

DISPUTE RESOLUTION ALERT

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CORPORATE INVESTIGATIONS:

RISKY BUSINESS – THE STATUS AND DECLASSIFICATION OF POLITICALLY EXPOSED PERSONS AFTER EXITING OFFICE

The Financial Action Task Force (FATF) defines a politically exposed person (PEP) as an individual who is or has been entrusted with a prominent public function. PEPs are at a greater of risk of exposure to bribery and corruption because of their prominent and influential positions. As a result, enhanced due diligence measures are required when dealing with PEPs.

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FATF'S recommendations 12 and 22 specifically require financial institutions and designated non-financial business and professions to implement enhanced due diligence measures when dealing with PEPs.



The Financial Action Task Force (FATF) defines a politically exposed person (PEP) as an individual who is or has been entrusted with a prominent public function. The FATF is an independent intergovernmental body established by the G-7 summit held in Paris in 1989. Its mandate includes developing policies to combat money laundering and terrorist financing in the global financial system. South Africa is a member of the FATF.

The FATF categorises foreign and domestic PEPs as individuals who have been entrusted with a prominent public function in a foreign country or domestically. International organisation PEPs are those individuals entrusted with a prominent public function, such as positions in senior management, by an international organisation.

PEPs are at a greater of risk of exposure to bribery and corruption because of their prominent and influential positions. For instance, a PEP may possess political influence, authority over procurement processes or access to state funds.

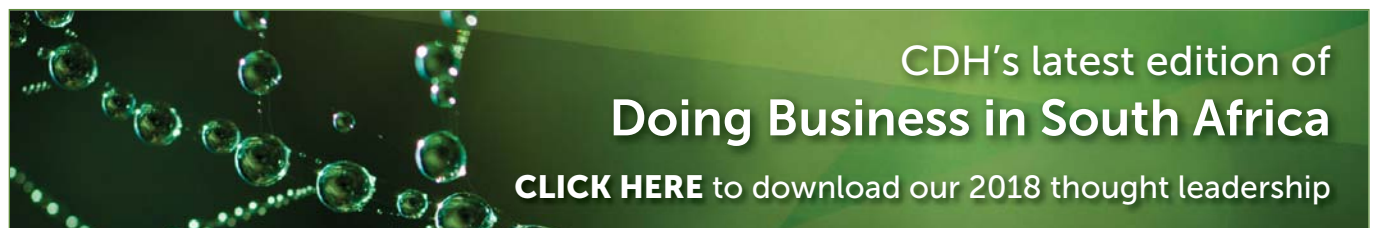
The FATF has published recommendations which provide a comprehensive framework of anti-money laundering (AML) and counter-terrorist financing measures which are recognised internationally as the AML standard of best practice.

Recommendations 12 and 22 specifically require financial institutions (FIs) and designated non-financial business and

professions (DNFBPs) to implement enhanced due diligence (EDD) measures when dealing with PEPs. These include:

- having appropriate risk management systems in place to determine whether a customer or its beneficial owner is a PEP;
- obtaining senior management approval for establishing business relationships with PEPs;
- taking reasonable measures to establish the source of wealth and the source of funds; and
- conducting enhanced ongoing monitoring of the business relationship.

Family members and close associates of PEPs are also subject to EDD because of their potential instrumentality in concealing, moving or disguising the proceeds of crime (or ownership thereof) on behalf of a PEP. South Africa has passed legislation that requires EDD of PEPs. This is set out in the Financial Intelligence Centre Act, No 38 of 2001.



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It is a widely accepted AML principle that mere classification as a PEP does not suggest wrongdoing or involvement in corruption and FIs should not stigmatise PEPs on that basis.



According to the Wolfsberg Group - an association of 13 global banks aimed at developing guidance to mitigate financial crime risks within the private banking sector - there is no agreed or accepted method for determining the period to declassify a PEP once the individual has exited the office which gave rise to the initial classification.

The local division of the Gauteng High Court considered this issue, along with the question of whether continued listing as a PEP is defamatory, in a recent judgment: *Kassel v Thompson Reuters (Markets) SA* (16/34227) [2018] ZAGPJHC 413 (12 June 2018).

The case concerned an application made by Kassel who is listed as a PEP in the World-Check database hosted by Thompson Reuters. World-check is an international database used by its subscribers, which include FIs and DNFBPs, to identify whether individuals are listed as PEPs as part of the process of fulfilling their EDD obligations. Kassel's classification as a PEP occurred as a result of his former position as a senior official of a state-owned enterprise.

Kassel argued that his continued listing as a PEP, long after his exit from the office which gave rise to the initial classification, is defamatory. He, accordingly, argued that his name should be removed from the listing.

In considering the matter, the High Court reasoned that political exposure attached to individuals by reason of their occupancy of a high office does not itself imply that such individuals have abused their office or are otherwise corrupt. It reasoned further, that it is the office itself which gives rise to the risk because of the influence attached

to it. There is, accordingly, no presumption whatsoever that merely listing a person as a PEP renders them suspect. The court further stated that listing a person as a PEP and the office that gives rise to this designation neither anticipates nor implies the outcome of the EDD procedures that are to be undertaken.

The High Court's finding is aligned with the widely accepted AML principle that mere classification as a PEP does not suggest wrongdoing or involvement in corruption and FIs should not stigmatise PEPs on that basis. In its guidance note, the FATF explicitly states that refusing a business relationship with a PEP simply based on their PEP status is contrary to the letter of its recommendations.

In the circumstances, the High Court found that Kassel's continued listing as a PEP is not defamatory and, at most, amounts to an incorrect assessment of Kassel's exposure to political risk.

The categorisation of PEP does not preclude a FI from entering into or maintaining a business relationship with a PEP. It merely necessitates EDD measures commensurate to the level of risk posed by that PEP. The application of varied levels of due diligence commensurate to the degree of risk identified in relation to a potential customer is central to the risk-based approach (RBA) to customer due diligence. The RBA is the internationally preferred approach to customer due diligence in the banking sector.

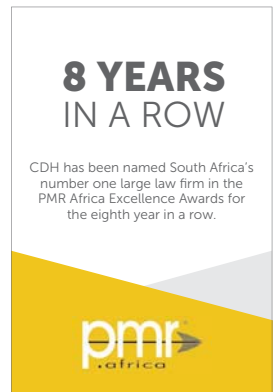
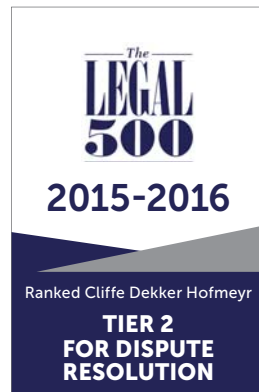
Zaakir Mohamed and Krevania Pillay



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OUR TEAM

For more information about our Dispute Resolution practice and services, please contact:



Tim Fletcher
National Practice Head
Director
T +27 (0)11 562 1061
E tim.fletcher@cdhlegal.com



Thabile Fuhrmann
Chairperson
Director
T +27 (0)11 562 1331
E thabile.fuhrmann@cdhlegal.com

Timothy Baker
Director
T +27 (0)21 481 6308
E timothy.baker@cdhlegal.com

Roy Barendse
Director
T +27 (0)21 405 6177
E roy.barendse@cdhlegal.com

Eugene Bester
Director
T +27 (0)11 562 1173
E eugene.bester@cdhlegal.com

Tracy Cohen
Director
Business Development
T +27 (0)11 562 1617
E tracy.cohen@cdhlegal.com

Lionel Egypt
Director
T +27 (0)21 481 6400
E lionel.egypt@cdhlegal.com

Jackwell Feris
Director
T +27 (0)11 562 1825
E jackwell.feris@cdhlegal.com

Anja Hofmeyr
Director
T +27 (0)11 562 1129
E anja.hofmeyr@cdhlegal.com

Julian Jones
Director
T +27 (0)11 562 1189
E julian.jones@cdhlegal.com

Tobie Jordaan
Director
T +27 (0)11 562 1356
E tobie.jordaan@cdhlegal.com

Corné Lewis
Director
T +27 (0)11 562 1042
E corne.lewis@cdhlegal.com

Janet MacKenzie
Director
T +27 (0)11 562 1614
E janet.mackenzie@cdhlegal.com

Richard Marcus
Director
T +27 (0)21 481 6396
E richard.marcus@cdhlegal.com

Burton Meyer
Director
T +27 (0)11 562 1056
E burton.meyer@cdhlegal.com

Zaakir Mohamed
Director
T +27 (0)11 562 1094
E zaakir.mohamed@cdhlegal.com

Rishaban Moodley
Director
T +27 (0)11 562 1666
E rishaban.moodley@cdhlegal.com

Byron O'Connor
Director
T +27 (0)11 562 1140
E byron.oconnor@cdhlegal.com

Ashley Pillay
Director
T +27 (0)21 481 6348
E ashley.pillay@cdhlegal.com

Lucinde Rhoodie
Director
T +27 (0)21 405 6080
E lucinde.rhodie@cdhlegal.com

Willie van Wyk
Director
T +27 (0)11 562 1057
E willie.vanwyk@cdhlegal.com

Joe Whittle
Director
T +27 (0)11 562 1138
E joe.whittle@cdhlegal.com

Pieter Conradie
Executive Consultant
T +27 (0)11 562 1071
E pieter.conradie@cdhlegal.com

Willem Janse van Rensburg
Executive Consultant
T +27 (0)11 562 1110
E willem.jansevanrensburg@cdhlegal.com

Nick Muller
Executive Consultant
T +27 (0)21 481 6385
E nick.muller@cdhlegal.com

Marius Potgieter
Executive Consultant
T +27 (0)11 562 1142
E marius.potgieter@cdhlegal.com

Jonathan Witts-Hewinson
Executive Consultant
T +27 (0)11 562 1146
E witts@cdhlegal.com

Nicole Amoretti
Professional Support Lawyer
T +27 (0)11 562 1420
E nicole.amoretti@cdhlegal.com

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JOHANNESBURG

1 Protea Place, Sandton, Johannesburg, 2196. Private Bag X40, Benmore, 2010, South Africa. Dx 154 Randburg and Dx 42 Johannesburg.
T +27 (0)11 562 1000 F +27 (0)11 562 1111 E jhb@cdhlegal.com

CAPE TOWN

11 Buitengracht Street, Cape Town, 8001. PO Box 695, Cape Town, 8000, South Africa. Dx 5 Cape Town.
T +27 (0)21 481 6300 F +27 (0)21 481 6388 E ctn@cdhlegal.com

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