



**UNIVERSITY of the
WESTERN CAPE**

LLM

**TRANSNATIONAL CRIMINAL JUSTICE: AN INTERNATIONAL AND AFRICAN
PERSPECTIVE**

RESEARCH PAPER

**AN APPRAISAL OF THE INSTITUTIONAL FRAMEWORK UNDER THE KENYAN
PROCEEDS OF CRIME AND ANTI-MONEY LAUNDERING ACT, 2009**

By

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**Research paper submitted in partial fulfilment of the requirements for the
LLM degree**

November 2017

Declaration

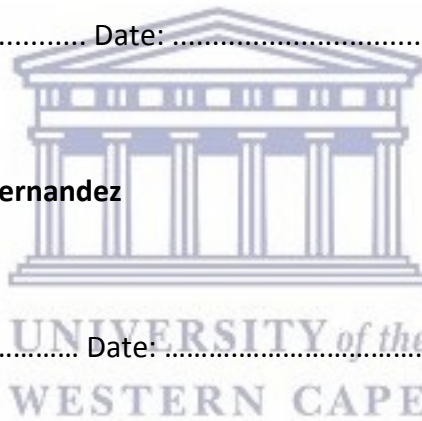
I, **Denis Wangwi Moroga**, declare that **An Appraisal of the Institutional Framework under the Kenyan Proceeds of Crime and Anti-Money Laundering Act, 2009** is my own work, that it has not been submitted for any degree or examination in any other university, and that all the sources I have used or quoted have been indicated and acknowledged by complete references.

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Dedication

To my beloved parents, Thomas Moroga and Pauline Gati, thank you for your unwavering support and inspiration.



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Acknowledgements

My sincere gratitude goes to my parents, brothers and kid sister, Nancy, for your love, support, and motivation.

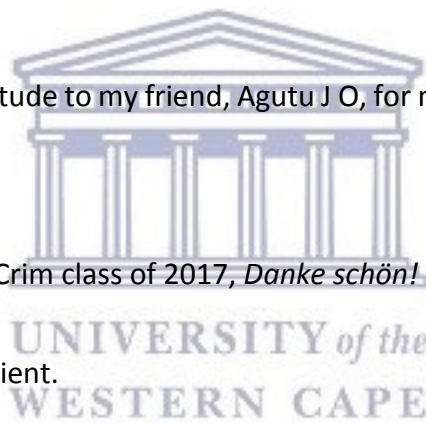
My thoughtful appreciation goes to my supervisor, Prof Lovell Fernandez, for his constructive ideas that were invaluable while writing this research paper.

Gratitude to my generous sponsor, *Deutscher Akademischer Austauschdienst (DAAD)*, for supporting my study and stay in Cape Town and Berlin. Also, my gratitude goes to Prof Werle, Prof Koen, Prof Mujuzi, Dr. Moritz and Dr. Marshet for sharing knowledge in their respective fields.

I would like to extend my gratitude to my friend, Agutu J O, for motivating me in my academic journey.

To my colleagues in the TransCrim class of 2017, *Danke schön!*

Above all, God's grace is sufficient.



Keywords

Competent authorities

Confidentiality principle

Financial institutions

Financial intelligence units

Kenya

Money laundering

Palermo Convention

Reporting institutions

Vienna Convention



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List of Abbreviations

AML	Anti-money laundering
AMLAB	Anti-Money Laundering Advisory Board
AUSTRAC	Australian Transaction Reports and Analysis Centre
CDD	Customer due diligence
CTF	Counter terrorism financing
DNFBPs	Designated non-financial businesses and professions
ESAAMLG	The Eastern and Southern Africa Anti-Money Laundering Group
FATF	Financial Action Task Force
FIC	Financial Intelligence Centre
FICA	Financial Intelligence Centre Act 2001.
FIU	Financial intelligence unit
FRC	Financial Reporting Centre
FSRB	Financial Action Task Force - Style Regional Bodies
HLP	High Level Panel on Illicit Financial Flows from Africa
KYC	Know your customer
ML	Money laundering
PEPs	Politically Exposed Persons

POCAMLA

Proceeds of Crime and Anti-Money Laundering Act 2009.

TF

Terrorism financing



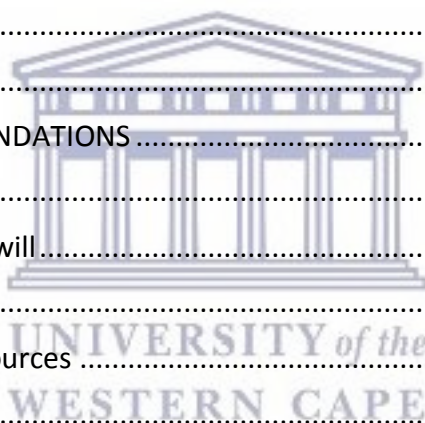
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CHAPTER ONE

INTRODUCING THE STUDY

1.1 Introduction

Money laundering (ML) evolves in tandem with global technological advancement. This phenomenon calls for multi-faceted responsive measures at national and international levels to combat this nefarious crime.¹ Today, combating ML requires co-operation among, *inter alia*, financial intelligence units (FIUs), reporting institutions, law enforcement agencies, the judiciary, as well as inter-state co-operation. In response to the ML threat, Kenya has adopted comprehensive anti-money laundering (AML) laws, such as the Proceeds of Crime and Anti-Money Laundering Act No. 9 of 2009 (POCAMLA) and the Prevention of Terrorism Act No. 30 of 2012. These, among other statutes, constitute the principal arsenal of the AML legal framework.

Also, in 2012, Kenya established its FIU, the Financial Reporting Centre (FRC) as an integral unit which works together with the Anti-Money Laundering Advisory Board (AMLAB). Another creature of POCAMLA is the Assets Recovery Agency, the task of which includes ensuring the forfeiture and confiscation of illegally obtained assets.² Notwithstanding the existence of these laws and bodies, ML continues to occur, with the authorities attaining only marginal success in its prevention and prosecution.³

This research paper aims, therefore, to interrogate the role played by the above-mentioned institutions in implementing the AML statutes. The main focus of this study will be on the structure, mandate, and powers of the FRC and AMLAB. These will be discussed against the

¹ Financial Action Task Force (FATF) Recommendation 2; Chatain PL *et al* (2009: 9).

² Sec 54 the Proceeds of Crime and Money Laundering Act (2009) (POCAMLA).

³ US Department of State Report (2017); US Department of State Report (2015); HLP Report (2015).

template of international best practices. Finally, the attendant challenges will be dealt with and the study will conclude with a set of recommendations on how to improve the efficiency of these institutions.

1.2 Background of the Study

Until 1994, Kenya did not have an AML law. The Narcotic Drugs and Psychotropic Substances Act No. 4 of 1994 was the first law to criminalise the use of proceeds from drug trafficking. As the name suggests, this Act criminalised drug related ML offences and provided for the recovery of proceeds from drug trafficking. Later, Parliament enacted the Anti-Corruption and Economic Crimes Act No. 3 of 2003 to provide for criminalisation of corruption and recovery of proceeds. In addition to these laws, the Central Bank of Kenya issued guidelines on AML to banks and mortgage companies to ensure the stability of the banking sector.⁴

Domestic and global developments, such as the 1998 US Embassy bombing in Nairobi and the 11 September 2001 terrorist attacks in the US respectively, did not nudge Kenya into formulating a comprehensive AML strategy. It was not until 2009 that Kenya enacted its first AML law, POCAMLA. In 2011, the Eastern and Southern Anti-Money Laundering Group (ESAAMLG) conducted a Mutual Evaluation for Kenya and identified a number of weaknesses of the AML measures, *inter alia*, the absence of an FIU.⁵ However, the government did not move with speed to implement the ESAAMLG recommendations.

In 2012, an alarm was sounded following Financial Action Task Force (FATF) listing Kenya as a non-compliant state.⁶ In response to this, Parliament amended POCAMLA to provide for the

⁴ Kegoro G (2004: 48).

⁵ ESAAMLG report (2011).

⁶ Kenya: Country spared from laundering blacklist Capital FM 26 October 2012, available at <http://allafrica.com/stories/201210270123.html> (accessed 25 February 2017).

establishment of the FRC. In addition, Parliament enacted the Prevention of Terrorism Act No. 30 of 2012 to criminalise the financing of terrorism.

Following Kenya's rapid response, the FATF removed Kenya from its watch list in 2014.⁷ Despite enacting AML laws, implementation remains an uphill task in Kenya. The country continues to be exposed to the risk of ML/TF from all quarters. Since the commencement of the war against the Al-Shabaab militia in Somalia, Kenya has experienced a series of terrorist attacks by the militia.⁸ Kenya is a major transshipment point for goods destined for land-locked countries such as Uganda and Rwanda. This makes the country vulnerable to predicate crimes such as smuggling of contraband goods and narcotic drugs.⁹

Also, the collapse of banks¹⁰ and grand corruption schemes in the last five years underscores the underlying ML threat and the inefficiency of the AML measures. The recent National Youth Service corruption scandal has shown that grand corruption still takes place in the public sector and that banks, too, could be facilitating concealment of the proceeds of corruption.¹¹ Surprisingly, most perpetrators of these crimes remain at large. Therefore, the failure to prevent these crimes from occurring and the resultant failure to prosecute the alleged perpetrators show that there is a massive enforcement deficit that requires urgent response.

⁷ FATF *Improving Global AML/CTF Compliance: On-Going Process* 27 June 2014.

⁸ Examples of terrorist attacks include the Garris University students attack (2015) and the Westgate mall terrorist attack (2013).

⁹ Hall J "Kenya set to BLOW UP £15million Norwegian cargo ship after 'white powder' was discovered on board because it is the country's policy to sink any vessel caught with drugs in its waters" 24 September 2015 *Mailonline*, available at <http://www.dailymail.co.uk/news/article-3247444/Kenya-set-BLOW-15-million-Norwegian-cargo-ship-white-powder-discovered-board-country-s-policy-sink-vessel-caught-drugs-waters.html#ixzz4wP1tLomo> (accessed on 20 October 2017).

¹⁰ See "A list of Kenyan Banks that have collapsed" available at <http://www.infohub.co.ke/2016/04/a-list-of-collapsed-kenyan-banks.html> (accessed 10 October 2017).

¹¹ Njagih M "National Youth Service (NYS) probe turns to Sh6.3b paid through 28 banks" 26 November 2016 *The Standard Digital*, available at <https://www.standardmedia.co.ke/article/2000224870/national-youth-service-nys-probe-turns-to-sh6-3b-paid-through-28-banks> (accessed 10 October 2017).

More recently, POCAMLA has been amended to widen the mandate and to reinforce the capacity of FRC, AMLAB and the Asset Recovery Agency.¹² Also, Kenya is yet to join the Egmont Group, (the international association of various FIUs) so as to be fully integrated into the wider global AML strategy. It is, therefore, necessary to evaluate the suitability of Kenya's AML institutional framework in the light of global standards and against the laws of other jurisdictions.

1.3 Research Problem

The FRC started its work after the enactment of POCAMLA on 12 April 2012.¹³ It was established in compliance with the FATF Recommendation 29.¹⁴ The FRC performs core duties of an FIU, namely, receiving, analysing and disseminating information to the appropriate authorities. Even though the FRC continues to report to the competent authorities, no meaningful results have so far been achieved. The question, therefore, is whether the FRC, as established under POCAMLA, is adequately equipped to realise its objectives as a central AML institution.

AMLAB became fully operational on 12 June 2011. The multi-agency AMLAB was established in accordance with the FATF Recommendation 2, which calls for effective inter-agency co-ordination in combating ML/TF.¹⁵ Its core mandates include formulating AML policies and underpropping the FRC. Given that AMLAB oversees the work of the FRC, the weaknesses of the latter are partially attributable to the former. Therefore, this study will look also into the composition and mandate of AMLAB.

¹² POCAMLA was enacted in 2009 and commenced in 2011. Since then it has been amended through Amendment Act No. 9 of 2009, Act No. 51 of 2012, Act No. 14 of 2015 and recently POCAMLA (Amendment) Act, 2017.

¹³ The FRC Background <http://frc.go.ke/about-frc/background.html> (accessed 11 March 2017).

¹⁴ FATF Recommendation 29 (2012).

¹⁵ Sec 49 of POCAMLA; ESAAMLG Report (2011: 200).

1.4 Research Question

The question which this study will seek to answer is: To what extent are the above-mentioned institutions equipped to fulfil their respective AML functions under POCAMLA, assessed against international best practices?

1.5 Limitations of the Study

The aim of this paper is to evaluate the institutional framework that Kenya has established under POCAMLA to enable it to combat ML and related crimes effectively. The study limits itself to the FRC and AMLAB. Since these institutions do not operate in isolation, the paper will discuss also the roles played by other Kenyan institutions insofar as their operations intersect with the country's AML strategy.

1.6 Research Methodology

This research will be based on qualitative research methods. It will rely on both primary sources such as international instruments and agreements, parliamentary enactments, case law and official reports, as well as secondary sources such as books, journal articles, media reports and electronic sources.

1.7 Literature Review

In devising an effective AML strategy, it is imperative to consider the ultimate goal. Even though seizure, asset forfeiture and prosecutions are key aspects of the AML discourse, Stessens cautions against losing sight of the ultimate goal, which is to reduce crime.¹⁶ He proposes that all strategies should be reconfigured to focus on the overarching goal of reducing crime. Further, he observes that reporting suspicious transactions without any

¹⁶ Stessens G (2008: 420).

meaningful prosecution of ML and predicate crimes obscures the main goal of preventing and reducing crime. Stessens further acknowledges the centrality of FIUs in information sharing in combating ML and other economic crimes.¹⁷ He describes different models of FIUs and discusses their key principles, such as the secrecy surrounding the workings of FIUs and the speciality principle.¹⁸ Therefore, drawing from his work, this research will interrogate the extent to which the FRC is empowered to undertake its duties while adhering to these core guiding principles for FIUs.

Simwayi and Haseed¹⁹ conducted a comparative analysis of FIUs in combating ML. In their analysis, they compared FIUs in Zambia, Zimbabwe and Malawi. Their research focused on the structure of the FIUs, but did not take into account the possible challenges that these FIUs face in their daily undertakings. Also, while noting the few publications on this topic, they conclude by calling for more research which is directed at devising the best model of an FIU. This research paper uses the Kenyan FIU as a case study, without proposing an ideal model of FIUs. FIUs need to be evaluated independently, having regard to the context within which they function and the ML/TF threats to which the country concerned is exposed.

Broek²⁰ examines various models of supervision under the preventive AML policy adopted by member states of the European Union. One of the models considered is where the FIU is at the apex of supervising the implementation of AML measures. She considers such a model to be of great advantage since the FIU ensures comprehensive compliance reviews by focusing only on institutional compliance with AML/CTF measures. On the flipside, she considers

¹⁷ Stessens G (2008: 421).

¹⁸ The duty to secrecy principle is based on the fact that FIU receive information from the banks among other agencies, they are under obligation to maintain secrecy of the information. The speciality principle defines the scope of using information shared to an FIU. See Stessens G (2008: 193).

¹⁹ Simwayi M & Haseed M (2012: 15).

²⁰ Broek M (2014: 163).

inadequate resources and lack of knowledge in operations of various reporting institutions as the main challenge. This is mainly because supervision may cause the FIU to stray from its core mandate of receiving, analysing and disseminating information. Kenya has adopted a similar model where its FIU, the FRC, is at the apex. Therefore, this research will seek to determine the efficacy of this model in the Kenyan context and how Kenya is prepared to address the attendant challenges.

1.8 Chapter Outline

Chapter two of this paper will discuss the evolution of the global framework for combating ML and the development of FIUs.

Chapter three will examine the structure, mandate and functions of the Kenyan FRC and AMLAB and the extent to which they meet international best practices.

Chapter Four will analyse the factors affecting the effectiveness of Kenya's AML framework and will provide possible solutions, based on experiences in other jurisdictions.

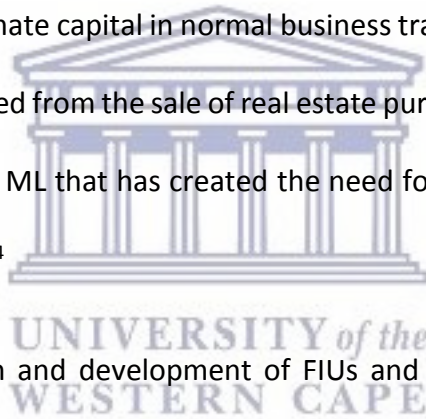


CHAPTER TWO

EVOLUTION AND DEVELOPMENT OF FINANCIAL INTELLIGENCE UNITS

2.1 Introduction

Money laundering (ML) involves knowingly disguising the source of funds obtained from criminal activities.¹ The ML cycle has three phases. The first phase is the placement, which entails the physical disposal of money and/or assets obtained from criminal activities. The second stage, which consists of layering the dirty proceeds, involves disguising the source or ownership of the illicit wealth. Successful layering may encompass investing in real estate or trading in stock markets.² The ultimate stage is integration, by which is meant that the illicit wealth is re-invested as legitimate capital in normal business transactions. An example would be investing the profits obtained from the sale of real estate purchased with the dirty money.³ It is this clandestine nature of ML that has created the need for specialised AML institutions in the criminal justice system.⁴



This chapter traces the origin and development of FIUs and other institutions created to combat ML. In addition, it outlines the evolution of the international AML legal framework. Finally, it highlights the role of other AML role-players such as regulators, supervisors, and professionals in the effort to combat ML both nationally and internationally.

2.2 History of Money Laundering and Financial Intelligence Units

FIUs are central national agencies responsible for receiving, analysing and transmitting to competent authorities information concerning proceeds of crime and the financing of

¹ Art 6 of the Palermo Convention (2000).

² Mugarura N (2012: 3).

³ Mugarura N (2012: 3).

⁴ Johnston D (2015).

terrorism; or information required by national legislation or regulation, in order to counter ML.⁵ Financial crimes, such as ML, erode the integrity of a country's financial system. This explains why FIUs have become important globally. FIUs complement the conventional law enforcement agencies through intelligence sharing.⁶ They achieve this task by collating information on ML activities and ensuring that reporting institutions adhere to rules such as the “know-your-customer” (KYC) and “customer due diligence” (CDD) rules.

The development of FIUs can be traced back to the early 1990s,⁷ although the crime of ML precedes this development.⁸ Formerly, ML was at the periphery of crimes such as drug trafficking, which was regarded a priority crime in most countries. Later, it became apparent in the USA, for example, that ML facilitated illicit dealing in narcotic drugs.⁹ In Australia, tax evasion played a significant role in promoting money laundering, while in Europe the spill over effect of drug trafficking into international trade and the threat of terrorism influenced the development of AML measures.¹⁰



In Kenya, a blend of the aforementioned factors has influenced the development of the AML laws.¹¹ Besides, the increasing demand for stringent anti-corruption measures, as well as the need to curb illicit financial flows, has had a direct impact on the AML measures of Kenya and most African states.¹² The diverse contexts that have influenced the development of AML measures partly explain the disparity in AML strategies, such as models of FIUs, among

⁵ IMF/World Bank (2004: 2).

⁶ German PM (2015: 49).

⁷ IMF/World Bank (2004: 9).

⁸ Chaikin D & Sharman JC (2009: 14).

⁹ Mugarura N (2012: 62).

¹⁰ Reuter P & Truman EM (2004: 79); Stessens G (2000: 194).

¹¹ Kegoro G (2004: 48).

¹² HLP Report (2015); Mugarura N (2012: 146).

countries.¹³ Nevertheless, rapid globalisation has increased the universality of ML threats, leading to the development of international standards to combat ML and to secure the integrity of financial systems and international trade.¹⁴

2.3 The International Anti-Money Laundering Instruments

2.3.1 The UN Convention against Illicit Traffic in Narcotic Drugs and Psychotropic Substances 1988 (Vienna Convention)

The 1988 Vienna Convention was the first international instrument regulating ML. Kenya acceded to the Convention on 19 October 1992.¹⁵ The Vienna Convention addresses ML stemming from drug trafficking without defining or mentioning expressly the crime of ML. In relation to drug trafficking, the Convention obligates states parties to criminalise “the acquisition, possession or use of property, knowing, at the time of receipt, that such property was derived from (ML) offences”.¹⁶ This provision strongly links the Convention to ML since AML laws have similar provisions, albeit with a widened scope to cover other predicate offences apart from those associated with drug trafficking. The Vienna Convention places at the fore international co-operation by broadening the obligation of states to include measures to eliminate bank secrecy laws that may impede mutual legal assistance.¹⁷ It also provides for the confiscation of criminal assets, thus making crime less profitable.¹⁸ Although the Convention lacks explicit AML provisions, such as provisions for the establishment of FIUs, it creates a platform for increased international co-operation in combating drug trafficking.

¹³ Mitsileges V (2003: 83).

¹⁴ These are evinced through the adoption of conventions such as the Palermo Convention and the Vienna Convention.

¹⁵ See https://treaties.un.org/Pages/ViewDetails.aspx?src=IND&mtdsg_no=VI-19&chapter=6&clang=en (accessed 20 August 2017).

¹⁶ Art. 3 of the Vienna Convention (1988).

¹⁷ Arts 3, 5 & 7 of the Vienna Convention (1988).

¹⁸ The preamble to the Vienna Convention (1988).

2.3.2 The United Nations Convention against Transnational Organized Crime and the Protocols thereto 2000 (Palermo Convention)

The adoption of the Palermo Convention was a significant achievement in international efforts to combat ML at the dawn of the 21st Century.¹⁹ Compared to the Vienna Convention, the Palermo Convention extended the scope of ML offences beyond drug trafficking and related offences. The offences set out in article 6 of the Palermo Convention remain the key focus of global AML initiatives. In essence, article 6 calls on all states parties to enact laws which criminalise the intentional:

“[C]onversion or transfer of property, knowing that such property is the proceeds of crime, for the purpose of concealing or disguising the illicit origin of the property or of helping any person who is involved in the commission of the predicate offence to evade the legal consequences of his or her action.”²⁰

This provision applies also to the acquisition of such criminal property and it includes an attempt to commit ML.

Drawing from article 6, three approaches inform the ML definitions contained in the laws of states parties,²¹ namely: the all crimes approach to ML as adopted in Kenya;²² a penalty threshold, in which ML results from predicate crimes that go beyond a set threshold,²³ for example, offences carrying a sentence of imprisonment of more than six months; and an approach which makes only certain crimes predicate crimes for ML.²⁴ This difference in approach affects the work of FIUs since, where a predicate crime in one state is not considered to be a predicate crime in another state, FIUs do not keep information about such

¹⁹ Kenya acceded to the treaty on 14 June 2004. See https://treaties.un.org/pages/ViewDetails.aspx?src=TREATY&mtdsq_no=XVIII-12&chapter=18&clang=en (accessed 20 August 2017).

²⁰ Art 6(1)(a) of the Palermo Convention.

²¹ Unger B (2007: 129).

²² Sec 2 of POCAMLA.

²³ Sec 35 of Malawi's Money Laundering, Proceeds of Serious Crime Terrorist Financing Act.

²⁴ Sec 3 of Tanzania's Anti-money Laundering Act, 2006.

crimes. Also, these variations constitute an impediment to requests for extradition or mutual legal assistance.

Furthermore, the Palermo Convention provides for the establishment of an FIU to serve as “a national centre for the collection, analysis and dissemination of information regarding potential ML”.²⁵ However, it does not clarify the structure of FIUs. The Convention also criminalises corruption and it implicitly endorses the FATF Recommendations by encouraging states to comply with internationally established standards in combating organised crime.²⁶

2.4 The International and Regional Anti-Money Laundering Institutions and Standards

2.4.1 The Financial Action Task Force (FATF) and its Recommendations

The FATF was established by the Group of Seven (G7) countries at their annual economic summit in Paris, France, in 1989.²⁷ The FATF headquarters are housed at the offices of the Organisation for Economic Co-operation and Development (OECD) where the FATF has a small secretariat. The FATF has grown to comprise a total of 37 members, amongst which are two regional organisations (the Gulf Co-operation Council and the European Commission).

At the time of formation, the primary goal of the FATF was to formulate international standards on combating ML.²⁸ Following the 11 September 2001 terrorist attacks in the US, members of the FATF met and resolved to include combating the financing of terrorism (CTF) within its mandate.²⁹ In 2008 the mandate of the FATF was extended to include combating the proliferation of arms.³⁰ The FATF contributes immensely to the global AML/CTF policy

²⁵ Art 7(1)(b) of the Palermo Convention (2000).

²⁶ Art 7(3) of the Palermo Convention (2000); Booth R *et al* (2011: 12).

²⁷ For details see <http://www.fatf-qafi.org/about/> (accessed 25 June 2017).

²⁸ Booth R *et al* (2010: 7).

²⁹ FATF Report (2001-2002).

³⁰ FATF (2008).

through its set of recommendations, first issued in 1990. Through periodic reviews, the FATF ensures that its recommendations keep abreast of ML/TF trends.³¹ The FATF's latest review was in 2012, during which it revised the Recommendations to include the Nine Special Recommendations in the 40 Recommendations.

Following the review, Recommendation 29 now provides for the establishment of FIUs as leading AML institutions. In the Interpretive Note to Recommendation 29, the FATF recommends that features of FIUs include operational independence, ability to carry out its operations without undue influence or interference and adherence to the *Egmont Group's Principles for Information Exchange between Financial Intelligence Units for Money Laundering Cases* (Egmont Principles).³² Apart from listing the key features of FIUs, the FATF does not recommend any particular model of FIU. Also, Recommendation 2 provides for national co-operation and co-ordination in combating ML/TF. This is the basis for the establishment of AML boards and committees such as AMLAB.

Although the FATF lacks the power to enforce fines and penalties, its Recommendations are authoritative nationally and internationally.³³ To ensure compliance with its Recommendations, the FATF reviews AML measures adopted in different jurisdictions.³⁴ From these reviews, the FATF lists the high-risk and non-cooperative jurisdictions. This process has prompted most countries to endeavour to comply with the FATF standards to avoid economic risks faced by high-risk and non-cooperative jurisdictions.³⁵ The threat of being listed as a

³¹ See <http://www.fatf-gafi.org/about/> (accessed 25 June 2017).

³² Adopted on 28 October 2013.

³³ See Para. 7 UN Security Council Resolution 1617 (2005); Booth *et al* (2011: 5).

³⁴ Reuter P & Truman EM (2004: 86).

³⁵ For example, Turkey in 1996.

high-risk jurisdiction jolted Kenya into reviewing its AML laws and establishing AML/CTF institutions.³⁶

2.4.2 The Egmont Group of Financial Intelligence Units

The Egmont Group of FIUs is a non-political, voluntary, international entity of FIUs committed to providing a forum for FIUs to improve co-operation in the effective exchange of information to combat ML and TF, and to foster the implementation of domestic programmes. It was established in 1995 at a meeting at Egmont-Arenberg Palace in Brussels, after which it is named. The objectives of the Egmont Group include: expanding and systematising the exchange of financial intelligence information; improving expertise and capabilities of personnel; fostering better communication among FIUs through technology; and helping to develop FIUs worldwide.³⁷

Membership of the Egmont Group is open to any country that establishes an FIU and undertakes to adhere to the *Egmont Group's Principles for Information Exchange between Financial Intelligence Units for Money Laundering Cases*.³⁸ These principles include confidentiality and restricting the use of the information (speciality principle). At the time of writing, the Egmont Group comprises 154 FIUs.³⁹ Kenya is presently gearing towards joining the group.

³⁶ ESAAMLG Report (2011).

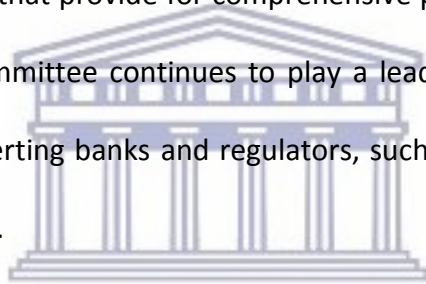
³⁷ See <https://www.egmontgroup.org/en/content/about> (accessed 25 June 2017).

³⁸ Mugarura N (2012: 93).

³⁹ See <https://www.egmontgroup.org/en/membership/list> (accessed 25 June 2017).

2.4.3 The Basel Committee on Banking Supervision

The Basel Committee on Banking Supervision sets global standards for the prudential regulation of banks and provides a forum for co-operation on banking supervisory matters.⁴⁰ It was established in 1974 by the central bank governors of the Group of Ten countries (G10). The Committee aims at strengthening the regulation, supervision and practices of banks worldwide to enhance financial stability. The Bank for International Settlements (BIS) in Basel, Switzerland, houses the Committee's secretariat. Key AML contributions emanating from the Basel Committee include the 1988 Statement of Principles, *Prevention of Criminal Use of the Banking System for the Purpose of Money Laundering*, and the 1997 *Core Principles for Effective Banking Supervision* that provide for comprehensive procedures for KYC principles, among others. The Basel Committee continues to play a leading role in research and the production of publications alerting banks and regulators, such as FIUs, to the ML risks that they continually have to avert.



2.4.4 The Wolfsberg Group

The Wolfsberg Group is an association of 13 global banks whose mandate includes developing AML/CTF standards for the financial industry and AML/CTF principles such as the KYC principles.⁴¹ The group was established in 2000 at the Chateau Wolfsberg in Switzerland, hence the appellation "Wolfsberg". The group has published a series of papers on AML/CTF for correspondent banking, such as the *Wolfsberg Statement on Monitoring Screening and Searching*,⁴² that help banks in applying KYC and CDD procedures. The Wolfsberg Statement and other policy measures are intended to apply worldwide and target particularly financial

⁴⁰ See <https://www.bis.org/bcbs/about.htm?m=3%7C14%7C573> (accessed 20 August 2017).

⁴¹ See <https://complyadvantage.com/knowledgebase/wolfsberg-group/> (accessed 20 August 2017).

⁴² Wolfsberg Statement (2009).

institutions and regulators. With the Group's commitment to addressing threats faced by financial institutions, its policy papers are meant to contribute to the work of FIUs in investigating ML.⁴³

2.5 Regional Initiatives and Regulations

2.5.1 The European Union Anti-Money Laundering Directives

The European Union's Anti-Money Laundering Directives (EU Directives) are an example of regional binding AML instruments. These Directives are binding on member states. The EU also continuously seeks to incorporate agreements to bind non-member states.⁴⁴ To ensure compliance, the European Commission institutes proceedings against non-compliant states at the European Court of Justice. In these proceedings, the Court may issue deterrent penalties against non-compliant states.

The EU Directives promote effective harmonisation of laws within its member states and also, they bring the EU AML/CTF measures in line with international standards such as the FATF recommendations.⁴⁵ In June 1991, the European Commission issued its *First EU Directive 91/308/EEC*. The EU reviewed its directives in 2001, 2005 and 2015, as a result of which it adopted the second, third and fourth directives respectively. By June this year, all countries were required to have complied with the Fourth Directive.⁴⁶

The scope of these directives has expanded to include reporting by legal professionals of suspicious transactions, the criminalisation of financing of terrorism, the creation of tax related crimes and the requirement to establish FIUs. Most importantly, the *Fourth EU*

⁴³ Pieth M (2007: 99).

⁴⁴ Mugarura N (2012: 74); Durrieu R (2013: 117).

⁴⁵ Durrieu R (2013: 166); Mugarura N (2012: 74).

⁴⁶ See <http://www.acams.org/aml-resources/eu-fourth-aml-directive/> (accessed 20 October 2017).

*Directive*⁴⁷ requires FIUs to be operationally independent and free from political or executive interference.⁴⁸ This Directive is the first hard law instrument that provides for the independence of FIUs. Even though Kenya and other African countries are not bound by these Directives, they constitute international best practices that need to be adopted or emulated widely. However, even though the directives are comprehensive and binding, they are not implemented effectively within all EU member states.⁴⁹

2.5.2 The Eastern and Southern Africa Anti-Money Laundering Group (ESAAMLG)

ESAAMLG was formed in 1999 as a FATF-Style Regional Body (FSRB). As such, its establishment was informed partly by the realisation that different regions are exposed to unique ML threats which might not be adequately addressed through joint global action.⁵⁰ ESAAMLG consists of 18 members, all being Eastern and Southern African countries.⁵¹ Members of ESAAMLG belong to the British Commonwealth and have committed themselves to implementing the FATF Recommendations.



ESAAMLG's main purpose is to combat ML by implementing the FATF Recommendations among member states. In addition, ESAAMLG studies regional ML/TF typologies and coordinates regional and international AML/CTF initiatives. As with the FATF, ESAAMLG enforces the FATF Recommendations by way of conducting peer reviews among member states. It bears noting that Kenya is among the countries that have already benefited from a

⁴⁷ Fourth EU Directive on Money Laundering (EU) 2015/849.

⁴⁸ Art 32(3) of the Fourth EU Directive on Money Laundering.

⁴⁹ International Bar Association "Europe" available at <https://www.anti-moneylaundering.org/Europe.aspx> (accessed 30 October 2017).

⁵⁰ Mitsileges V (2003:84); On the need for regional co-operation, see arts 7(3) & (4) and 27 – 30 of the Palermo Convention (2000) and FATF Recommendations 36-40.

⁵¹ See <http://www.fatf-qafi.org/pages/easternandsouthernafrikaanti-moneylaunderinggroupesaamlg.html> (accessed 26 June 2017).

review by ESAAMLG.⁵² In its report, ESAAMLG recommended that Kenya should speed up its effort to establish an FIU.⁵³

2.5.3 The East African Community Anti-Money Laundering Framework

Kenya is a member of the East African Community, which aims, *inter alia*, at establishing a common market and a monetary union. In the course of establishing a common market, the region has become more vulnerable to ML,⁵⁴ which threatens the sustainability of the common market and the full realisation of a monetary union.⁵⁵ To contain the threat posed by ML, the East African Council of Ministers adopted *the East African Community Directive on Anti-Money Laundering in the Securities Market*.⁵⁶ This Directive calls for increased co-operation among member states in combating ML and for the establishment of an effective AML framework. This Directive is binding on member states and therefore requires full implementation.⁵⁷ Unlike the European Union Directives on ML,⁵⁸ the East African Community Directive is not a comprehensive prescription for combating ML and it lacks an effective enforcement framework.⁵⁹ As the name suggests, its focus is on ML in the area of securities exchange, therefore it does not provide for the establishment of FIUs. As implementation is ongoing, gauging from previous engagements, lack of political will on the part of some of the countries often hinder the implementation of such directives across the board.⁶⁰

⁵² ESAAMLG Report (2011).

⁵³ ESAAMLG Report (2011: 47).

⁵⁴ Shetret L *et al* (2015: 31).

⁵⁵ The World Bank/East African Community Secretariat (2016).

⁵⁶ EAC Directive 2014/14/EAC.

⁵⁷ Art 16 of the Treaty for the Establishment of the East African Community (2000).

⁵⁸ Mugarura N (2012: 71).

⁵⁹ Arts 3 & 4 the East African Community Directive on Anti-Money Laundering in the Securities Market.

⁶⁰ Mathieson C (2016).

2.6 Money Laundering and Related Crimes

2.6.1 Money Laundering and Terrorism Financing

Unlike ML, terrorism financing entails the misuse of clean or dirty money for terrorist purposes.⁶¹ Primarily, terrorists do not commit crimes for financial gain but in pursuit of political or ideological aims. Also, in some cases, the funds used to finance terrorism have a lawful provenance. In 1999, the UN General Assembly adopted the *United Nation Convention on the Suppression of the Financing of Terrorism* to regulate terrorism financing and related offences.⁶² At the time of adoption, counter-terrorism financing (CTF) was not part of the global AML measures.⁶³

The shock of the 9/11 terrorist attacks in the US prompted the UN Security Council to endorse the role of the FATF by mandating it to formulate Special Recommendations to counter terrorism financing.⁶⁴ These developments increased the convergence between AML and CTF measures. A common but key thread running through both regulatory mechanisms is the sharing of intelligence by FIUs. In spite of the differences between ML and TF, today CTF is within the scope of national and international AML strategies. As a result, FIUs have a role also to analyse information relating to TF and the financing of the proliferation of weapons of mass destruction. The idea is to cut off the “lifeblood of terrorism”.⁶⁵

2.6.2 Money Laundering and Corruption

The 2003 United Nations Convention against Corruption (UNCAC) is the main international instrument for combating corruption. Transparency International defines corruption as “the

⁶¹ Booth et al (2012: 13).

⁶² See the Preamble of the UN Convention on the Suppression of the Financing of Terrorism.

⁶³ Booth R et al (2012: 13).

⁶⁴ FATF Report (2001-2002).

⁶⁵ Booth R et al (2012: 13).

misuse of entrusted power for private gain”.⁶⁶ Viewed through the lens of grand corruption,⁶⁷ ML methods can be used to disguise the source of dirty money deriving from corruption and to inject it into a country’s financial system. Furthermore, the complexity of grand corruption dossiers requires intelligence sharing in tracing and confiscating the proceeds of crime. These explain why UNCAC calls upon States Parties to consider establishing FIUs.⁶⁸ However, like the Palermo Convention, it does not provide for features of FIUs.

Despite the direct link between corruption and ML, most states, including Kenya, tackle these two crimes by using distinct anti-corruption units and FIUs, respectively. Without proper coordination, such distinct approaches hinder an effective response to corruption and ML in areas where the crimes converge or overlap, such as confiscation and asset recovery.⁶⁹ Chaikin and Sharman have called for a fusion of the anti-corruption and AML measures, arguing that this will avoid duplication of mandate and ensure optimum utilisation of resources.⁷⁰ Adding to the fact that corruption is a predicate offence of ML, a fused approach is plausible in areas of convergence to the extent that it guarantees the effectiveness of anti-corruption and AML measures. Botswana is among the few countries that have adopted this model.⁷¹ To avoid an overlap of mandate between the Ethics and Anti-Corruption Commission

⁶⁶ Chaikin D & Sharman JC (2009: 8); For a detailed definition of corruption see Arts 15-22 of UNCAC.

⁶⁷ Grand corruption occurs when a public official or other person deprives a particular social group or substantial part of the population of a state of a fundamental right. Mostly it is perpetuated by senior public officials. Petty corruption is the everyday abuse of entrusted power by public officials in their interactions with ordinary citizens, who often are trying to access basic goods or services in places like hospitals, schools, police departments and other agencies. Transparency International (2016).

⁶⁸ Arts 14(1)(b) and 58 of UNCAC.

⁶⁹ UNCAC provisions on ML include art 14 on measures to prevent ML, art 23 on laundering proceeds of crime, art 52 on prevention and detection of transfers on proceeds of crimes, and Art 58 which, among others, calls for the establishment of FIUs.

⁷⁰ Chaikin D & Sharman JC (2009: 29).

⁷¹ See Botswana’s Directorate on Corruption and Economic Crime, available at <http://www.gov.bw/en/Ministries--Authorities/Ministries/State-President/Department-of-Corruption-and-Economic-Crime-DCEC/Money-Laundering/> (accessed 20 August 2017).

and the FRC, Kenya has an autonomous Asset Recovery Agency solely tasked with asset recovery functions.⁷²

2.7 Models of Financial Intelligence Units

The Egmont Group identifies four models of FIUs, namely, the judicial or prosecutorial model; the law enforcement model; the administrative model; and the hybrid or mixed financial intelligence unit model.⁷³

2.7.1 The Law Enforcement Model

This FIU model implements AML measures alongside other law enforcement agencies. In this model, the FIU supports existing law enforcement mechanisms and the judiciary by acting concurrently or, at times, with competing jurisdiction to combat ML. This type of FIU is located in already existing structures such as the criminal investigation departments and does not have to be set up from scratch. The advantages of this model are: first, it is set up in already existing structures, which means it is cost-effective; second, this model maximises the use of information disclosed to it, often extending its reach to economic crimes beyond ML; third, it can easily expedite action, such as making warrantless arrests and taking other extra-judicial steps to intercept ML; and finally, this model has the advantage of enabling an FIU to enjoy ready access to information by virtue of its national and international connections, for example, with Interpol and Europol.⁷⁴

The main shortcomings of this model include: first, reporting institutions may be reluctant to disclose information, knowing that it can be misused for purposes other than the combating

⁷² Sec 54 of POCAMLA.

⁷³ See <https://www.egmontgroup.org/en/content/financial-intelligence-units-fius> (accessed 04 August 2017); IMF/World Bank (2004: 9).

⁷⁴ Stessens G (2000: 186).

of ML; second, this model tends to focus on investigation as opposed to prevention; third, since law enforcement agencies are not always interlocutors for financial institutions, their efficacy is based partly on the establishment of mutual trust.⁷⁵ Still, in most cases, the imminent risk of criminal proceedings because of failure to report ensures compliance by reporting institutions. Finally, in most cases, FIUs lack channels through which they can lobby for policy and legislative review.⁷⁶ Examples of jurisdictions with this model are Canada, Germany and Japan.⁷⁷

2.7.2 The Judicial or Prosecutorial Model

The judicial or prosecutorial model is established within the judiciary and in most cases under an independent prosecutor. This model is found mostly in European countries in which the prosecutor enjoys wide discretionary powers.⁷⁸ It is suitable for jurisdictions with stringent bank secrecy laws, where judicial intervention to access documents is frequently necessary. This model has the following advantages. First, it enables an expeditious response to suspicious transactions reported by investigating units since the FIU has quick access to the courts in matters requiring the freezing of assets and the granting of judicial assistance to execute search warrants. Second, this model is insulated well against political interference.⁷⁹ Its drawbacks are similar to those facing the law enforcement type of FIUs sketched above. Examples of jurisdictions with this model are Luxembourg and Portugal.⁸⁰

⁷⁵ Stessens G (2000: 186).

⁷⁶ Strauss K (2010: 14).

⁷⁷ IMF/World Bank (2004: 15).

⁷⁸ IMF/World Bank (2004: 16); Stessens G (2000: 187).

⁷⁹ IMF/World Bank (2004: 17).

⁸⁰ IMF/World Bank (2004: 18).

2.7.3 The Administrative Model

This model of FIUs acts as an intermediary between reporting institutions and the law enforcement agencies or the judiciary. Therefore, these FIUs nurture a good relationship with financial institutions and other reporting institutions since they forward only information that raises significant suspicion to law enforcement agencies.⁸¹ This practice helps safeguard confidentiality and restricts the use of information, hence fostering a close-knit relationship with reporting institutions.⁸² FIUs adhering to this model are centralised and staffed by personnel capable of analysing information received from reporting institutions. They can operate alone under the supervision of the ministry of finance or completely independent, as is the case in Belgium.⁸³

Administrative FIUs have the following advantages. First, they create a “buffer” between reporting institutions and law enforcement agencies. This helps avoid direct institutional links between law enforcement agencies and financial institutions by limiting information shared to suspicious transactions that warrant further investigation. Second, this model inspires confidence among reporting institutions since there is a guarantee that the information forwarded will be used only for combating ML, TF and related crime. Third, because of the high level of trust existing among these FIUs, there is increased information sharing with similar FIUs in other jurisdictions.

The drawbacks of this model are the following. First, the FIU is not part of the judicial or law enforcement units, which means that there might be delays in obtaining judicial remedies, such as freezing orders in case of suspicious transactions or where a suspect needs to be

⁸¹ IMF/World Bank (2004: 10).

⁸² Al-Rashdan M (2012: 490); Stessens G (2000: 189).

⁸³ Stessens G (2000: 189).

arrested forthwith. Coupled to this shortcoming is the fact that this type of FIU lacks the wide range of investigative powers as compared to law enforcement units. Second, depending on its location and source of funds, this model suffers from lack of autonomy since at times it works under the supervision of the executive. This lack of independence makes it vulnerable to political manipulation.⁸⁴ Examples of countries with this model are Belgium, the Netherlands, France, the US and Kenya.

2.7.4 Hybrid FIUs

The hybrid model is a mix of the traits of at least two of the aforementioned models. It combines the benefits accruing from each model while scaling down disadvantages associated with a particular model. Such FIUs are found in Denmark and Norway.⁸⁵

The foregoing models of FIUs do not necessarily inhibit the operation of an FIU. They represent the various ways in which FIUs work. Any FIU model is acceptable to the Egmont Group, provided it meets and adheres to the prescribed Egmont Principles. In some jurisdictions, apart from the primary duty of receiving and analysing information, FIUs prescribe regulations that are binding on reporting institutions and other regulated institutions.⁸⁶

2.7.5 Reasons for the Establishment of Centralised FIUs

With the description above as background, five reasons explain why there has been a need to have FIUs as centralised institutions in combating ML and TF. First, centralising operations of the FIUs brings together experts from diverse fields to trace laundered proceeds in the often

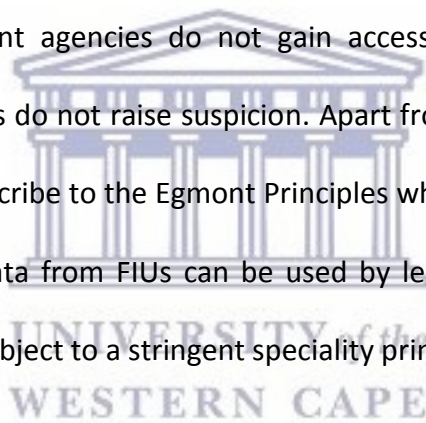
⁸⁴ Strauss K (2010: 20); Stessens G (2000: 189).

⁸⁵ IMF/World Bank (2004: 17).

⁸⁶ Broek M (2014: 163). Examples include Bulgaria and Spain; also Kenya courtesy of sec 36A (1) & (2) of POCAMLA (2009).

complex layering process. Second, unlike a decentralised system based in various state departments, a centralised unit ensures quick access to the requisite information and the initiation of investigations where necessary.⁸⁷

Third, centralisation helps in ensuring optimum and efficient utilisation of resources. FIUs screen the reports submitted and submit to the investigative authorities only the cases warranting investigation. Therefore, centralisation helps to ensure that the investigative authorities handle only cases that pose a real threat, as opposed to following up all cases referred to them by reporting institutions. Fourth, FIUs, especially those with administrative features, create a buffer between reporting institutions and law enforcement agencies. This ensures that law enforcement agencies do not gain access to financial information of customers whose transactions do not raise suspicion. Apart from administrative FIUs, other FIU models undertake to subscribe to the Egmont Principles when joining the Group. Finally, in some cases, centralised data from FIUs can be used by legislators in formulating fiscal policies where they are not subject to a stringent speciality principle.⁸⁸



2.8 Other Anti-Money Laundering institutions

2.8.1 The Anti-money Laundering Boards or Committees

Money laundering boards or committees are interdepartmental agencies formed to co-ordinate and formulate national AML policies.⁸⁹ Their existence can be traced from FATF Recommendation 2 that calls for national co-operation and co-ordination in combating organised crime. These institutions are required to be all inclusive in the way they work. The

⁸⁷ Stessens G (2000: 195).

⁸⁸ For example in Australia, increased revenue from tax collection is a goal of the AML measures. Stessens (2000: 194).

⁸⁹ Booth R *et al* (2012: 24).

rationale is that this kind of board has to be all-encompassing, for it congregates the work of reporting institutions, law enforcement agencies, central/reserve banks, regulatory agencies, FIUs, professions and high-risk businesses.⁹⁰ This assembly of different institutions enables the board to formulate a comprehensive and effective AML policy. Also, with all participants on board, it is easy to co-ordinate AML measures. Effective co-ordination avoids overlapping mandates, thereby ensuring optimal utilisation of resources and effectiveness of the AML measures.⁹¹ The United Kingdom's Money Advisory Laundering Committee⁹² and Kenya's AMLAB are examples of such multi-agency institutions.

2.8.2 Regulators and Supervisors

Regulators and supervisors have an important role in setting standards and ensuring compliance among various reporting institutions. Therefore, unlike the police and other law enforcement agencies, regulators understand the intricacies of their respective fields.⁹³ Given the significance of the role played by regulators, FATF Recommendation 26 mandates regulators and supervisors of financial institutions to include AML measures within the ambit of their supervisory roles. Further, in the interpretive notes to Recommendation 26, the FATF emphasises the need for a risk-based approach. The implementation of a risk-based approach to customer due diligence procedures enhances vigilance, given that regulators and supervisors are required to help the legislature to develop laws that regulate high-risk areas in the economy and financial sector.⁹⁴ Kenya has supervisory bodies such as the Central Bank

⁹⁰ Chatain PL *et al* (2009: 9).

⁹¹ Strauss K (2010: 28).

⁹² Booth R *et al* (2012: 25).

⁹³ Booth R *et al* (2012: 28); Stessens G (2000: 200).

⁹⁴ FATF Recommendation 1; Reuter P & Truman EM (2004: 79).

and the Capital Markets Authority, both of which play a role in implementing the country's AML measures.

2.9 Conclusion

This chapter has highlighted the global and national legal and institutional structure of combating ML, terrorism financing and corruption. Furthermore, it highlighted the fact that regulatory structures are not coherent globally. However, there are salient crosscutting standards in most institutions. Most importantly, is the fact that the FIUs and anti-money laundering boards are globally recognised as key AML institutions. The next chapter looks at the extent to which the Kenyan POCAMLA provides for the establishment of the FRC and AMLAB and their respective mandates and functions.



CHAPTER THREE

THE STRUCTURE AND FUNCTIONS OF KENYA'S ANTI-MONEY LAUNDERING INSTITUTIONS

3.1 Introduction

In response to the global call to establish FIUs, Kenya established the Financial Reporting Centre (FRC) in 2012. The primary goal of setting up the FRC is to secure the integrity and stability of Kenya's financial system and to forestall economic criminal activity. The FRC, among other AML institutions, instils confidence that Kenya has in place adequate measures to combat ML/TF. Moreover, the FATF has removed Kenya from the list of high-risk jurisdictions.¹ However, compliance with international standards does not guarantee the effectiveness of an AML/CTF system.² This chapter takes stock of both the FRC and AMLAB by examining their structure, composition, powers and functions against the background of the FATF Recommendations and international best practices.

3.2 The Financial Reporting Centre (FRC)

Part III of POCAMLA establishes the FRC as a body corporate, with perpetual succession and a common seal.³ As a juristic person, the FRC can institute legal proceedings, own property and enter into contracts, among other functions, in furtherance of its objectives.⁴

The principal objective of the FRC is to assist in the identification of the proceeds of crime and the combating of ML and TF.⁵ Other objectives of the FRC include: availing information to investigative authorities; supervising bodies and other law enforcement units; exchanging

¹ See <http://www.fatf-gafi.org/publications/high-riskandnon-cooperativejurisdictions/documents/public-statement-february-2017.html> (accessed 30 September 2017).

² Mugarura (2012: 249); Strauss K (2010).

³ Sec 21 of POCAMLA.

⁴ Sec 21 of POCAMLA.

⁵ Sec 23 of POCAMLA.

information with analogous bodies in other countries regarding ML activities and related offences; and ensuring compliance with international standards and best practices in the implementation of AML measures.⁶ These objectives are in line with the core functions of FIUs that include receiving, analysing and disseminating information to competent authorities.

3.2.1 Independence and Autonomy of the Financial Reporting Centre

FIUs handle financial information which is always sensitive and is protected by strict privacy rules.⁷ To be able to do this, the FATF recommends that FIUs need to function independently.⁸ Unlike the FATF Recommendations that are non-binding, the Fourth European Union Directive on Money Laundering requires FIUs to be operationally independent and free from political or executive interference.⁹ The European Union position ought to be followed by states in Africa which still rely on the FATF recommendations that are non-binding. Also, if the Egmont Group is to function properly, its member FIUs should operate independently. Currently, independence of FIUs is not a precondition for joining the Egmont Group.¹⁰ By working autonomously, FIUs are cushioned against external influence, which prevents them from being used for unsanctioned purposes, such as espionage.¹¹

Like many FIUs,¹² the FRC operates under the auspices of the Cabinet Secretary in charge of finance (Cabinet Secretary).¹³ This arrangement comes with its limitations since cabinet secretaries are usually politically exposed persons (PEPs) who can easily be parties to ML

⁶ Sec 23 of POCAMLA.

⁷ Schott PA (2006: VI-20).

⁸ Para 8 Interpretive note to FATF Recommendation 29; IMF/World Bank (2004: 25).

⁹ Art 32(3) of the 4th EU Directive on Money Laundering.

¹⁰ Egmont Group of Financial Intelligence Units Charter (2013) 30.

¹¹ Strauss K (2010: 22).

¹² For example, the South African FIU FIC, the USA FIU, FinCEN. On statistics on the placement of FIUs, see Egmont Group and World Bank Project (2007).

¹³ Secs 31(1),40(C) & 42(3) of POCAMLA.

syndicates.¹⁴ At the moment, the FRC is physically housed in the Central Bank of Kenya. Chaikin and Sharman consider this location to be more advantageous to the FIUs, mostly in low-capacity countries, as central banks are some of the best functioning institutions in such countries.¹⁵ Other indicators that determine the independence of the FIUs include the manner of appointing officials, their tenure and terms of service, the sources of funds, and most importantly, the effectiveness of their oversight role.

a) Appointment of the Director-General and the Deputy Director-General

POCAMLA establishes the office of the Director-General and the Deputy Director-General whose functions are to ensure that the FRC fulfils its objectives.¹⁶ These are the only positions specifically established by POCAMLA, which explains partly why inadequate staffing is one of the challenges confronting the FRC. In the absence of political will to combat ML, the government can resort to employing only the two officers since doing so meets the basic requirements of POCAMLA.¹⁷ In South Africa, even though FICA establishes the position of Director-General only, the government has been supportive in ensuring proper staffing of the FICA office.¹⁸ The Kenyan government should also follow suit to ensure adequate staff in the FRC.

b) Qualification and Appointment Process

A person eligible for appointment as a Director-General or Deputy Director-General should be a fit, competent and proper person.¹⁹ He or she should hold a degree in law, public administration, management, international relations, economics or finance from a recognised

¹⁴ FATF Recommendation, the definition of PEPs; Parkman T (2012: 105).

¹⁵ Chaikin D & Sharman J C (2009: 68).

¹⁶ Sec 25 of POCAMLA.

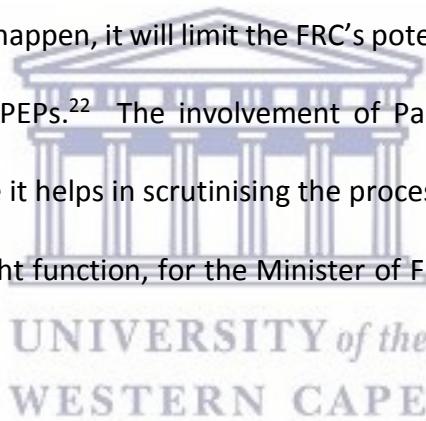
¹⁷ Strauss K (2010: 15).

¹⁸ Sec 6 of FICA.

¹⁹ Sec 25 of POCAMLA.

university and should have ten years work experience in the relevant field. AMLAB may set other eligibility criteria for such persons. AMLAB selects and forwards names of persons who meet the above-mentioned requirements to Parliament for approval. Thereafter, the Cabinet Secretary appoints the successful candidates. This process is structured to minimise partiality and guarantee the independence of the Director-General and Deputy Director-General. Since AMLAB selects the candidates, Parliament approves and the Cabinet Secretary appoints successful candidates.

Nevertheless, as Kenya wrestles with implementing its Constitutional provisions on integrity,²⁰ there is a risk of setting a low threshold for determining a “fit, competent and proper” person.²¹ Should this happen, it will limit the FRC’s potential to adopt stern measures against corrupt officials and PEPs.²² The involvement of Parliament in the appointment process is commendable since it helps in scrutinising the process. In South Africa, Parliament does not exercise this oversight function, for the Minister of Finance has more discretion in the appointment process.²³



²⁰ Ch Six of the Constitution of Kenya of 2010.

²¹ For example, in *Mumo Matemu v Trusted Society of Human Rights Alliance & 5 Others* [2013] eKLR, the Court of Appeal found the appellant (Mumo Matemu) to be fit to hold office as the chairperson of the Ethics and Anti-Corruption Commission. This was so, despite the fact that the appellant was under criminal investigations emanating from fraudulent conduct in positions he had previously held. Contrast this scenario with the South African case of *Democratic Alliance v President of South Africa and Others* 2013 (1) SA 248, where the Constitutional Court held that Mr Simelane, who had been appointed as the National Director of Public Prosecutions (NDPP) was not ‘fit and proper’ as required under the South African Constitution. This finding was based on the fact that the Minister of Justice had ignored a report by the Public Service Commission which showed that Mr Simelane had acted dishonestly previously.

²² Also, Parliament has previously settled for low standards. For example, in appointing commissioners to steer the Ethics and Anti-Corruption Commission, Parliament approved names of commissioners despite the recommendation by Parliament’s Interviewing Committee that the names be rejected on the grounds that the persons “lacked the passion, initiative and the drive to lead the fight against corruption”. See *Mumo Matemu v Trusted Society of Human Rights Alliance & 5 Others* [2013] eKLR, para. 4.

²³ Sec 6 of FICA.

c) Tenure of Office and Removal from Office

The Director-General and the Deputy Director-General hold office for a renewable term of four years and three years respectively.²⁴ The renewal is limited to two terms. This guarantees continuity of the institution since their terms do not end at the same time. The Cabinet Secretary, in consultation with AMLAB, may remove the Director-General or Deputy Director-General from office on the grounds of gross misconduct, mental or physical incapacity or failure to satisfy the employment terms and conditions set by AMLAB.²⁵ Other grounds for removal include: (a) proof of a financial conflict of interest with any reporting institution; (b) bankruptcy; and (c) conviction for a crime with a sentence carrying imprisonment for a term exceeding six months. Pending determination of these grounds, the Cabinet Secretary, in consultation with AMLAB, may suspend the Director-General or the Deputy Director-General.²⁶

A decision to suspend the Director-General and the Deputy Director-General must be based on a joint consultation process. This ensures that they do not hold office at the whim of the Cabinet Secretary or AMLAB. Judicial recourse is also available in securing the right to a fair administrative action.²⁷ A stronger protection for the Director-General and the Deputy Director-General will be attained upon clarifying the meaning of “financial conflict of interest with any reporting institution” as a ground for removal.²⁸ Does this exclude a bank-customer relationship? Or does being a shareholder in a reporting institution translate into a financial conflict of interest? Also, gross misconduct can be a point for judicial determination on a case-

²⁴ Sec 25(5)(a) of POCAMLA.

²⁵ Sec 27 of POCAMLA.

²⁶ Sec 27(2) of POCAMLA.

²⁷ Art 47 Constitution of Kenya 2010.

²⁸ Sec 27(1)(a) of POCAMLA.

by-case basis.²⁹ Finally, failure to meet performance targets set by AMLAB is a double-edged sword. High and unrealistic standards set by AMLAB can trigger removal from office, while low standards will keep incompetent officials in office. Here, principles such as reasonableness should be the starting point. Despite the potential loopholes, POCAMLA provides for a sufficient degree of security of tenure.

d) Functions of the Director-General

The Director-General is the chief executive officer of the FRC.³⁰ His main function is to form and develop an efficient and performance-driven administration.³¹ The 2017 amendments to POCAMLA expanded the functions of the Director-General to include control of staff, maintenance of discipline and making all decisions of the FRC in the exercise of its mandate. In exercising this mandate, the Director-General is bound to abide by a policy framework formulated by the Cabinet Secretary in consultation with AMLAB.³² The Deputy Director-General complements the Director-General and acts on his behalf when the Director-General is absent.³³ This ensures that the FRC has the capacity to execute its mandate always. In South Africa, in the absence of the Director-General, the Minister appoints a member of staff to act in the Director-General's position.³⁴

e) Appointment of Staff

The FRC has the power to appoint its own officers to assist in realising its goals. The terms of service of staff appointed are formulated by the FRC and approved by the Cabinet Secretary.³⁵

²⁹ On the judicial interpretation of gross misconduct in Kenya see *Nicholas Otinyu Muruka v Equity Bank Limited* [2013] eKLR.

³⁰ Sec 28(1) of POCAMLA.

³¹ Sec 28(2)(a) of POCAMLA.

³² Sec 28(3) of POCAMLA.

³³ Sec 30 of POCAMLA.

³⁴ Sec 8 of FICA.

³⁵ Sec 31 of POCAMLA.

Besides, in the performance of its duties the FRC may engage other state departments or enter into a contract for services with any person with requisite expertise.³⁶ These provisions give the FRC some degree of autonomy in determining the composition of its own structure and staff.³⁷ However, the effectiveness of these provisions depends on the terms of service and remuneration stipulated by the Cabinet Secretary.

Good terms of service and adequate remuneration attract experts and allows adequate staffing by reducing competition from the private sector, thus helping the FRC in discharging its mandate effectively.³⁸ Also, the FRC can contract experts where necessary.³⁹ Currently, inadequate staff bedevils the FRC.⁴⁰ Therefore, there is a need to augment the funds allocated to the FRC to allow it to recruit more competent personnel. In an attempt to ensure adequate staffing, the FRC advertised a number of vacancies recently.⁴¹

f) Sources of Funds

Adequate funding is crucial in enabling FIUs to discharge their mandates properly. Insufficient funding may cripple the operations of FIUs and limit their effectiveness.⁴² The Kenyan FRC obtains its funding from the budgetary allocation by Parliament, government grants, donations, and fines and penalties received from non-compliant reporting institutions and other permissible sources.⁴³ Donations to the FRC are subject to the approval of the Cabinet Secretary. Subjecting donations to approval ensures proper oversight, as long as such oversight is not abused to frustrate legitimate donations. The degree of success in raising

³⁶ Sec 31 of POCAMLA Amendment Act 2017.

³⁷ Chaikin D & Sharman J C (2009: 67); Simwayi M & Haseed M (2011: 130).

³⁸ Chaikin D & Sharman J C (2009: 67).

³⁹ Sec 31(3) of POCAMLA.

⁴⁰ US Department of State Report (2017:117).

⁴¹ See <http://frc.go.ke/others/2016-07-07-20-12-50.html> (accessed 30 September 2017).

⁴² Strauss K (2010: 15).

⁴³ Sec 40 & 24B(3)(a) of POCAMLA.

funds through fines and penalties depends on the FRC's success in monitoring and detecting non-compliant institutions or persons. Thus, Parliamentary allocations remain the main source of funds. But, as mentioned above, under-funding continues to be an impediment to the FRC.⁴⁴ It is advantageous to be funded mainly through parliamentary allocations since it gives the FRC more room to function independently.⁴⁵

Generally, other options available for funding FIUs include raising the budget through imposing levies on reporting institutions. In Belgium, for example, the FIU budget is funded by reporting institutions.⁴⁶ Even though this is burdensome to reporting institutions, it guarantees the Belgian FIU a higher degree of independence, which is key to realising its mandate. The South African FIC is funded similarly to the Kenyan FRC.⁴⁷

g) Oversight of the Financial Reporting Centre

The need for independence and autonomy among FIUs does not negate the need to subject them to oversight.⁴⁸ In practice, there is a need to strike a balance between granting independence and autonomy, on the one hand, and ensuring proper oversight of the FRC, on the other.⁴⁹ Proper accountability mechanisms are vital for ensuring the effectiveness of the FRC. The Cabinet Secretary and AMLAB are the key oversight institutions that determine the effectiveness of the FRC. Their oversight powers straddle the gamut of the FRC activities. These include appointment and removal of the Director-General and the Deputy Director-General, their terms of service, the setting of performance targets and the budgeting process.

⁴⁴ US Department of State Report (2017:117).

⁴⁵ World Bank/Egmont group (2010).

⁴⁶ Stessens G (2003: 190).

⁴⁷ Sec 14 of FICA.

⁴⁸ OECD (2008: 27).

⁴⁹ Strauss K (2010: 22).

In cases where the Cabinet Secretary acts in consultation with AMLAB, there are proper safeguards since failure to consult constitutes a ground for impugning the legality of a particular process.⁵⁰ Examples include approving the terms of service for the staff of the FRC and approving the FRC's budget estimates forwarded by AMLAB. These are crucial areas in respect of which the Cabinet Secretary wields significant control over the functioning of the FRC. Therefore, in areas such as budgeting, submitting the budget directly to Parliament for approval would guarantee the independence of the FRC as opposed to having it first approved by the Cabinet Secretary.⁵¹ Also, the terms of service for the FRC's staff ought to be determined by the independent Salaries and Remuneration Commission.⁵² Besides, the Controller and Auditor-General conduct annual audits of the FRC's accounts.⁵³ In cases where the FRC violates an individual right, judicial remedies are available.⁵⁴

3.3 Functions of the Financial Reporting Centre

3.3.1 Receipt of Information

The FATF Recommendations require an FIU to receive suspicious transaction reports (STRs), cash transaction reports, wire transfers reports and other threshold-based declarations for analysis.⁵⁵ To conform to this obligation, the FRC receives STRs from reporting institutions and information relating to the conveyance of monetary instruments to and from Kenya.⁵⁶ In Kenya, reporting institutions consist of financial institutions and designated non-financial businesses or professions (DNFBPs). The financial institutions include banks, forex bureaux,

⁵⁰ see *Henry Nyabuto Ondieko v Charles Apudo Owelle & 2 others* [2017] eKLR.

⁵¹ OECD (2008: 26).

⁵² Art 230 of the Constitution of Kenya 2010.

⁵³ Sec 43 of POCAMLA.

⁵⁴ Art 23 of Constitution of Kenya 2010.

⁵⁵ FATF, Interpretive note to Recommendation 29.

⁵⁶ Sec 24(a) of POCAMLA

and insurance agencies. The DNFBPs include casinos, real estate agencies, dealers in precious metals and stones, accountants and non-governmental organisations.⁵⁷ Currently, the scope of DNFBPs has been expanded to include motor vehicle dealerships and real estate agents.⁵⁸

A glaring omission among the DNFBPs are members of the legal profession as well as trust and company service providers.⁵⁹ As a result of this omission, these professions and businesses do not have reporting obligations. This omission contravenes FATF Recommendation 23 which requires DNFBPs to file STRs. Lawyers wield expertise and, in most cases, they make complex legal arrangements that allow money launderers to escape the long arm of the law. Such stratagems include forming corporate vehicles, such as companies and trusts, as well as acting as fiduciaries to their clients. Also, the FRC has not published a list of PEPs to enable the reporting institutions to pay more attention to transactions involving PEPs.

Reporting institutions have a continuous mandate to monitor and report to the FRC all transactions that are complex, unusual, suspicious, and large⁶⁰ and those suspected to be related to funding terrorist activities.⁶¹ According to the FRC guidelines, suspicious transactions occur when one “suspects or have reasonable grounds to suspect” that the funds involved are from crime or that they are related to TF.⁶² In England and Scotland, "suspicion" means "imagining something without evidence or slender evidence," while in the USA, it refers to “slight or no evidence without definitive proof”.⁶³ By comparison, the Kenyan FRC’s approach is broad to allow filing a wide range of STRs. Moreover, the FRC has expanded the

⁵⁷ Sec 2 of POCAMLA.

⁵⁸ See <http://frc.go.ke/registration/reporting-institutions.html> (accessed 30 September 2017).

⁵⁹ Sec 18 of POCAMLA; ESAAMLG Report (2011) para. 46.

⁶⁰ Sec 44(1) of POCAMLA.

⁶¹ Sec 24 of POCAMLA.

⁶² FRC Guidelines (2017: 14).

⁶³ IMF/World Bank (2004: 43).

scope of the definition of “transaction” to include opening an account, as well as conducting any activity in a particular account, and a proposed or attempted transaction.⁶⁴

For cash transaction reporting, reporting institutions must report all cash transactions exceeding US\$ 10,000.⁶⁵ The FRC has in place online software that enables speedy transmission of cash transaction reports.⁶⁶ To become more effective and efficient, the FRC should adopt a risk-based approach in implementing its due diligence procedures. An effective risk-based approach will help the FRC to improve the quality of STRs it receives from reporting institutions. Following the 2017 amendments of FICA, South Africa has adopted an extensive risk-based approach with respect to all aspects of ML.⁶⁷

To facilitate reporting effectively, POCAMLA provides immunity to persons who report suspicious transactions in good faith.⁶⁸ This immunity has two functions. First, it exempts persons reporting from the legal requirement to uphold professional secrecy and confidentiality.⁶⁹ Second, it protects persons making a report in good faith against damages claims by the persons whom they report to the FRC. Besides, POCAMLA provides that the details of the informant should be kept confidential, with only a few exceptions in which they can be disclosed.⁷⁰ Therefore, persons are free to report suspicious transactions or any case related to ML. As of 2015, the FRC had received 876 STRs.⁷¹ Surprisingly, adequate protection of staff is yet to be realised. In 2016, the Central Bank Governor complained that following

⁶⁴ FRC Guidelines (2017: 15).

⁶⁵ Fourth Schedule of POCAMLA.

⁶⁶ See <http://frc.go.ke/reporting/cash-transactions.html> (accessed 30 September 2017).

⁶⁷ Preamble Financial Intelligence Centre Amendment Act No. 1 of 2017.

⁶⁸ Sec 19 of POCAMLA.

⁶⁹ Sec 17 of POCAMLA.

⁷⁰ Sec 20 of POCAMLA.

⁷¹ US Department of State Report (2017).

stringent action against rogue banks, some of the bank's staff had been threatened.⁷² Such incidents should be well investigated and the culprits should be prosecuted to inspire confidence among the staff and persons who may have information on ML incidents.

The FRC needs to secure the reporting process against incidents of tipping off persons involved in suspicious transactions. Despite prohibiting tipping off, Section 8(2) of POCAMLA falls short of the FATF recommendation, since the provision appears to prevent only divulging "information or other matters that might prejudice any investigation of an offence or possible offence of money laundering".⁷³ The 2017 US Department of State Report on *Money Laundering and Financial Crimes* published by the Bureau for International Narcotics and Law Enforcement Affairs shows that the confidentiality of the process is not well secured.⁷⁴ Divulging information on STRs allows parties involved to rearrange their affairs to avoid detection or to dissipate illicitly obtained assets.

Another area of concern is that it is possible for smurfs to structure cash transactions below the reporting threshold and use the banking system undetected. The *FRC Reporting Guideline 2017* describes the typologies of smurfing, which is a welcome step in keeping smurfs from gaining access to financial institutions. However, porous borders and the vibrant cash-based economy, which is typical of Africa, allows cash to be smuggled in and out of the country undetected.⁷⁵ Such clandestine cross-border crimes may undermine the efficacy of cash

⁷² Mutai E "CBK staff receive threats over Imperial Bank audit" 17 May 2016 *Business Daily*, available at <http://www.businessdailyafrica.com/CBK-staff-get-threats-over-Imperial-Bank-audit/539546-3207578-n42r9dz/index.html> accessed (on 16 October 2017).

⁷³ ESAAMLG Report (2011: 128).

⁷⁴ Sec 8 of POCAMLA; US Department of State Report (2017: 117).

⁷⁵ Shetret L *et al* (2015: 31).

declaration requirements.⁷⁶ It is therefore necessary that the FRC be proactive and innovative in responding to potential threats to effective reporting.

3.3.2 Access to information

FIUs should have adequate powers to gain access to information in the course of carrying out their mandate.⁷⁷ This information can come from reporting institutions or any other person. Section 24(e) of POCAMLA allows the FRC to request reporting institutions to provide it with additional information. This information should be readily available since POCAMLA requires reporting institutions to keep customer identification records and transaction data for at least seven years.⁷⁸

Where necessary, the FRC may inspect the premises and documents of reporting institutions or their officers.⁷⁹ During the inspection, the inspecting officer may question officers and request to look at written correspondence. The information shared during the inspection has to be treated as confidential and used solely for the purposes prescribed by the law.⁸⁰ This provision is aimed at preventing the admissibility of incriminating information shared by an officer of a reporting institution when facing criminal charges.⁸¹ Furthermore, the FRC may request a supervisory body, monetary authority, financial regulatory authority, fiscal or tax agency or fraud investigations agency for further information in the course of its duties.⁸²

⁷⁶ Sec 12 of POCAMLA.

⁷⁷ Paras 5 & 6 Interpretive note to FATF Recommendation 29.

⁷⁸ Secs 12(5B)(b), 44(5) & 46(4) of POCAMLA.

⁷⁹ Secs 24(c), 33, 34 & 35 of POCAMLA.

⁸⁰ Sec 33(5) of POCAMLA.

⁸¹ In the UK, information obtained during inspection is only admissible in a criminal case which the accused is facing charges of perjury or giving false information. See Booth R *et al* (2011: 249).

⁸² Sec 24(r) of POCAMLA.

The FRC has the power to apply for search warrants⁸³ as well as for property tracking and monitoring orders.⁸⁴ Both applications are made to the High court. Conferring jurisdiction exclusively on the High Court may occasion delays in obtaining court orders in cases from regions without a permanent High Court. Once granted, search warrants allow the FRC to gain access to information that may be concealed by a reporting institution or its officials. Property tracking and monitoring orders are powerful tools that permit the FRC to retrieve the confidential information necessary for constructing a financial profile of a suspected person.⁸⁵ Considering the intrusive nature of the orders into a person's privacy, the courts have to strike a balance between enabling the expeditious enforcement of AML/CTF measures, on the one hand, and protecting a person's privacy, on the other hand.⁸⁶

3.3.3 Analysing Information

In general, FIUs need to use the information they receive gainfully.⁸⁷ This is done through a rigorous analysis process that leads to obtaining the required financial intelligence. FIUs have to design workable and efficient methods that will help accelerate responses to the wide range of information garnered from the STRs they receive. To guarantee the effectiveness of FIUs, the interpretive note to FATF Recommendation 29 stresses the need to computerise data and to use state-of-the-art software with analytical capacity. But the FATF cautions against replacing human judgment with computers.⁸⁸ However, as noted in the 2017 US report on ML, manual analysis of information poses a significant challenge to the FRC.⁸⁹

⁸³ Sec 37 of POCAMLA.

⁸⁴ Sec 38 of POCAMLA.

⁸⁵ Smit P (2007: 793).

⁸⁶ Boszormenyi J & Schweighofer E (2015: 71).

⁸⁷ Para 3 of the Interpretive note to FATF Recommendation 29.

⁸⁸ Para 3 of the Interpretive note to FATF Recommendation 29.

⁸⁹ US Department of State Report (2017: 117).

The FATF recommends that FIUs adopt two levels of analysis, namely, operational analysis and strategic analysis.⁹⁰ Operational analysis is the starting point of analysing data. Data received is matched with other received information to identify cases that merit further investigation. The FIU focuses on building a specific case. Strategies such as financial profiling may be used to detect anomalies in property ownership. Though the methods used by the Kenyan FRC could not be established at the time of writing, the low number of ML prosecutions suggest that the operational analysis is not up to scratch.⁹¹ This is not to say that, barring the inadequacies of the FRC, the prosecution service and the judiciary are flawless.

The second and final part of the analysis is the strategic analysis. Unlike the tactical analysis, the strategic analysis does not focus on a particular case or transaction,⁹² but takes account of general typologies and trends in evolving criminal patterns. It is a painstaking exercise, for it involves voluminous data analysis and expertise. It is from this analysis that the FRC can recommend policy changes in response to ML typologies. Unfortunately, an effective strategic analysis is hampered by both an inadequately staffed FRC and the lack of expertise.

3.2.3 Dissemination of Information

FIUs are required to disseminate information upon request or spontaneously for further investigation or prosecution by law enforcement units and other sanctioned entities.⁹³ Spontaneous dissemination occurs when the FIU shares information with competent authorities where there are grounds to suspect cases of ML, the commission of predicate

⁹⁰ Para 3 of the Interpretive note to FATF Recommendation 29; Schott P A (2006: VII-6).

⁹¹ For example, in 2015, there were two prosecutions for ML out of which as of 2016, there was no conviction. See US Department of State Report (2015).

⁹² IMF/World Bank (2004: 67).

⁹³ FATF Recommendation 29; Para 4 of the Interpretive note to FATF Recommendation 29.

offences or terrorist financing. Dissemination upon request allows FIUs to respond to requests for information made by competent authorities or foreign FIUs when conducting investigations on ML, predicate offences or TF.⁹⁴ In sharing information upon request, the decision to comply with such a request should remain with the FIU.⁹⁵ This bolsters the functional independence of FIUs. The duty to disseminate information can be classified into three categories, namely, the duty to share information for investigation or prosecution; sharing information with other domestic agencies; and international sharing of information.⁹⁶

a) The Duty to Share Information with Law Enforcement Agencies

The FRC has a duty to share information with law enforcement agencies and intelligence units where the Director-General “has reasonable grounds to suspect that a transaction or activity involves proceeds of crime, money laundering or financing of terrorism”.⁹⁷ By including “proceeds of crime”, the information shared is not confined to ML and TF cases.⁹⁸ This conforms to the “all crimes approach” adopted by POCAMLA in defining ML. This means that all acquisitive crimes are predicate offences for ML. Since the use of information from the FIUs is strictly regulated (speciality principle), the “all crimes approach” allows the FRC to share information with other agencies such as the tax authorities, where the information is required for fiscal purposes and for combating tax related crimes. As of 2015, of the 876 STRs submitted to the FRC since its inception in 2012, a total of 254 had been disseminated to law enforcement agencies.⁹⁹

⁹⁴ FATF Recommendation 31.

⁹⁵ Interpretive note to FATF Recommendation 29.

⁹⁶ IMF/World Bank (2004: 60).

⁹⁷ Sec 24(b) & (c) of POCAMLA.

⁹⁸ Sec 2 of POCAMLA and Article 2(e) of the Palermo Convention define proceeds of crime.

⁹⁹ USA Department of State Report (2015).

b) Sharing Information with other Domestic Agencies

POCAMLA allows the FRC to share information with listed regulatory bodies.¹⁰⁰ Because of the strict regulations of sharing information by FIUs, the FRC may not share information with any supervisory body excluded from this list.¹⁰¹ Information shared with supervisory bodies encompasses statistics and misconduct among persons regulated by the relevant supervisory body. Unlike law enforcement agencies that receive information only in cases of suspected criminal activity, supervisory bodies receive information on unethical conduct that allows room for administrative or civil sanctions. The FRC has signed a memorandum of understanding already with regulatory bodies through which information is shared.¹⁰² Such memoranda of understanding may provide a detailed outline of the information that the FRC shares and whether supervisory bodies are entitled to request information.

c) International Sharing of Information

Effective exchange of information among FIUs is part of the global strategy for combating transnational crime. The FIUs provide an informal and secure channel that allows for the prompt exchange of information between states. This can be done under the auspices of the Egmont Group, the international body that co-ordinates the work of national FIUs. However, of their own volition, FIUs can enter into a mutual agreement with foreign FIUs. Non-member states such as Kenya cannot have access to the database of the Egmont Group. Nevertheless, section 24(l) of POCAMLA allows the FRC to enter into a mutual agreement to share information with foreign FIUs. The information is shared on a case-by-case basis and,

¹⁰⁰ Sec 23(2)(a) of POCAMLA; The First Schedule of POCAMLA lists regulatory bodies, namely, the Central Bank of Kenya; Insurance Regulatory Authority; Betting and Licensing Control Board; Capital Markets Authority; Institute of Certified Public Accountants of Kenya; Estate Agents Registration Board; Non-Governmental Organisations Co-ordination Board; and the Retirement Benefits Authority.

¹⁰¹ Stessens G (2003: 190).

¹⁰² See Remarks by Njuguna Ndung'u, Governor of the Central Bank of Kenya (2014).

therefore, there is no room for spontaneous dissemination.¹⁰³ In each case, the foreign FIU must give a written undertaking to protect the confidentiality of information received, and to exercise control over the use of such information. The requirement of a written undertaking shows strict observance of the confidentiality and speciality principles. Before Kenya joins the Egmont Group, it will be important that the standard for the mutual agreement be akin to the Egmont Group standards.¹⁰⁴

Apart from acting in terms of a mutual agreement, the FRC can share information relating to the commission of an offence with any foreign FIU or appropriate foreign law enforcement authorities.¹⁰⁵ The FRC can use this provision to exchange information with other authorities, such as Interpol and Europol, in preventing transnational crimes. The success of international co-operation is predicated upon the level of trust and integrity maintained by the FRC.¹⁰⁶ Since most relations are based on reciprocal mutual agreements, failure to maintain high standards of trust can lead to exclusion from the global crime prevention networks.¹⁰⁷ Despite POCAMLA's enabling framework of sharing information, the FRC needs to accelerate its effort to join the Egmont Group.

3.4 Other Functions of the Financial Reporting Centre

Apart from the core functions of receiving, analysing and disseminating intelligence to competent authorities, FIUs monitor compliance with the AML/CTF requirements, block transactions, train staff of reporting institutions on their AML/CTF obligations, conduct

¹⁰³ IMF/World Bank (2004: 69).

¹⁰⁴ See Egmont Group Principles for Exchange of Information (2013).

¹⁰⁵ Sec 24(k) of POCAMLA.

¹⁰⁶ IMF/World Bank (2004: 69).

¹⁰⁷ Schott P A (2006: VIII-6). IMF/World Bank (2004: 69).

research, sensitise the public to AML/CTF issues, store data, and formulate policies.¹⁰⁸ The FRC has powers to carry out these obligations, as discussed below.

3.4.1 Monitoring Compliance

The FRC has a primary role of monitoring compliance with AML/CTF obligations among reporting institutions.¹⁰⁹ However, it may delegate monitoring duties to regulatory bodies. The FRC is authorised to inspect reporting institutions.¹¹⁰ During the inspection, the respective reporting institutions and their officers are under obligation to co-operate with the FRC's officer or appointed inspector.¹¹¹ Failure to give information within the prescribed time or obstruction of the inspection process is a criminal offence.¹¹²

The power of the FRC to inspect reporting institutions allows it to monitor compliance directly without the need for a regulatory body. These powers can be utilised intensively when dealing with non-regulated reporting institutions such as dealers in high-value goods and car dealers, and sparingly among the regulated sector in complementing regulatory bodies.¹¹³ Bearing in mind the high number of non-regulated reporting institutions, the FRC needs to adopt an innovative approach to monitor compliance. For example, the FRC needs to provide registration or licencing guidelines with a periodic renewal of operating licences to facilitate easy monitoring.¹¹⁴

Section 36A(3) provides that monitoring compliance with POCAMLA constitutes a core function of supervisory bodies. Unlike the FRC, supervisory bodies have expertise in

¹⁰⁸ IMF/World Bank (2004: 70).

¹⁰⁹ Sec 36A of POCAMLA.

¹¹⁰ Sec 24(c) & 33 of POCAMLA.

¹¹¹ Sec 35 of POCAMLA.

¹¹² Sec 35(2) of POCAMLA.

¹¹³ Broek M (2011: 161).

¹¹⁴ Broek M (2011: 161).

supervising the various institutions. They already have established procedures and prudential regulations, and often AML monitoring may not strain their resources.¹¹⁵ For example, the Central Bank of Kenya has in place the *Anti- Money Laundering Guidelines for the provision of Mobile Payment Services* of 2013, among other banking sector AML regulations, while the Insurance Regulatory Authority has the *Guidelines to the Insurance Industry on Implementation of the Proceeds of Crime and Anti-Money Laundering Act and Prevention of Terrorism Act of 2016*. POCAMLA allows supervisory bodies to use fines paid by non-compliant institutions to defray their incurred expenses.¹¹⁶ This may act as an incentive for regulatory bodies to heighten their AML compliance supervision. POCAMLA gives supervisory bodies extensive powers to monitor compliance. These include the power to determine whether employees of a reporting institution are fit and proper persons and whether the reporting institution has in place up-to-date technology.¹¹⁷

Furthermore, supervisory bodies have an obligation to submit periodic reports to the FRC on actions taken or rules formulated in the exercise of their respective supervisory mandates.¹¹⁸ In 2013, the FRC signed a memorandum of understanding with regulators to monitor AML compliance in the respective sectors.¹¹⁹ These are significant strides towards effective co-ordination and making the supervisory bodies understand the ML threat facing a particular industry or sector.

Generally, the efficacy of regulatory bodies and reporting institutions in giving effect to AML/CTF measures is predicated on the conviction that ML/TF threatens the well-being of

¹¹⁵ Broek M (2011: 157).

¹¹⁶ Sec 36A(4) of POCAMLA.

¹¹⁷ Sec 36A(5)(e) of POCAMLA.

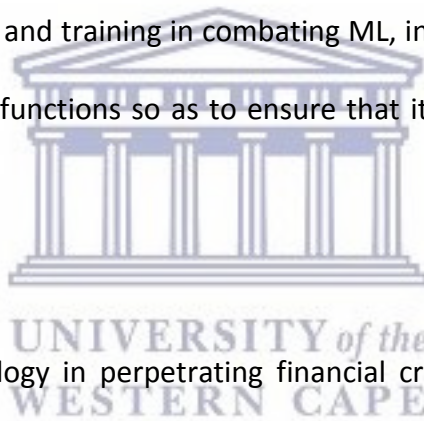
¹¹⁸ Sec 36(6) of POCAMLA.

¹¹⁹ See Remarks by Njuguna Ndung'u, Governor of the Central Bank of Kenya (2014).

the respective sector.¹²⁰ Therefore, the FRC needs continually to educate supervisory bodies on typologies and the perilous effects of ML for the respective sector.

3.4.2 Training, Research and Sensitisation

The clandestine nature of ML requires absolute awareness among the staff of the reporting institutions and also the public at large.¹²¹ Also, during training, the FRC staff interact with officials of reporting institutions. This helps in building trust among them.¹²² It increases co-operation between the FRC and reporting institutions and equips officials in reporting institutions with knowledge on ML typologies. Furthermore the evolving nature of ML requires extensive research to ensure that responses keep abreast of the portending risks. Despite the utility of research and training in combating ML, in light of resource constraints, the FRC needs to balance its functions so as to ensure that it does not stray from its core objectives.¹²³



3.4.3 Blocking Transactions

The increased use of technology in perpetrating financial crimes requires swift action in blocking transactions. FIUs need adequate power to respond promptly before suspects dissipate the proceeds of crime.¹²⁴ Section 12(4) of POCAMLA allows authorised officers, who are defined as police officers, customs officials and the director of the Asset Recovery Agency, to seize temporarily monetary instruments suspected to be tainted. This seizure can last for a maximum of five days without judicial recourse. Considering the limited definition of an

¹²⁰ Broek M (2011: 155); Al-Rashdan M (2012: 493).

¹²¹ Sec 24(g) of POCAMLA.

¹²² Simwayi M & Haseed M (2011: 130).

¹²³ Schott PA (2006: VI-17).

¹²⁴ Art 12 of the Palermo Convention; Art 8 of the International Convention for the Suppression of the Financing of Terrorism.

authorised officer, it is not certain whether this power is directly available to the FRC in blocking transactions.

In South Africa, the FIC can direct the reporting institutions to block suspicious transactions for five days.¹²⁵ In the UK, seizure of cash lasts for 48 hours.¹²⁶ Notwithstanding the absence of an express provision, effective co-operation with authorised officers such as those in the Asset Recovery Agency would allow the FRC to benefit from this provision.

Holding assets or suspending a transaction for five days can affect a person's economic circumstances severely. Hence, this power should be exercised reasonably. In cases where the power is invoked maliciously, an aggrieved party should be able to seek compensation from the state.¹²⁷ Therefore, this power should be exercised only in cases where, once the transaction is carried out, the subsequent judicial process would be unfeasible or severely compromised.¹²⁸ Also, developing a close working relationship with the police and asset recovery agency contributes hugely to swift interventions by way of seizure and freezing of property, which fall within the mandate of the Asset Recovery Agency and police.

3.4.4 Data Storage

The automation of data protection and storage by the FRC is a key determinant for discharging its function effectively. Data held by the FRC should be encrypted and secured from hackers and other internet surveillance agencies. However, it should be readily accessible for use by authorised persons. POCAMLA does not stipulate the maximum period that the FRC may store data. However, among reporting institutions, customer information is kept for seven

¹²⁵ Sec 34 of FICA.

¹²⁶ Booth R *et al* (2011: 276).

¹²⁷ Sieńczyło-Chlabicz J & Filipkowski W (2001: 155).

¹²⁸ Sieńczyło-Chlabicz J & Filipkowski W (2001: 155).

years.¹²⁹ Section 24(j) mandates the FRC to keep and maintain a database of STRs and other incidental information. The FRC has a duty to compile statistics and, where necessary, to share such statistics with other agencies. Proper storage of data helps in generating statistics often used in assessing the effectiveness of the FRC and the entire AML process.¹³⁰ It also enables the FRC to maintain its crucial capacity to carry out strategic analysis.

3.5 The Secrecy Duty of the Financial Reporting Centre

The functions of the FIUs allow them to gain access to vast amounts of information which need to be held confidentially. The sensitivity of this information imposes a corresponding obligation on FIUs to adhere strictly to confidentiality principles.¹³¹ In addition, FIUs have a corollary obligation to restrict the use of this information.

The importance of maintaining secrecy is invaluable. First, it creates a climate of trust between FIUs and reporting institutions.¹³² As discussed under the drawbacks of the law enforcement model of FIUs, financial institutions are not natural partners of law enforcement agencies. Therefore, an assurance of confidentiality allows increased sharing of information by financial institutions. To guarantee confidentiality, POCAMLA provides that: (i) the Director-General and other officials of the FRC must take a prescribed oath of confidentiality before commencing their employment;¹³³ (ii) before sharing information with foreign FIUs, they must undertake to uphold the confidentiality of the information shared;¹³⁴ (iii) all information accessed by FRC officials during inspections of reporting institutions should be

¹²⁹ Sec 46(4) of POCAMLA.

¹³⁰ FATF Recommendation 33; Koker L & Turkington M (2015: 526).

¹³¹ Para 7 of the Interpretive Note to FATF Recommendation 29.

¹³² Stessens G (2003: 190)

¹³³ Sec 32 of POCAMLA.

¹³⁴ Sec 24(l)(i) of POCAMLA.

kept confidential;¹³⁵ and (iv) section 121(3) prohibits any person from disclosing information obtained in the course of executing his mandate under the POCAMLA without obtaining written permission from the Attorney-General. This provision binds also persons or institutions co-opted by the FRC in the course of carrying out its mandate.

Exceptions to maintaining confidentiality include where one is performing functions under POCAMLA, adducing evidence in criminal proceedings or proceedings under POCAMLA, when required by a court order, or when one has obtained written permission from the Attorney-General.¹³⁶ These exceptions guarantee a heightened degree of confidentiality. However, it is not clear under which circumstances the Attorney-General sanctions the sharing of information.¹³⁷ There is therefore a need to prescribe narrowly such situations to guard against misuse of power by the Attorney-General. Persons who contravene POCAMLA commit a criminal offence which is punishable by a maximum fine of three million Kenya shillings (approximately US\$ 29,000) or a maximum jail term of three years or both.¹³⁸

Second, the secrecy duty aims at protecting personnel of reporting institutions.¹³⁹ They are thus cushioned against the risk of retaliation when they forward suspicious transactions to the FRC. Also, it acts as an incentive for personnel to share information readily. Section 20(1) of POCAMLA bars the FRC or authorised officers from disclosing the identity of informers. The identity of informers can be disclosed only when it is necessary to perform duties under POCAMLA, or in judicial or other proceedings where the court deems the disclosure necessary.

¹³⁵ Sec 33(5) of POCAMLA.

¹³⁶ Sec 121(3) of POCAMLA.

¹³⁷ Sec 121(3) of POCAMLA.

¹³⁸ Sec 121(4) of POCAMLA.

¹³⁹ Stessens G (2003: 190).

Third, to the extent that the information shared with FIU is protected by the right to privacy, the secrecy duty safeguards the right to privacy of persons in respect of whom the information shared relates.¹⁴⁰ Article 31 of the Kenyan Constitution protects a person's right to privacy.¹⁴¹ Considering the sensitive nature of financial information handled by FIUs, failure to maintain confidentiality violates the right to privacy. This may open the floodgates for affected persons to petition the courts for remedies.

Fourth, the adherence to the secrecy duty allows information to be subjected to the speciality principle. The secrecy duty and speciality principle complement each other in that the FIU can share information for permissible use only. Therefore, the duty to keep information confidential allows sanctioned entities only to access and to use the secret financial information.¹⁴² Without observing the secrecy duty, it will be inconceivable to regulate the use of the information.

Despite the importance of maintaining secrecy and confidentiality, FIUs should be cautious to prevent this circumstance from unnecessarily affecting their relationship and co-operation with other agencies. This is a problem in countries like Belgium, where the FIU divulges information to the prosecution authorities, and not the police, only when a serious crime is suspected to have been committed.¹⁴³ Even though it is desirable that the information is made accessible to law-enforcement agencies to facilitate the investigation and prosecution of suspects,¹⁴⁴ in Kenya, additional diligence is required since widespread corruption within the police service frustrates investigations at times.¹⁴⁵

¹⁴⁰ Stessens G (2003: 190).

¹⁴¹ Art 31 of the Constitution of Kenya 2010.

¹⁴² Egmont Group Principles for Exchange of Information (2013).

¹⁴³ Stessens G (2003: 192).

¹⁴⁴ IMF/World Bank (2004: ix).

¹⁴⁵ US Department of State Report (2017: 117)

3.6 The Speciality Principle

Although this principle co-exists with the duty of secrecy, the two are different concepts. Unlike the secrecy duty that safeguards the confidentiality of information, the speciality principle restricts the use of information. In principle, information divulged to the FIU or by the FIU can be used only for specific purposes.¹⁴⁶ In jurisdictions such as Belgium, the use of information shared is confined strictly to combating ML and TF. However, in countries such as Kenya, in which all crimes are predicate offences for ML, the information can be shared more widely in combating crime.¹⁴⁷

Apart from being used to combat crime, it is not clear whether information from the FRC can be used for fiscal and administrative purposes. POCAMLA lacks an explicit clause that allows the use of information for tax collection and other related matters. Where the information is used for fiscal administration, it helps to circumvent legal impediments to gaining access to bank files.¹⁴⁸ In Australia, one of the goals of AML measures is to increase revenue from tax collection. In 2013-2014, Australia's FIU, AUSTRAC, helped the Australian Taxation Office raise US\$278.7 million in tax assessments.¹⁴⁹ In such cases, FIUs play a beneficial role in combating tax evasion and related crime. In South Africa, customs authorities can gain access to information which is shared for tax administration.¹⁵⁰ Therefore, in Kenya, the FRC needs to establish a close working relationship with the Kenya Revenue Authority in combating tax crimes.

¹⁴⁶ Durrieu R (2013: 166).

¹⁴⁷ Unger B (2007: 129).

¹⁴⁸ Stessens G (2003: 194).

¹⁴⁹ See "AUSTRAC: Australia's financial intelligence unit" available at <http://www.austrac.gov.au/about-us/intelligence> (accessed 20 October 2017).

¹⁵⁰ Sec 29(1)(b)(iv) of FICA.

3.7 Sharing Information with Reporting Institutions

FATF Recommendation 34 requires FIUs to give feedback on information sent to them and to provide guidance to reporting institutions. However, sharing feedback with Reporting Institutions can be seen as a threat to the secrecy principle. POCAMLA does not mention whether or not the FRC should give feedback to the reporting institutions.

Feedback allows reporting institutions also to identify the type of transactions susceptible to ML.¹⁵¹ These can help in developing a risk-based approach to AML/CTF reporting. A risk-based approach entails a comprehensive diagnosis of the ML threats, thus enabling the reporting institution to channel most of its resources to focus on the riskiest areas. This approach ensures that the response is more precise and cost-effective.¹⁵² In addition, by sharing feedback, reporting institutions can take the appropriate internal measures, such as terminating the relationship with specific clients. Finally, feedback motivates reporting institutions since they appreciate their role in the national AML strategy.¹⁵³

Where no feedback is given frustration sets in, as reporting institutions can gain the impression that they are performing a perfunctory duty, which is not helpful in the fight against ML/TF. Although it may be desirable to share information on a case-by-case basis, general information based on statistics helps reporting institutions and law enforcement units to understand the typologies of ML/TF. To avoid compromising ongoing information, it is desirable that the FRC provide feedback to reporting institutions upon completion of investigations.¹⁵⁴

¹⁵¹ Gordon R K (2011: 528).

¹⁵² FATF Recommendation 1; Parkman T (2012: 99).

¹⁵³ Gordon R K (2011: 528).

¹⁵⁴ Stessens G (2003: 193).

3.8 Powers of the Financial Reporting Centre to Impose Sanctions

The FRC has the power to impose civil and administrative sanctions against non-compliant reporting entities. Section 24A of POCAMLA mandates the FRC to issue directions or instructions to reporting institutions. Any person who fails to comply with the instructions or rules is liable to incur a civil penalty in the form of a fine payable to the FRC.¹⁵⁵ Once imposed, the monetary fine becomes a debt owed to the FRC and is enforceable through court proceedings.¹⁵⁶

Besides being able to impose civil penalties, the FRC may issue administrative sanctions in appropriate cases.¹⁵⁷ The prescribed administrative sanctions include warning the non-compliant reporting institution, issuing compelling orders to the reporting institutions or specific officers, and banning an employee from working in a specific sector or holding certain positions. Furthermore, the FRC can direct a supervisory body to enforce drastic sanctions such as suspension or withdrawal of an operating licence of a reporting institution, or banning a specific person from the industry.¹⁵⁸

Unlike criminal trials with a high standard of proof, administrative proceedings require a lower standard of proof, which is proof on a balance of probabilities, and reckless or negligent conduct may suffice for *mens rea*.¹⁵⁹ Based on the complex nature of ML crimes, especially when dealing with financial institutions, administrative sanctions remain a viable tool for the FRC and regulators.¹⁶⁰

¹⁵⁵ Sec 24B of POCAMLA.

¹⁵⁶ Sec 24B(4) of POCAMLA.

¹⁵⁷ Sec 24C of POCAMLA.

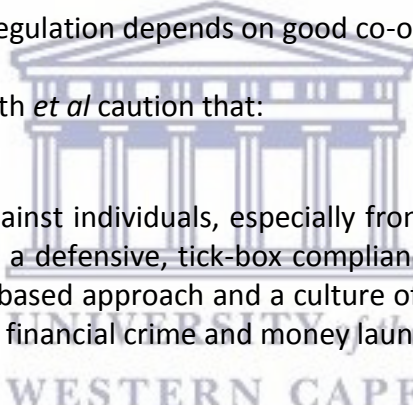
¹⁵⁸ Sec 24C(d) of POCAMLA.

¹⁵⁹ Gilchrist GM (2014: 45).

¹⁶⁰ Gilchrist GM (2014: 52).

Before enforcing sanctions, the FRC must give a written notice to the reporting institution, indicating the extent of the breach.¹⁶¹ Also, under section 39 of POCAMLA, the FRC may apply to the High Court to enforce its orders. Issuing notice and involving the court in enforcing the FRC orders safeguards a person's right to a fair administrative action, and increases the legitimacy of the administrative sanctions.¹⁶² As Gilchrist notes, civil and administrative sanctions are more dissuasive where they complement criminal sanctions.¹⁶³ Thus, where the criminal conduct of a person or entity is established, criminal sanctions are preferable.

In line with FATF Recommendation 35, the FRC should formulate effective, proportionate and dissuasive sanctions. Even though harsh sanctions have a high deterrent value, they may not be desirable where effective regulation depends on good co-operation between the FRC and the reporting institutions. Booth *et al* caution that:



[C]riminal sanctions against individuals, especially frontline staff, create a fear culture and encourage a defensive, tick-box compliance. They may inhibit the development of a risk-based approach and a culture of active involvement and cooperation in tackling financial crime and money laundering.¹⁶⁴

These effects may occur also where the front-line staff face threats of harsh administrative sanctions, such as being banned from working in the industry.¹⁶⁵ Even though harsh sanctions have had a positive influence in countries like the USA, they have limitations in the financial sectors. Gilchrist states that huge fines paid by big banks are not commensurate to the profits

¹⁶¹ Sections 24B(2) & 24C(2) of POCAMLA.

¹⁶² Art 47 the Constitution of Kenya 2010; Gilchrist GM (2014: 50).

¹⁶³ Gilchrist GM (2014: 52).

¹⁶⁴ Booth *et al* (2011: 27).

¹⁶⁵ Gilchrist G M (2014: 50).

derived from crime. He cautions that commensurate sanctions may lead to bank failures and affect adversely the interests of innocent third parties such as shareholders.¹⁶⁶

In Kenya, the FRC would do well to adopt a co-operative strategy by establishing an ongoing dialogue with reporting institutions. Part of the dialogue should entail capacity-building measures. Where there is a need for sanctions, they should be effective and proportionate. Strategies such as rewarding most compliant institutions for their dutifulness can motivate reporting institutions to co-operate effectively.¹⁶⁷ Finally, a bigger role that befalls the FRC, is establishing comprehensive regulations to seal all loopholes that can be exploited by money launderers and terrorist financiers.

3.9 The Anti-Money Laundering Advisory Board (AMLAB)

FATF Recommendation 2 provides for the establishment of effective national co-operation among AML/CTF agencies. In establishing effective co-operation, states have the discretion to adopt formal, informal or ad-hoc institutions. In Kenya, AMLAB was established as a platform to co-ordinate the country's AML strategy. AMLAB consists of:¹⁶⁸

- The Permanent Secretary of the Treasury;
- The Attorney-General;
- The Governor of the Central Bank of Kenya;
- The Inspector General of the National Police Service;
- The Chairman of Kenya Bankers' Association;
- The Chief Executive Officer of the Institute of Certified Public Accountants of Kenya;
- The Director-General of the National Intelligence Service;

¹⁶⁶ Gilchrist G M (2014: 21).

¹⁶⁷ Al-Rashdan M (2012: 493).

¹⁶⁸ Sec 49 of POCAMLA.

- The Director of the Asset Recovery Agency;
- Two other persons appointed by the Cabinet Secretary in charge of finance from the private sector; and
- The Director-General of the Financial Reporting Centre, who is also the Secretary to the Board.

The composition of AMLAB is broad and it includes reporting institutions, supervisory bodies and law enforcement agencies. Its profile is enhanced also by the fact that the Cabinet Secretary can appoint two persons from the private sector. However, it omits representatives from the Law Society of Kenya and the gambling industry, who remain vulnerable to ML and TF.¹⁶⁹ In line with Recommendation 2, the inclusive composition of AMLAB enhances proper co-ordination in formulating and implementing AML policies. In addition, AMLAB has powers to co-opt experts in AML/CTF to participate in its deliberations.¹⁷⁰

The discretion of the Cabinet Secretary to appoint two members from the private sector and the chairperson of AMLAB, may be a drawback in AMLAB's composition, for unbounded discretion can be exercised to reward cronies. Also, since persons appointed act in their individual capacity and not as institutional representatives, it is not clear who should represent them in case of their absence.¹⁷¹ In appointing the chairperson, a vote by the members would have ensured a proper safeguard and a sense of ownership of the entire process among the members of AMLAB. Private persons appointed by the Cabinet Secretary

¹⁶⁹ In the UK, the Money Laundering Advisory Committee goes an extra step to include representatives from the gambling industry, the law society and the surveyors. See Booth R *et al* (2011:25).

¹⁷⁰ Sec 49(4) of POCAMLA.

¹⁷¹ Sec 49(2) of POCAMLA allows all members to attend meetings in person or through designated representatives.

hold office for a term of three years and are eligible for re-appointment.¹⁷² In 2014, delayed renewal of terms by the Cabinet Secretary almost crippled the functions of the AMLAB.¹⁷³ Based on its mandate, it is important for AMLAB to be constituted adequately.

3.9.1 Functions of AMLAB

AMLAB has three main functions, namely, advising the Cabinet Secretary on best practices and policies in AML/CTF, advising the FRC on its powers and functions in combating ML and creating a forum for consultation among the FRC, state organs, supervisory bodies and reporting institutions.¹⁷⁴ Through these consultations, the government can devise responsive anti-corruption policies that take into account the views of stakeholders.¹⁷⁵ AMLAB relies on the administrative support and resources of the FRC in performing its function.¹⁷⁶ Therefore, the FRC's constraints, such as inadequate funds, have a bearing on AMLAB's effectiveness. Considering the infancy of Kenya's AML regime, AMLAB needs to play a more pro-active role. Following the 2017 amendment of the FICA, South Africa abolished the Counter-Money Laundering Advisory Council, which was the equivalent of Kenya's present AMLAB.¹⁷⁷ Such a measure may be desirable once the country has an effective AML regime and strong inter-agency co-operation.

3.9.2 General Working of AMLAB

AMLAB meets at least four times a year. The Chairperson presides over the meetings. The decisions by AMLAB are taken by a majority vote. In case of a tie, the Chairperson has a casting

¹⁷² Sec 49(3) of POCAMLA.

¹⁷³ Anyanzwa J "Trouble brews at Kenya's financial intelligence unit" *The East African*, available at <http://www.theeastafrican.co.ke/news/Trouble-brews-at-Kenya-financial-intelligence-unit-/2558-2555128-rxc3isz/index.html> (accessed 30 September 2017).

¹⁷⁴ Sec 50 of POCAMLA.

¹⁷⁵ Booth R *et al* (2011: 24).

¹⁷⁶ Sec 50(2) of POCAMLA.

¹⁷⁷ Preamble to the Financial Intelligence Centre Amendment Act no. 1 of 2017.

vote. Each member is allowed to have his opinion recorded where AMLAB adopts a resolution contrary to his advice or to law. This provision is in line with sound principles of corporate governance which ensure accountability in decision-making.¹⁷⁸ In the event of a conflict of interest, a member is allowed to notify AMLAB and recuse himself. Ordinarily, a quorum of six is sufficient for AMLAB to constitute a meeting.

3.10 Conclusion

Despite a few drawbacks, such as inadequate funding and the wide discretion vested in the Cabinet Secretary, POCAMLA gives the FRC and AMLAB a strong legal backing to combat ML/TF in Kenya and globally. It is appalling that since its establishment in 2012, the FRC has been operating under an interim Director-General. With its instrumental responsibility in fighting ML, this indefiniteness casts doubt on the government's commitment to fighting ML. The recent effort to reconstitute and to augment the funding of the FRC is a positive development. However, taking into account the budgetary allocations for the 2017/2018 financial year, the reconstitution may not be as rapid as initially thought. These, among other, challenges are outlined in the next chapter. Also, the chapter gives a set of recommendations aimed at improving the efficacy of the FRC and AMLAB.

¹⁷⁸ Global Corporate Governance Forum (2011: 15).

CHAPTER 4

CHALLENGES AND RECOMMENDATIONS

This research paper has discussed the structure, mandate, and functions of the Financial Reporting Centre (FRC) and the Anti-Money Laundering Advisory Board (AMLAB). Despite the loopholes highlighted in this paper, these institutions could still establish a strong and effective AML framework. This concluding chapter discusses pressing challenges that need to be surmounted and it gives recommendations to ensure the effective and proper functioning of the FRC and AMLAB.

4.1 Challenges

4.1.1 Lack of political will

In most cases, the beneficiaries of the grand ML schemes are top government officials or their proxies. For example, in 2010, a report tabled in Kenya's Parliament implicated six members of parliament in trafficking drugs.¹ Surprisingly, subsequent investigations did not come to a conclusion. This explains in part why in most cases the political elites are ambivalent about implementing AML measures. The FRC, which was established in 2012, continues to function under an interim Director-General.² Coupled with the delayed recruitment of staff of the FRC, this shows that the government does not prioritise AML measures. In some cases, where institutions, such as the judiciary, perform their mandate effectively, their budgets have been

¹ Wafula C "Six Kenya MPs named in drug baron scandal" 22 December 2010 *Daily Nation*, available at <http://www.nation.co.ke/news/politics/Six-Kenya-MPs-named-in-drug-baron-scandal/1064-1077186-hwjiroz/index.html> (accessed 20 October 2017).

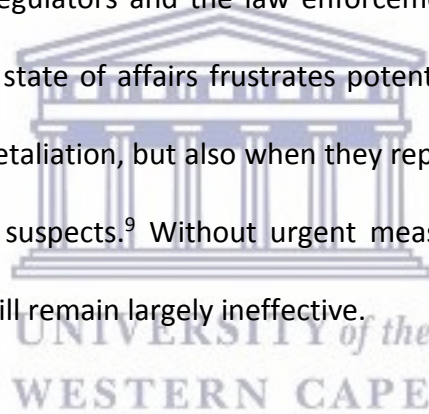
² See <http://frc.go.ke/others/2016-07-07-20-12-50.html> (accessed 28 August 2017).

cut.³ In turn, this has affected the implementation of the AML policies and undermined effective inter-agency co-operation.⁴

4.1.2 Corruption

Preventing corruption starves money launderers of the proceeds of crime, and it disrupts the facilitating channels through which money launderers pay bribes in the course of laundering.⁵

Kenya has tolerated corruption within its law enforcement institutions and regulators, as indicated by the country's poor performance in Transparency International's Corruption Perceptions Index.⁶ Also, allegations of corruption have been levelled against the officials of the Central Bank⁷ and the judiciary.⁸ It is difficult to envisage having an effective FRC and AMLAB while the judiciary, regulators and the law enforcement agencies remain corrupt. Furthermore, this unedifying state of affairs frustrates potential whistle-blowers since not only do they face the risk of retaliation, but also when they report, law enforcement officers end up tipping off potential suspects.⁹ Without urgent measures to address widespread corruption, the AML efforts will remain largely ineffective.



³ Shiundu A & Obala R "Kenyan MPs cut Senate, SRC and Judiciary budgets to fund counties" 4 June 2014 *Standard Digital*, available at <https://www.standardmedia.co.ke/article/2000164515/kenyan-mps-cut-senate-src-and-judiciary-budgets-to-fund-counties> (accessed 20 October 2017).

⁴ Chatain PL *et al* (2009: 8).

⁵ Chaikin D & Sharman JC (2009: 28).

⁶ In the 2016 TI's Ranking, Kenya was number scored 26 out of 100. Where 100 indicates the absence of corruption. See <https://www.transparency.org/country/KEN> (accessed 20 October 2017).

⁷ "Ex-CBK governor's wife sought favours from Imperial Bank boss" 23 February 2016 *Business Daily*, available at <http://www.businessdailyafrica.com/corporate/Ex-CBK-governor-s-wife-sought-favours-from-Imperial-boss/539550-3088938-10h4jirz/index.html> (accessed 20 October 2017).

⁸ "Supreme Court Judge suspended over bribery claims" 23 February 2017 *Daily Maverick*, available at <https://www.dailymaverick.co.za/article/2016-02-23-supreme-court-judge-suspended-over-bribery-claims#.We4M6FuCzIU> (Accessed on 20 October 2017).

⁹ US Department of State Report (2017:117).

4.1.3 Inadequate Resources

Setting up effective AML institutions and implementation of AML measures is a resource-intensive undertaking. Pressing needs such as the high poverty rate and poor infrastructure have kept investment in AML measures at the periphery of Kenya's national budget. The FRC is understaffed and therefore it lacks the requisite manpower and expertise to ensure timely analysis of information. Also, it lacks the requisite technology since it has been relying on manual analysis of data as of 2016.¹⁰

4.1.4 Lack of Statistics

The lack of comprehensive statistics on ML makes it difficult to measure the extent of its prevalence.¹¹ As in most African countries, Kenya lacks statistics on ML cases and on the remedial action taken. In cases where these statistics are available, they are not disclosed to the general public. Therefore, these hinders assessment of the overall effectiveness and the cost-effectiveness of the AML measures. The last statistics available in the course of conducting research for this paper were the 2015 statistics.¹² Lack of statistics also may influence policy bodies such as parliament in making a low budgetary allocation to the FRC. Therefore, keeping up-to-date statistics will help the stakeholders in formulating AML policies. These statistics should be shared widely so that they give rise to a nationwide dialogue on AML measures.

¹⁰ US Department of State Report (2017: 117).

¹¹ HLP report (2015).

¹² At the time of writing, I sent emails to the FRC requesting the latest statistics, but there was no response.

4.1.5 Inadequate Safeguards to Guarantee Independence of the FRC

The increased mandate of the Cabinet Secretary in the oversight roles of the FRC threatens its independence. Cabinet Secretaries are PEPs who are generally considered to be more predisposed to ML.¹³ In Kenya, where senior government officials are the likely perpetrators of grand ML, this is a great challenge. For example, in 2006, the then Governor of the Central Bank was suspended by the Finance Minister after he recommended that Charter House Bank, which was implicated in a ML scandal, be closed.¹⁴ Whereas the Governor faced charges of abuse of office, the fact that no action was subsequently taken against the bank shows how dangerous it is to investigate ML cases involving senior government officials or their proxies.

4.2 Recommendations

4.2.1 Recruitment and Training of Staff

The FRC should recruit and train staff to ensure adequate and qualified personnel to run its operations. The ongoing recruitment process needs to be expedited to fill all vacant posts. Training should be conducted on a periodic basis since ML typologies keep changing. Once their staff is well trained, they can be called upon to train personnel in other institutions, thus helping in building capacity to combat ML.

4.2.2 Speed Up Efforts to Join the Egmont Group

The FRC should redouble its efforts to join the Egmont Group. As a member of the Egmont Group, it will benefit in accessing a wide pool of financial intelligence, expertise, trainers and it will profit from information sharing regarding contemporary ML/TF typologies.

¹³ Parkman T (2012: 105).

¹⁴ Kamau J "Ten-year-old puzzle that was Charterhouse Bank" 4 June 2016 *Daily Nation*, available at <http://www.nation.co.ke/news/Ten-year-old-puzzle-that-was-Charterhouse-Bank/1056-3233030-136xk9k/index.html> (accessed 20 October 2017).

4.2.3 Implementation of a Risk-Based Approach

Kenya should speed up its ongoing National Risk Assessment to allow for the implementation of a risk-based approach to ML. A risk-based approach will not only ensure the effectiveness of the AML measures, but also, the adoption of cost-effective measures by the FRC, reporting institutions and the regulatory bodies. This will help in addressing budget constraints and lack of effectiveness which presently prevent the FRC from realising its mandate. In addition, the FRC should publish a list of PEPs in order to facilitate the implementation of a risk-based approach.

4.2.4 Increasing Government Commitment to Fight Corruption and Money Laundering

The government should address the massive enforcement deficit for the AML and anti-corruption laws. The close nexus between ML and corruption testifies to the fact that a country riddled with corruption cannot successfully implement its AML laws. Therefore, the government should rejuvenate its commitment to fighting corruption and ML/TF. Also, Parliament needs to spearhead the fight against ML and corruption.

4.2.5 Maintain and Publicise up-to-Date Statistics

The FRC should keep and publicise up-to-date statistics on suspicious transaction reports and what the state has done about them. This information has to be shared with the general public on platforms such as the FRC's website since it is not confidential information. Information provided to the public will help in approximating the extent of ML in Kenya and will contribute to fostering a nationwide dialogue on ML. Importantly, the FRC should give feedback to reporting institutions where the information does not jeopardise investigations.

4.2.6 Reduce Powers of the Cabinet Secretary

There is need to reduce the powers of the Cabinet Secretary in various AML fronts. First, the FRC should submit its budget to Parliament directly and it should also table its reports before

Parliament. Second, persons appointed by the Cabinet Secretary to AMLAB should be seconded by their respective professional bodies. For example, where the seconded person is a lawyer, the Law Society of Kenya should be consulted. Without such safeguards, persons appointed arbitrarily tend to be at the bidding of the executive.

4.2.7 Regulation of the Legal Profession and Other Entities.

Finally, AMLAB and the Cabinet Secretary need to formulate policies to provide for reporting obligations for the legal profession. The legal profession is vulnerable to ML. Therefore, it too should be obligated to report suspicious transactions to the FRC. Furthermore, all business enterprises should file STRs where the value of purchases meets a set threshold.

Word Count: 17796



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