compliance and AML functions within regulated entities?

A. A D&O insurance policy provides legal liability protection for individual directors and officers of an insured organisation. If the individual is not being indemnified by the organisation (as a result of the company's insolvency or a legal prohibition, for example), insurance cover may be accessed by the individual under the D&O policy, commonly referred to as Side A cover.

Q. Who is covered under a D&O insurance policy?

A. The definition of an insured person under a D&O policy varies, however it typically includes duly elected or appointed directors and officers and may extend to include employees of the insured organisation. Most policies include others in key positions, such as the organisation's compliance officers and money laundering reporting officers in each jurisdiction.

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Q. Does the policy cover fines and penalties for individual insured persons?

A. Globally, most D&O policies do not contemplate coverage for fines and penalties. Nevertheless, in the context of an individual's failure (in good faith) to comply with applicable AML reporting obligations that can trigger a civil fine or penalty, coverage has commonly been included for policies issued in Australia. However, in the wake of the banking Royal Commission which handed down its report in February 2019, this cover has been excluded in many cases.

Criminal fines and penalties for deliberate or egregious acts (including aiding and abetting) would not be contemplated for coverage under a D&O policy.

Q. What conditions must be met for coverage to apply?

A. Policies will vary, sometimes significantly by jurisdiction, however, where the policy covers civil fines and penalties, the insured person must have acted honestly and in good faith. Other policies may provide cover where the fine or penalty is predicated on unintentional conduct. We encourage individuals to review their organisation's D&O policy for conditions specific to them.

Q. Are there any exclusions that may apply?

A. Certain exclusions could negate cover under a D&O policy. D&O policies will always exclude cover for deliberately dishonest, wilful or fraudulent conduct and any personal profit or financial advantage gained to which the individual insured person was not legally entitled. Such conduct must be the subject of a judicial finding or established by way of admission.

With the evolution of Australia's AML regime and increased regulatory activity in recent years, there are examples of exclusions being applied to D&O policies which exclude cover for matters relating to money laundering.

Q. Will a D&O insurer provide defence costs if the allegations made against the individual insured person lead to a fine or penalty being imposed?

A. Generally, D&O insurers cover defence costs arising from allegations that could lead to a fine, penalty or pecuniary sanction being imposed on an individual insured person. If there is a finding of criminal conduct or other deliberate or dishonest conduct, defence costs may be repayable by the individual insured person to the D&O insurer.

Q. What is the limit of liability available for civil fines or penalties under a D&O policy?

A. The limit of liability varies greatly from one policy to another, however it is not unusual for coverage for civil fines and penalties to be limited to a modest amount.

Q. Is there a deductible applicable to the coverage provided to an individual insured person?

A. No, there is not typically a deductible applicable to the Side A coverage that applies to individual insured persons covered under a D&O policy.

It is recommended that organisations talk to their broker to understand the breadth, scope and limitations of coverage afforded under their D&O policies. At WTW we can assist organisations in navigating through the regulatory expectations and how insurance can play its part in providing the appropriate level of protection for senior executives and anti-money laundering officers.

This is the first article in a two-part series. The second article will be published following the release of the Australian Legal and Constitutional Affairs References Committee report into the adequacy and efficiency of the current anti-money laundering regime.

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