

ANTI- MONEY LAUNDERING LEGISLATION IN KENYA: INADEQUACIES

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SUPERVISEE DECLARATION

I, **MIRIAM WAMBUI GAITURI**, do hereby declare that this project is my original work and it has not been presented or submitted, in part or in whole for the award of a degree in any other university.

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DEDICATION AND ACKNOWLEDGEMENTS

I thank my supervisor Mr. Njaramba Gichuki for his unwavering support, supervision and guidance and for making the effort worthwhile.

I thank and dedicate this thesis to my spouse John Njenga and my children Wanjiku, Keru and Wanjiru; for their words of encouragement and for bearing with my absence when this work had to be done.

God bless you.

TABLE OF ABBREVIATIONS

AML	Anti-money Laundering
ESAAMLG	Eastern and Southern Africa anti-money Laundering Group
FATF	Financial Action Task Force
FIC	Financial Intelligence Centre
FINTRAC	Financial Transactions and Reports Analysis Centre
FRC	Financial Reporting Centre
KYC	Know Your Customer
MVNO	Mobile Virtual Network Operator
PEP	Politically Exposed Person
STR	Suspicious Transaction Reporting
TFML	Task Force on Money Laundering
UN	United Nations

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Consultative Document on Customer Due Diligence for Banks, 2001.
Cross-border Currency and Monetary Instruments Reporting Regulations of South Africa.

Criminal Code of South Africa.
Financial Intelligence Centre Act of South Africa.
International Cooperation in Criminal Matters Act of South Africa.
Prevention of Organised Crime Act of South Africa.
Proceeds of Crime (Money Laundering) and Terrorist Financing Act of South Africa.
Proceeds of Crime (Money Laundering) and Terrorist Financing Regulations of South Africa.
Proceeds of Crime (Money Laundering) and Terrorist Financing Suspicious Transaction Reporting Regulations of South Africa.
Protection of Constitutional Democracy against Terrorist and Related Activities Act of South Africa.
South African Reserve Bank Act, Act No. 90 of 1989.
The Wolfsberg Anti-Money Laundering Principles for Corresponding Banking Guidelines, 2002.
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CHAPTER ONE

INTRODUCTION

1.1 Overview

Money laundering is the process by which the proceeds of crime are transformed into ostensibly legitimate money or other assets. Criminals, who through their criminal activities dispose of large amounts of money, need to give this money a legitimate appearance by “cleaning it up”, hence the word “laundering”. Traditional money laundering entails transferring illegally obtained funds to conceal their origin and make them appear legal while a newer form of money laundering is the transfer of mostly legal funds for illegal purposes such as terrorism.¹ The laundering is done for two reasons: to prevent the dirty money from serving the crimes that generated it; and to ensure the money can be used without danger of detection and confiscation.² What, then follows, is an attempt to cover the tracks and erase the trail by injecting the dirty money back into the economy.

Globally, money laundering began to be recognized as a real issue and threat to national security and stable economies towards the late 1980s. For a long time, the attitude of most states, societies and criminal justice systems was that money does not stink (*pecunia non olet*) and much thought was not given to sources of money.³ This attitude implicitly allowed offenders to enjoy the fruits of their crimes without having to look over their shoulders more so because in money laundering there are no identifiable victims. Though there existed pieces of legislation that allowed for forfeiture or confiscation of the subject of crime, most of these laws did not give

¹ Elods Takats, ‘A Theory of Crying Wolf: The Economics of Money Laundering Enforcement’ (IMF Working Paper, 2007) available at: <http://www.imf.org/external/pubs/ft/wp/2007/wp0781.pdf>, accessed 26 May 2013.

² Guy Stessens, *Money Laundering: A New International Law Enforcement Model* (New York: Cambridge University Press, 2000) p. 5.

³ *Ibid.*

the State express authority to confiscate proceeds or profits of crime. Some countries such as Switzerland, Belgium and Netherlands were a step ahead and had in place laws providing for confiscation of proceeds of crime but the laws were still limited in terms of application and enforcement. In Belgium for instance, the law was only applicable to the offence of drug dealing while in Netherlands and Switzerland, the law was never quite enforced.⁴ This gap in the laws continued to exist and to be a stumbling block in addressing drug dealing and organized crime until England took the first bold initiative and enacted the Drug Trafficking Offences Act 1986. This law empowered courts to confiscate the proceeds of drug trafficking.

By the late 1980s, the anti-money laundering crusade had gained momentum following the 1988 UN Convention Against Illicit Traffic in Narcotic and Psychotropic Substances and the 1990 Council of Europe Convention on Laundering, Search, Seizure and Confiscation of the Proceeds from Crime.⁵ A huge step in the anti-money laundering fight was made in 1989 with the formation of a Financial Action Task Force at the Paris G7 Summit. The task force was mandated to “*assess the results of cooperation already undertaken in order to prevent the utilization of the banking system and financial institutions for the purpose of money laundering and to consider additional preventive efforts in this field, including the adaptation of the legal and regulatory systems as to enhance multilateral judicial assistance.*” The work of the Task Force culminated in dissemination of the Forty Financial Action Task Force (FATF) recommendations in 1990.⁶

⁴ Guy Stessens, *Money Laundering: A New International Law Enforcement Model* (New York: Cambridge University Press, 2000) p. 7

⁵ 1990 Council of Europe Convention on Laundering, Search, Seizure and Confiscation of the Proceeds from Crime available at: <http://conventions.coe.int/Treaty/en/Treaties/Html/141.htm>, accessed 26 May 2013.

⁶ For a detailed discussion of these recommendations see: <http://www.fatf-gafi.org/media/fatf/documents/recommendations/pdfs/FATF%20Recommendations%201990.pdf>, accessed 29 May 2013.

In 2002, the Wolfsberg Group, representing an association of eleven global banks which aim to develop financial services industry standards, anti-money laundering and counter terrorist financing policies, developed the Wolfsberg Anti-Money Laundering Principles.⁷

Due to the inherent transnational nature of money laundering, an international response was sought and encouraged. Today, money laundering has been extended to the offences of corruption, terrorism and arms trafficking as potential sources of illicit money. The argument has been that by taking away or confiscating proceeds of crime and by making it more difficult to launder the illicit money, the incentive to engage in organized crime is consequently taken away.⁸

With a long history of corruption, Kenya's money laundering problem has grown more significant as the country has become a major financial hub for East Africa. Kenya has come under increasing pressure on the international front to implement anti-money laundering laws in the face of rising crime posed by the drug traffickers, international terrorists and illicit arms traders operating in the country.⁹

In May, 2008, the Proceeds of Crime and Anti-Money Laundering Bill was introduced in Parliament, which extends reporting requirements to legal professionals.¹⁰ In 2009, the Proceeds of Crime and Anti-Money Laundering Act ("The Act")¹¹ was passed. The Act was aimed at establishing and providing for the offence of money laundering and to introduce measures for

⁷ The Wolfsberg Anti-Money Laundering Principles for Corresponding Banking Guidelines (2002) available at: [http://www.wolfsberg-principles.com/pdf/Wolfsberg_Correspondent_Banking_Guidelines_\(2002\).pdf](http://www.wolfsberg-principles.com/pdf/Wolfsberg_Correspondent_Banking_Guidelines_(2002).pdf), accessed 29 May 2013.

⁸ *Ibid.*

⁹ Banker's Academy Report (2012) available at: <http://www.bankersacademy.com/resources/free-tutorials/324-aml-kenya>, accessed 30 May 2013.

¹⁰ *Ibid.*

¹¹ The Proceeds of Crime and Anti-Money Laundering Act, 2009.

combating the offence, to provide for the identification, tracing, freezing, seizure and confiscation of the proceeds of crime.¹² Although prior to the promulgation of the Act there existed other pieces of legislation that attempted to address the money laundering menace, none was as comprehensive and direct as the Proceeds of Crime and Anti-Money Laundering Act. The other pieces of legislation included the Penal Code,¹³ the Criminal Procedure Code¹⁴ and the Narcotic Drugs and Psychotropic Substances (Control) Act.¹⁵

The Act provides the necessary details for reporting requirements, penalties and money laundering offences. It also establishes the Financial Reporting Centre which is charged with receiving reports of Suspicious Transaction Reports (STRs), tracing, freezing and seizing of criminal proceeds.¹⁶ In addition, in order to combat money laundering activities, Kenya has signed and ratified all of the United Nations Conventions on combating money laundering and the financing of terrorism.

With that background, this research will assess the practicability of using the anti-money laundering legislation in Kenya to curb money laundering and deter organized criminal activity.

1.2 Statement of the Problem

The practicability of using the Proceeds of Crime and Anti-Money Laundering Act to curb money laundering and deter organized criminal activities has in the last decade been questioned and heavily critiqued. It has been argued that most countries, especially those in the developing

¹² The Preamble states that it's an Act of Parliament to provide for the offence of money laundering and to introduce measures for combating the offence, to provide for the identification, tracing, freezing, seizure and confiscation of the proceeds of crime, and for connected purposes.

¹³ Penal Code, Cap 63, Laws of Kenya.

¹⁴ Criminal Procedure Code, Cap 75, Laws of Kenya.

¹⁵ Narcotics Drugs and Psychotropic Substances (Control) Act, 1994.

¹⁶ The Proceeds of Crime and Anti-Money Laundering Act, 2009, s 21, 23 and 24.

world, adopted the FATF recommendations blindly in a view to comply with and conform to what Western countries demanded without quite understanding and appreciating the rationale and agenda behind the requirements. They were also not well prepared or equipped to implement the requirements and for that reason, they have lagged behind in compliance leading to the perception that they are unwilling and uncooperative. In a statement released by FATF on 22nd February 2013, Ethiopia, Kenya, Nigeria and Tanzania were listed as high risk and non-cooperative jurisdictions.¹⁷

Despite the concerted efforts and the laws and regulations that have been put in place in Kenya to counter money laundering and by extension crime, there is little evidence of the twin vices being contained. This thesis will seek to interrogate whether the failure to contain money laundering and crimes such as terrorism is as a result of a legislative framework that is not practical and therefore ineffective in dealing with the problem.

The Proceeds of Crime and Anti-Money Laundering Act has inherent shortcomings which serve to defeat the critical purpose of its enactment. For instance, the Financial Reporting Centre which is an institution established under the Act, lacks the power to prosecute those it considers to have committed offences under the Act.¹⁸ The Financing Reporting Centre is required to report all suspicious money laundering activity to law enforcement agents. The agents are then mandated to carry out an independent investigation to verify the claim before taking appropriate measures. The bureaucracy created by this lengthy process hinders the achievement of the objectives of the Act. The Asset Recovery Agency, on the other hand, is required, through an application, to seek the authority of the High Court before it can seize or attach any proceeds of

¹⁷ FATF, 'Public Statement on Anti money Laundering Compliance' (22nd February, 2012) available at:<http://www.fatf-gafi.org>, accessed 25 March 2013.

¹⁸ The Proceeds of Crime and Anti-Money Laundering Act 2009, s 25(d).

crime. Due to the time needed to prepare the application to the High Court and the likelihood of a protracted hearing of the application, a suspected money launderer may get an opportunity to dispose of the proceeds of crime and erase the trail.

Globalization and technological advancements have brought about an era of e-commerce, internet and mobile banking, mobile and electronic money transfers all of which are instantaneous. With money launderers having become very sophisticated, they are able to circumvent all monitoring mechanisms with ease, making a mockery of the law. Lack of equally sophisticated institutional structures has made it difficult for the Financial Reporting Centre to fulfill its mandate of detecting the movement of illicit funds within the financial systems and financial institutions in Kenya perhaps due to the sheer volumes and speed of transacting.

1.3 Theoretical Framework

The dominant theory in the enactment and enforcement of anti-money laundering legislation is the deterrence theory.¹⁹ The concept of anti-money laundering and confiscation of proceeds of crime is therefore premised on the legal theory of deterrence. The deterrence theory argues that criminal acts are inhibited or deterred because of the punishment that is associated with crime. General deterrence occurs when someone who has not yet been punished refrains from committing a crime because of the punishment they may receive should they get caught. The deterrence theory was originally developed in the 18th century by the legal/moral philosophers Jeremy Bentham and Cesare Beccaria who conceived it in terms of the threat of formal legal punishment, sanctions or penalties applied by a state or some legal authority.²⁰ The confiscation of proceeds of crime envisaged in the Proceeds of Crime and Anti-Money Laundering Act aims

¹⁹ Robert Jervis, "Rational Deterrence: Theory and Evidence," *World Politics* 41 January, (1989), p. 183.

²⁰ J Mitchell Miller, *21st Century Criminology*, (Thousand Oaks, Calif.: Sage, 2009) (Volume 2), p. 236.

at deterring crime by instilling fear in criminals that they shall lose their illicit wealth to the state if arrested and prosecuted. Indeed, the argument has been that by taking away or confiscating proceeds of crime and by making it more difficult to launder the illicit money, the incentive to engage in organized crime is consequently taken away or deterred.²¹

Anti-money laundering laws and regulations are also premised on the secondary and complimentary theory of natural law as advanced by amongst others, Thomas Aquinas. Natural law theorists assert that, necessarily, law is a rational standard for conduct: it is a standard that agents have strong, even decisive, reasons to comply with and enforce.²² Money laundering is essentially viewed as immoral and unethical conduct because it involves an attempt at cleaning up and concealing the source of money. The State, acting as an agent of society and deeming the act of laundering money as highly immoral has enacted a law prohibiting this conduct.

1.4 Conceptual Framework

Money laundering is both a means of concealing the proceeds of crime and funding terrorism and other criminal activities. This presents the legislators and law enforcement agencies with diverse challenges that include establishing a link between criminal activities and the proceeds derived from such activities. Since Kenya's enforcement mechanisms and the institutional framework established under the Act are weak, the practice continues to thrive in the country.

Third world economies have not been aggressive in fighting money laundering perhaps because they don't quite understand it, are unable to keep up with its evolving nature or because they fear that aggressively dealing with it might cause serious negative effects on their state economies. In

²¹ J Mitchell Miller, *21st Century Criminology*, (Thousand Oaks, Calif.: Sage, 2009) (Volume 2), p. 236.

²² Martin P. Golding & William A. Edmundson (eds.), *The Blackwell Guide to the Philosophy of Law and Legal Theory*, (Blackwell Pub, 2005), p. 15.

Kenya for example, it is said that Chinese nationals are fuelling and driving the illegal poaching of elephant tusks. Despite this knowledge, we have not seen any serious or drastic action being taken against the said Chinese when caught. The government's reaction to this phenomenon has been lackluster and more of lip service than real action.

For most countries, money laundering and terrorism financing raise significant issues with regard to prevention, detection and prosecution. Sophisticated techniques used to launder money and finance terrorism add to the complexity of these issues. Such sophisticated techniques may involve many different types of financial institutions and other entities such as financial advisers, shell corporations and service providers as intermediaries, transfers to, through and from different countries; and the use of many different financial instruments and other kinds of value-storing assets. It is the process by which proceeds from a criminal activity are disguised to conceal their illicit origins.²³ Such sophisticated techniques used in money laundering have made it difficult for Kenya to detect and deal with money laundering. The situation is probably worsened by rampant corruption within the ranks of the law enforcement agencies in Kenya which has possibly contributed to failure to take decisive action with regard to investigation of cases of money laundering.

1.4.1 Definition of Money Laundering

Most countries, including Kenya, subscribe to the definition adopted by the United Nations Convention against Illicit Traffic in Narcotic Drugs and Psychotropic Substances.²⁴ The Convention defines money laundering as the conversion or transfer of property, knowing that

²³ World Bank Report on Money Laundering and Terrorist Financing: Definitions and Explanations available at: <http://www1.worldbank.org/finance/assets/images/01-chap01-f.qxd.pdf>, accessed 30th May, 2013.

²⁴ United Nations Convention Against Illicit Transfer in Narcotic Drugs and Psychotropic Substances 1988, Article 3(b).

such property is derived from any offence or offences or from an act of participation in such offence(s), for the purpose of concealing or disguising the illicit origin of the property or of assisting any person who is involved in the commission of such an offence or offences to evade the legal consequences of his actions.²⁵ It is also the concealment or disguise of the true nature, source, location, disposition, movement, rights with respect to, or ownership of property, knowing that such property is derived from an offence or offences or from an act of participation in such an offence or offences.²⁶ Since this definition is limiting, other international instruments have been passed to address this shortcoming. For instance, the United Nations Convention Against Transnational Organised Crime²⁷ requires all participant countries to apply that Convention's money laundering offences to 'the widest range of predicted offences.'²⁸

The Financial Action Task Force on Money Laundering defines money laundering as "*the processing of...criminal proceeds to disguise their illegal origin in order to legitimize the ill-gotten gains of crime.*" In its 40 recommendations, FATF incorporates the Vienna Convention's technical and legal definition of money laundering and recommends expanding the predictable offences of that definition to include all serious crimes.²⁹

²⁵ United Nations Convention Against Illicit Transfer in Narcotic Drugs and Psychotropic Substances 1988, Article 3(b).

²⁶ *Ibid.*

²⁷ See the 2000 United Nations Convention Against Transnational Organised Crime (Palermo Convention) and the Protocols available at: <http://www.unodc.org/documents/treaties/UNTOC/Publications/TOC%20Convention/TOCebook-e.pdf>, accessed 30th May 2013.

²⁸ *Ibid.*, Article 2(b).

²⁹ For a detailed discussion on the definition see the FATF website available at: <http://www.fatf-gafi.org/pages/faq/moneylaundering/>, accessed 30 May 2013.

1.4.2 The Processes of Money Laundering

Money laundering takes three stages as explained below:

1.4.2.1 Placement

The initial stage of the process involves placement of illegally derived funds into the financial system, usually through a financial institution. This can be accomplished by depositing cash into a bank account. Large amounts of cash are broken into smaller, less conspicuous amounts and deposited over time in different offices of a single financial institution or in multiple financial instruments, such as money orders or cheques and commingled with legitimate funds to divert suspicion. It can also be accomplished by the cash purchases of a security or a form of an insurance contract.

1.4.2.2 Layering

This occurs after the ill-gotten gains have entered the financial system, at which point the funds, security or insurance contract are converted or moved to other institutions further separating them from their criminal sources. Such funds could be used to purchase other securities, insurance contracts or other easily transferable investment instruments and then sold through yet another institution. The funds could also be transferred by any form of negotiable instrument such as cheque, money order or bearer bond or transferred electronically to other accounts in various jurisdictions. The launderer may also disguise the transfer as a payment for goods or services.

1.4.2.3 Integration

This process involves the integration of the funds into the legitimate economy. This is accomplished through the purchase of assets such as real estate, securities or other financial assets or luxury goods.

1.5 Literature Review

One of the earliest international anti-money laundering initiatives was undertaken in 1980 when Recommendation number R (80) (10) was adopted by the Committee of Ministers of the Council of Europe. The recommendation was entitled “Measures against the Transfer and Safeguarding of The Funds of Criminal Origin”.³⁰ With this adoption, the international impetus for the creation of anti-money laundering laws was born. The 1988 Basel Statement of Principles was the first international instrument to address money laundering specifically. The Basel Committee which comprised the authorities charged with banking supervision of 12 Western countries thought it necessary to address money laundering due to the potential image denting damage that a perception of associating with criminals can have on banking institutions. Notwithstanding its non-binding character, the statement was made indirectly binding on financial institutions in various countries thereby gaining acceptance as a valid enforceable instrument.³¹

The Basel statement was followed closely by the 1990 Forty Recommendations of the FATF. The various international initiatives have resulted in an international law enforcement regime

³⁰ Liliya Gelemerova, *The Anti-Money Laundering System in the Context of Globalisation: A Panopticon Built On Quicksand?* (Wolf Legal Publishers, 2011), p. 49.

³¹ Guy Stessens, *Money Laundering: A New International Law Enforcement Model* (Cambridge University Press, 2002), p. 16.

which is defined as a global arrangement among governments to cooperate against particular transnational crimes.³² The influence of an international anti-money laundering regime has been very instrumental in shaping domestic anti-money laundering laws of most nations. Fearing sanctions and blacklisting, most have complied.

Time has now come to assess whether the fuss that surrounded the speedy formulation and enactment of anti-money laundering laws and institutions around the globe has resulted in any meaningful and measurable gains as far as deterring organized crime is concerned. It has been argued that with the current state of globalization, the concept of anti-money laundering is a myth whose only real effect has been great inconvenience to users of financial systems worldwide.

Liliya Gelemerova in her book *“The Anti-money Laundering System in the Context of Globalisation: A Panopticon Built On Quicksand?”* observes that:

*“for over 20 years, since the introduction of the first anti money laundering laws, regulators have sought to curb the phenomenon of money laundering, but to little avail. Undeniably, crime for profit continues, as far as we can observe, and after two decades of fighting money laundering, crime-markets continue to flourish”.*³³

She goes ahead to pose, *“Why, despite enhanced global cooperation and globally coordinated efforts, do crime entrepreneurs continue to find ways to earn money and consequently launder these revenues and enjoy their wealth?”*³⁴

³² Ethan Nadelmann, *Cops Across Borders: The Internationalization of U.S Criminal Law Enforcement* (Pennsylvania State University Press, 1993), p. 22.

³³ Liliya Gelemerova, *The Anti-money Laundering System In The Context of Globalisation: A Panopticon Built On Quicksand?*(Wolf Legal Publishers, 2011) p. 5.

³⁴ *Ibid*, p.8

The phenomenon of money laundering appears difficult to assess as it depends on other crimes. It is a consequential crime that only exists in the context of another predicate crime.³⁵

1.5.1 Anti-money laundering vis-à-vis globalisation

Trade liberalisation, globalisation and the development of communication have increased the mobility of funds, including crime-money, making surveillance and tracking of these funds almost impossible.³⁶ As a result, anti-money laundering laws and regulations have not been effective in curbing money laundering or reducing the incidence of crime as was anticipated. For instance, due to technological advancement e-commerce now poses a great challenge to the anti-money laundering war. E-commerce has enabled people to conclude complex international financial transactions within a short period of time. This can facilitate money laundering as it is possible to put the proceeds of crime through these transactions and make the source of the money look legitimate within a very short period of time.³⁷

1.5.2 Anti-money laundering vis-à-vis encrypted cash transfers

Christopher D. Hoffman in his article *“Encrypted Digital Cash Transfers: Why Traditional Money Laundering Controls May Fail without Uniform Cryptography Regulations”* cites e-transactions in the form of digital payments as an unregulated avenue for money laundering.³⁸ Because digital payment systems do not require financial institutions as an intermediary, individuals making digital payments can disregard regulations that govern financial institutions. In addition, they can use cryptography to encode and decode messages with a numeric value

³⁵ Liliya Gelemerova, *The Anti-money Laundering System In The Context of Globalisation: A Panopticon Built On Quicksand?* (Wolf Legal Publishers, 2011) p. 62.

³⁶ *Ibid*, p.65

³⁷ *Ibid*, p.70

³⁸ Christopher D. Hoffman, ‘*Encrypted Digital Cash Transfers: Why Traditional Money Laundering Controls May Fail Without Uniform Cryptography Regulations*’ *Fordham International Law Journal* (1997) p.801

called the key and whose purpose is to secure electronic money transfers from theft and manipulation. A digital transfer encoded with cryptography will not reveal its origin or destination. Without regulatory oversight and with the protection of cryptography, criminals can easily adapt digital payment systems for money laundering purposes.³⁹

1.5.3 Anti-money laundering vis-à-vis online/electronic banking

Olga Mironenko in her book *“Antilaunching Money Policies in the E-Contracts Used by the Electronic Trading Platforms”* posits that terrorist and criminal groups have found a new refuge in cyber space, a refuge that makes their activities simpler as physical entities are transformed into virtual entities.⁴⁰ *“The internet allows the maintenance of a bank account in jurisdiction A by a person in jurisdiction B so as to buy goods in jurisdiction C with the currency of jurisdiction D for delivery anywhere in the world.”*⁴¹ Electronic payment systems provide benefits to consumers while enabling money launderers to ply their trade with greater ease and freedom. Going hand in hand with online banking is mobile banking and mobile money transfers. In Kenya for example, mobile money transfers are currently accounting for over KES 140 billion worth of transactions every month.⁴² With the application and granting of MVNO (Mobile Virtual Network Operator) licences to other market players other than Telecom network operators, there is every indication that cash transactions will soon be a thing of the past as they will be replaced by paperless card and mobile money transactions. It will therefore soon be

³⁹ Christopher D. Hoffman, ‘*Encrypted Digital Cash Transfers: Why Traditional Money Laundering Controls May Fail Without Uniform Cryptography Regulations*’ Fordham International Law Journal (1997) 801.

⁴⁰ Olga Mironenko, *Antilaunching Money Policies In The E-Contracts Used By The Electronic Trading Platforms* (University of Oslo, 2011) 1.

⁴¹ Alldridge Peter, *Money Laundering Law Forfeiture, Confiscation, Civil Recovery, Criminal Laundering and Taxation of the Proceeds of Crime* (Oxford – Portland Oregon: Hart Publishing 2003, 1st edition), p. 16.

⁴² Kenya’s M-Pesa transactions rise despite high charges available at: <http://www.theeastafrican.co.ke/news/Kenya-MPesa-transactions-rise-despite-high-charges/-/2558/1728544/-/2urcv1z/-/index.html>, accessed 10th June 2014.

virtually impossible to trace the source and ultimate destination of funds because financial institutions and systems can be bypassed altogether.

1.5.4 Anti-money laundering vis-à-vis Hawala system

The Hawala system has also been identified as playing a key role in laundering of illicit money. Hawala may be defined as transferring money without actually moving it and is an alternative or parallel remittance system. It exists and operates outside of, or parallel to 'traditional' banking or financial channels. It was developed in India, before the introduction of western banking practices, and is currently a major remittance system used around the world.⁴³ The Hawala system is distinguished from other remittance channels by trust and family affiliation factors and because it is paperless and lacking in trail, it is quite appealing to those wishing to launder money.⁴⁴

1.5.5 Limited nature and ambiguity of anti-money laundering legislation

The restrictive and limited nature of anti-money laundering legislation has partly been blamed for its ineffectiveness. Currently, money laundering legislation is limited to some predicate, specified offences and this limitation is likely to hamper the efficacy of law enforcement agencies and subject the process to technical legal difficulties which may impede the fight against money laundering.⁴⁵ It has been argued that in order for the law to have the intended impact and effect, the scope of anti-money laundering should be extended and the laws revised to cover any kind of money laundering. This argument has been advanced by Guy Stessens in his

⁴³ Patrick M. Jost and Harjit Singh Sandhu, *The Hawala Alternative Remittance System and its Role in Money Laundering* (2009) p.1.

⁴⁴ *Ibid.*, p.2

⁴⁵ Guy Stessens, *Money Laundering: A New International Law Enforcement Model* (Cambridge University Press, 2002) p. 14

article “*Money Laundering: A New International Law Enforcement Model*”. He posits that the major challenge arises because the proceeds of various activities of organized crime groups are mixed and intermingled with the result that the proceeds from drug trafficking or terrorist financing cannot be identified or calculated with accuracy.⁴⁶ Likewise, confiscation of proceeds of crime should include any kind of crime.

The language of anti-money laundering policies contains much vagueness. The ambiguity of definitions leads to arbitrary results and uncertainties in the application of penal law. This is very problematic in the context of globalisation when law enforcement and regulatory efforts should be standardised globally to fight crime that is claimed to be globally spread.⁴⁷ Standardization, on the other hand, requires precise and definite conceptual definitions that may require answering the following questions: How far should we go with the criminalisation of the various financial aspects of a criminal’s conduct? Should any use of crime-money be considered money laundering? Should use of legally obtained money to commit a crime such as is done by terrorists fall within money laundering offences?

Going by the results of research conducted by various scholars and experts on the subject of anti-money laundering, it would appear that the legal and regulatory frameworks and institutions established globally to fight this menace have not been successful in eliminating both money laundering and the specified predicate crimes. Despite law enforcement’s broad powers, estimates provided by national and international authorities suggest ever increasing volumes of money laundering and one may wonder why.⁴⁸

⁴⁶ Guy Stessens, *Money Laundering: A New International Law Enforcement Model* (Cambridge University Press, 2002) p. 14.

⁴⁷ *Ibid*, p.16

⁴⁸ *Ibid*, p.16

As observed by Liliya Gelemerova, it appears like *“the fight against money laundering is based on a rhetoric political superstructure with dire consequences in the compliance orbit but little or no evidence of success. The entire business, globally, is called upon to conduct due diligence and gather information to ensure that profit-oriented crime does not pay, but thus far little has been done by the authorities to ease and streamline the process of information gathering or to design some performance measurement procedure.”*⁴⁹ According to her, it appears that the fight against money laundering has become a variable of political choices and subject to double standards rather than a targeted effort to curb crime for profit. Though the FATF has sought to achieve some level of consistency in the anti-money laundering approach across the world, it remains a question whether all specific measures it has recommended have worked besides being religiously adopted.⁵⁰

In Kenya for example, the Proceeds of Crime and Anti-money Laundering Act has been in force for close to 3 years and not a single person has been prosecuted for money laundering. Though it is alleged that proceeds of piracy, poaching, drug trafficking and other crimes have been invested in the real estate industry in Kenya, the concerned law enforcement institutions appear unable to investigate the claims comprehensively.

As Mona Doshi aptly puts it, *“...although the Act has been in force since 31st December, 2009 the administrative structure that needed to be established pursuant to the Act is not yet all in place. Very recently draft regulations have been made pursuant to the Act and have been circulated to stakeholders for review and feedback. The failure to implement the Act has resulted*

⁴⁹ Liliya Gelemerova, *The Anti-Money Laundering System in the Context of Globalisation: A Panopticon Built On Quicksand?* (Wolf Legal Publishers, 2011) p. 249.

⁵⁰ *Ibid*, p.257

in the Act being ineffective to deal with the purposes for which it was enacted. Of late there is international pressure on the Government to act quickly towards implementation of the Act.”⁵¹

To deal with money laundering comprehensively, a change in strategy is necessary and it may require an overhaul of the existing law. As aptly put by R. Jones and Prof K. Keasey in their article “*Money Laundering and the Internet: A Challenge for Regulation,*” “*recent developments will require some updating and revision of the regulations, but the main problem, both now and in the future, appears to lie in implementing and enforcing the regulations and in being able to gather sufficient evidence to gain a criminal conviction.*”⁵²

Applying the anti-money laundering strategy, as it stands now, as a general tool to fight crime is of little help because each type of criminal offence may require different complementing measures to reduce its prevalence.⁵³

Not much has been written in Kenya on the subject of money laundering and terrorism financing perhaps because both subjects are relatively new phenomenon. This research and the resultant thesis will add value into the anti-money laundering space by providing additional literature that can be referred to in future.

⁵¹ Mona K Doshi, ‘*Anti-money laundering laws Kenya country Guide for Thomson Reuters*’ (2012 Chambers Global) p. 3.

⁵² R. Jones and Prof K. Keasey, ‘*Money Laundering and the Internet: A Challenge for Regulation*’ (1999) p. 4.

⁵³ Liliya Gelemerova, *The Anti-Money Laundering System in the Context of Globalisation: A Panopticon Built On Quicksand?* (Wolf Legal Publishers, 2011) p. 254.

1.6 Objectives of the Research

1.6.1 Main Objective

The main objective of this research is to assess the practicability of enforcing the Proceeds of Crime and Anti-money Laundering Act in Kenya to curb money laundering and organized crime.

1.6.2 Specific Objectives

- a) To assess the practicability of enforcing the Proceeds of Crime and Anti-Money Laundering Act in Kenya.
- b) To assess the ascertainable capacity of the institutions created by anti-money laundering legislation in Kenya to carry out their mandate.
- c) To assess the extent to which Kenya can learn from other jurisdictions on various aspects of dealing with money laundering and organized crime.
- d) To recommend legal reform on money laundering in Kenya to better deal with the problem.

1.7 Research Hypothesis

The hypothesis of this research is that the Proceeds of Crime and Anti -Money Laundering Act has not been effective at curbing money laundering and organized crime in Kenya and there is need for law reform in this area.

The study is premised on the following specific assumptions:

- a) The legal framework established under the Proceeds of Crime and Anti-Money Laundering Act is not sufficient to curb the money laundering problem in Kenya.
- b) The institutional framework created under the Act is too weak to ensure its full compliance of its provisions

- c) The enforcement mechanism established under the Act is too weak.

1.8 Research Questions

This study is guided by the following questions:

- a) To what extent is the Proceeds of Crime and Anti-money Laundering Act appropriate for curbing money laundering and organized crime in Kenya?
- b) Is the institutional framework established under the Act sufficient to ensure enforcement of the provisions of the Proceeds of Crime and Anti-money Laundering Act and to deal with money laundering in Kenya?
- c) Is Kenya's legal, institutional and administrative framework as provided under the Act in conformity with international best practices in dealing with money laundering?
- d) Has the Proceeds of Crime and Anti-money Laundering Act achieved its core objective of introducing measures for combating the offence of money laundering and providing for the identification, tracing, freezing, seizure and confiscation of the proceeds of crime?

1.9 Research Methodology

The primary source of material for this research paper is existing literature on money laundering. The research is enriched through the use and review of local statutes, subsidiary legislation, law reports, government policy papers, textbooks, local and international journals, articles, research papers, case law, newspapers and magazines, internet sources and other materials relevant to this study.

The University of Nairobi Law Library, Jomo Kenyatta Memorial Library, International Commission of Jurists (Kenya Chapter) Library and the Financial Reporting Centre Library are the main places the research has been undertaken.

1.10 Limitations of the Study

This research paper does not focus on the other pieces of legislation that were previously employed in Kenya to deal with proceeds of crime. The main focus of this study is to demonstrate that the Proceeds of Crime and Anti-money Laundering Act has gaps and weak enforcement mechanisms to curb the money laundering practices in Kenya. However, the research paper appreciates that anti-money laundering law in Kenya is also contained in other pieces of legislation applicable to other specific crimes. In the same breathe, there are many international instruments touching on anti-money laundering. All these do not fall under the purview of this study although some of them are mentioned for their value to specific aspects of this research paper. In addition, this research is limited to the qualitative approach of data collection. Due to time constraints, quantitative approach of data collection has not been adopted.

1.11 Summary of chapters

This study is broken down into five chapters.

Chapter One provides the context in which the study is set, the focus and objectives of the study, its significance and other preliminary matters including the hypothesis, research questions and the literature review.

Chapter Two seeks to critically examine the legal provisions Proceeds of Crime and Anti-money Laundering Act and the institutions established therein. A critique of the Act is provided

and the weaknesses exposed for consideration. I have opted to discuss the Kenyan context before the global one to enable my readers gain a domestic and local understanding of the anti-money laundering legal framework before venturing into the global, more complex and wider realm of anti-money laundering and terrorism financing.

Chapter Three highlights international instruments and institutions that deal with money laundering with a view to expounding on the origin as well as the legal and quasi legal foundation and basis for the anti-money laundering concept in Kenya and around the globe.

Chapter Four provides a comparative analysis of the law in Kenya vis-a-vis similar laws in the Republic of South Africa and Canada. The two jurisdictions have been selected due to the advanced nature of their anti-money laundering laws. Canada first promulgated on the issue of money laundering in 1991 and has had the benefit of continuously amending and improving its laws to serve the needs of its populace and the state at large. South Africa on the other hand first promulgated on the money laundering issue in 1998, a decade before Kenya enacted its law. To this extent, the two jurisdictions can provide good insights on the anti-money laundering, the corresponding legislation and institutional frameworks necessary to fight the vice. .

Chapter Five proposes recommendations on enhancement of the Proceeds of Crime and Anti-money Laundering Act to make its operation and enforceability more viable.

CHAPTER TWO

A CRITICAL ANALYSIS OF THE SHORTCOMINGS OF THE PROCEEDS OF CRIME AND ANTI-MONEY LAUNDERING ACT

2.1 Overview

This chapter is divided into two main parts. The first part discusses the background or the historical perspective leading to the enactment of the Proceeds of Crime and Anti-Money Laundering Act (“the Act”). The second part is dedicated to examining the various provisions of the Act.

2.2 Background to the enactment of the Act

Money laundering in Kenya follows a number of predicate offences. These offences include, *inter alia*, political corruption, human and drug trafficking, wildlife poaching, smuggling of counterfeit goods and import tax evasion. It occurs through a range of vehicles including real estate investments, charitable trusts and foundations, casinos, bureau de change establishments, election finance and cash remittance entities such as Hawala. The absence of effective anti-money laundering controls has made Kenya vulnerable to terrorism financing. This is of major concern given the continuing presence and activity of terrorist cells in Kenya. Reporting by the United Nations Monitoring Group on Somalia and Eritrea makes clear, for example, that terrorism financing has occurred in recent years through a number of avenues in Kenya, including informal money transfers, cash couriers and exploitation of charities and not for profit organizations.⁵⁴

⁵⁴ Tu'emay Aregawi Desta and James Cockayne, eds., *'ISSP-CGCC Joint Baseline Study on Anti-Money Laundering and Countering the Financing of Terrorism in the IGAD Subregion, New York and Addis Ababa'* May 2012 available at: http://www.google.com/#output=search&client=psy-ab&q=baseline+study+on+the+financing+of+anti+money+lauding+in+the+igad+region&oq=baseline+study+on+the+financing+of+antimoney+lauding+in+the+igad+region&gs_l=hp.3...50.33028.0.33685.97.83.3.0.0.7.1460.37207.4j3-2j53j10j4j3.76.0....0.0..1c.1.20.psy-

According to the United States Department on Money Laundering, Kenya is developing into a major money laundering country.⁵⁵ Kenya's use as a transit point for international drug traffickers continues to increase and the laundering of funds related to Somali piracy is a substantial problem. Reportedly, Kenya's financial system may be laundering over \$ 100 million each year, including an undetermined amount of narcotics' proceeds and Somali piracy-related funds. There is a black market for smuggled goods in Kenya, which serves as the major transit country for Uganda, Tanzania, Rwanda, Burundi, Northern Democratic Republic of Congo and Southern Sudan.⁵⁶ Goods marked for transit to these northern corridor countries avoid Kenyan customs duties but authorities acknowledge they are often sold in Kenya. Many entities in Kenya are involved in exporting and importing goods, including not for profit entities. As a regional financial and trade center for Eastern, Central and Southern Africa, Kenya's economy has large formal and informal sectors. Although banks and other formal channels execute funds transfers, there are also thriving, unregulated informal networks of *hawala* and other alternative remittance systems using cash-based, unreported transfers that the Government of Kenya cannot track. Immigrants and in particular the large Somali refugee population primarily use *hawala* to send and receive remittances internationally.⁵⁷

In 2010, a staggering \$ 2.1 billion found its way into the Kenyan economy without the government being able to explain its source.⁵⁸ Debate on the extent to which this amount might

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⁵⁵ United States Department of Money Laundering and Financial Crimes, 'International Narcotics Control Strategy Report' March 2010 available at: <http://www.state.gov/documents/organization/137429.pdf>, accessed 22 July 2013.

⁵⁶ *Ibid.*

⁵⁷ *Ibid.*

⁵⁸ Jaindi Kiseru, 'Mystery of Shs 164 billion Smuggled into Kenya' *Daily Nation* (21st May, 2010) available at: <http://allafrica.com/stories/201005200888.html>, accessed 29th July 2013.

consist of laundered ransom money from piracy, terrorism, wildlife poaching, drug trafficking or other proceeds of crime remains unresolved.⁵⁹

Major financial scandals have been revealed but there has not been any successful prosecution. The 2004 Kroll Report, for instance, suggests that relatives and associates of former President Daniel Moi siphoned off more than \$ 1.8 billion of government money into banks and asset acquisitions abroad.⁶⁰ Charterhouse Bank which was owned and operated by prominent personalities and politicians and which was described as a “money-laundering machine”⁶¹ had its accounts frozen amidst allegations of massive tax evasion, fraud and money laundering, including massive transfers into accounts abroad. The prominent businessmen and politicians involved in the Charterhouse Bank and other scandals appear to enjoy impunity and have not been called to account for fleecing and laundering billions of public funds and for undermining Kenya’s economy and international integrity.⁶² Successive governments seem to have ignored these allegations.

Anti-Money Laundering (“AML”) initiatives in Kenya have largely been driven by the civil service, with some complementary work being done by the financial sector. Legislative reforms have moved slowly, apparently under pressure from external players such as FATF. For the last decade, the Kenyan National Task Force on Money Laundering (TFML) has coordinated the country’s official AML efforts. Its membership is drawn from various government departments and regulatory agencies.

⁵⁹ *Ibid.*

⁶⁰ Xan Rice, ‘The Looting of Kenya’ *The Guardian* (London, 31st August 2007) available at: www.guardian.co.uk/world/2007/aug/31/kenya.topstories3. For a copy of the 110-page report, published on 27th April, 2004, see The Basel Institute on Governance, International Institute for Asset Recovery, *Kroll Report* available at: www.assetrecovery.org/kc/node/0086b5a2-c6c8-11dd-b3f1fd61180437d9.0.jsessionid=63546BFC111DD623D4FEC137B1C20A7, accessed 29th July 2013.

⁶¹ Star Team, ‘Kenya: State Deep in Charterhouse Conspiracy’ *Nairobi Star* (Nairobi, 1st October 2010) available at: <http://allafrica.com/stories/201010010131.html>, accessed 29th July 2013.

⁶² African Centre for Open Governance (Africog), ‘Smoldering Evidence-The Charterhouse Scandal’ (2011) available at: www.africog.org/?q=reports/smoldering_evidence, accessed 29th July 2013.

In 2001, money laundering was criminalized to include only proceeds of drug trafficking. This was done through the Narcotic Drugs and Psychotropic Substances (Control) Act.⁶³ Subsequently, the Central Bank of Kenya issued prudential regulations on money laundering to the financial sector. They took effect on 1st October, 2000.⁶⁴ These regulations are founded on the Know Your Customer (KYC) policy as proposed by the 1988 Basel Customer Due Diligence.⁶⁵ The Guidelines require all banks to follow the basic principles of customer identification, reporting to the Central Bank all suspicious transactions, keeping of records, enhanced internal controls and training of staff on money laundering prevention and detection.⁶⁶

It is against this background that on 10th December, 2009, Kenya's legislature enacted AML legislation of general application for the first time.⁶⁷ This Act was originally introduced into Parliament in mid-2004. Prior to this, the only law that criminalized money laundering was only applicable to proceeds of drug trafficking.

⁶³ Narcotic Drugs and Psychotropic Substances (Control) Act.

⁶⁴ Central Bank of Kenya Prudential Guidelines of Crime and Money Laundering (Prevention) available at: http://www.imolin.org/doc/amlid/Kenya_Prudential%20Guidelines%20for%20Institutions%202006_Guideline%20on%20Proceeds%20of%20Crime%20and%20Money%20Laundering%20CBK_PG_08.pdf, accessed 23rd July 2013.

⁶⁵ Basel Customer Due Diligence Regulations <<http://www.bis.org/publ/bcbs85annex.htm>> accessed 29 July 2013

⁶⁶ Consultative Document on Customer Due Diligence for Banks (2001) available at: <http://www.bis.org/publ/bcbs77.pdf>, accessed 23rd July 2013. The report succinctly stipulates several basic principles, encouraging banks to identify customers, refuse suspicious transactions and cooperate with law enforcement agencies. In addition, as part of a sound internal control environment, banks should have adequate policies, practices and procedures in place that promote high ethical and professional standards in the financial sector and prevent the bank from being used, intentionally or unintentionally, by criminal elements. In addition, supervisors are encouraged to adopt the relevant recommendations of the FTF, relating to customer identification and record-keeping, reporting suspicious transactions and measures to deal with countries with insufficient or no anti-money laundering measures...

⁶⁷ The Proceeds of Crime and Anti-Money Laundering Act, 2009.

2.3 Money Laundering and Related Offences

The Proceeds of Crime and Anti-Money Laundering Act provides the Kenya Government with relatively new and substantial powers in the fight against money laundering. The principal areas of focus in the Act are the provision, for the first time in the country's legislative history, of the offence of money laundering and the introduction of measures to combat the offence. The Act also provides for the identification, tracing, freezing, seizure and confiscation of the proceeds of crime.⁶⁸

The definition of money laundering under the Act is wide and includes entering into any agreement or engaging in any arrangement or transaction with anyone in connection with property which one knows or ought to reasonably have known that it is or forms part of the proceeds of crime regardless of whether such agreement, arrangement or transaction is legally enforceable or not. Such an arrangement should also have the effect of concealing or disguising the nature or ownership of the property or assisting a person who has committed an offence to avoid prosecution or concealing any proceeds of crime.⁶⁹ The definition also covers acquisition, use or possession of property which at the time of acquisition, use or possession one knows or ought to reasonably have known that it is or forms part of the proceeds of a crime committed by another person.⁷⁰ It is also an offence for a person who knowingly transports, transmits, transfers or receives or attempts to transport, transmit, transfer or receive a monetary instrument or anything of value to another person, with intent to commit an offence.⁷¹

This definition is similar to the one adopted by the Central Bank of Kenya AML Guidelines.

Money laundering is defined as the act of a person who engages directly or indirectly, in a

⁶⁸The Proceeds of Crime and Anti-Money Laundering Act, 2009.

⁶⁹ *Ibid*, s 3

⁷⁰ *Ibid*, s 4

⁷¹ *Ibid*, s 7

transaction that involves proceeds of any unlawful activity or acquires, receives, possesses, disguises, transfers, converts, exchanges, carries, disposes, uses, removes from or brings into Kenya proceeds of any unlawful activity or conceals, disguises or impedes the establishment of the true nature, origin, location, movement, disposition, title of, rights with respect to or ownership of, proceeds of any unlawful activity whereas may be inferred from objective factual circumstances, the person knows or has reason to believe, that the property is the proceed of any unlawful activity or in respect of the conduct of a natural person, the person without reasonable excuse fails to take reasonable steps to ascertain whether or not the property is the proceed of any unlawful activity.⁷² Although the definition of money laundering under the Act is laudable for being broad, it falls short for failure to define terrorism financing which is a key concern for Kenya presently. Whereas the Act ably envisages sources of money that are criminal in nature, it fails to take into account that legitimately acquired money can, and is often used, to finance illegitimate and criminal activities such as terrorism.

2.3.1 Failure to report suspicion regarding proceeds of crime

The Act provides that a person who wilfully fails to comply with an obligation contemplated in section 44(2) commits an offence. The Act requires a reporting institution⁷³ to monitor on an ongoing basis all complex, unusual, suspiciously large or other transaction as may be specified in the regulations, whether completed or not. The reporting institution shall pay attention to all unusual patterns of transactions, to insignificant but periodic patterns of transactions that have no

⁷² The Central Bank of Kenya Guidelines available at: <http://www.centralbank.go.ke/index.php/news/233-aml-regulations-2012>, accessed 29th July, 2013.

⁷³ A reporting institution means a financial institution and designated non-financial business and profession.

apparent economic or lawful purpose as stipulated in the regulations.⁷⁴ The reporting institution shall upon suspicion that any of the transactions or activities described or any other transaction or activity could constitute or be related to money laundering or the proceeds of crime, report to the Financial Reporting Centre.⁷⁵ The reporting should be in the prescribed form and should be done immediately and in any event, within seven days of the date the transaction or activity that is considered to be suspicious occurred.⁷⁶ Firstly, the regulations mentioned in the Act have not yet been issued and this makes the implementation of the provisions of this Act very challenging due to the lack of legislative guidelines. Secondly, monitoring of transactions by the reporting institutions can be very challenging due to the sheer volumes and frequencies involved. Take for example Safaricom which has in excess of 20 million registered M-Pesa users. If all these users performed even a single transaction daily, the reporting institution, in this case Safaricom, would encounter difficult challenges trying to monitor and perhaps investigate the purpose and legitimacy behind all those transactions not to mention the cost implications that would be associated with such an exercise on a daily basis. Thirdly, besides detecting and reporting, the Act does not prescribe any measures that might help preempt and forestall money laundering that is in progress. In the seven days that the Act has allowed for a reporting institution to report a suspicious transaction, the money would have moved through a complex and intricate web of transactions that it would become difficult, even impossible to trace. Any action taken thereafter would be reactive as opposed to a more helpful proactive action. A fourth shortcoming of this provision is that reporting institutions are required to report based on mere speculation and suspicion as opposed to reporting information that has been investigated and confirmed to be valid. Whereas some transactions might appear to meet the threshold of money laundering on the

⁷⁴ The Proceeds of Crime and Anti-Money laundering Act 2009, s 44(1).

⁷⁵ This is the Financial Reporting Centre as established under Section 21 of the Act.

⁷⁶ The Proceeds of Crime and Anti-Money laundering Act 2009, s 44(2).

face of it due to frequency or amount, a scrutiny of the background, source, destination and purpose of transaction might reveal that the said transactions are indeed legitimate and lawful. Therefore, unless a preliminary investigation is conducted to establish that a transaction is indeed a money laundering activity, there is the risk that reporting institutions, in their quest to comply with the law, will send many false positive reports to the Financial Reporting Centre and overwhelm it with unnecessary reports.

2.3.2 Tipping off

The Act provides that it is an offence if a person knows or ought reasonably to have known that a report under section 44 of the Act⁷⁷ is being prepared or has been or is about to be sent to the Financial Reporting Centre and discloses to another person information or other matters which are likely to prejudice any investigation of an offence or possible offence of money laundering. If this provision is contravened, in the case of a natural person, the penalty is imprisonment for a term not exceeding seven years, or a fine not exceeding two million, five hundred thousand shillings, or to both and in the case of a body corporate, to a fine not exceeding ten million shillings or the amount of the value of the property involved in the offence, whichever is the higher.⁷⁸ This provision prohibits the disclosure of information or other matters that might prejudice any investigation of an offence or possible offence of money laundering. This provision is very difficult, almost impossible to enforce for the following reasons. Firstly, unless done in writing, it is virtually impossible to prove disclosure. Secondly, even if disclosure were

⁷⁷ Section 44 generally provides a raft of obligations to a reporting institution. Specifically, section 44(1) provides that a reporting institution shall monitor on an ongoing basis all complex, unusual, suspicious, large or other transaction as may be specified in the regulations, whether completed or not, and shall pay attention to all unusual patterns of transactions, to insignificant but periodic patterns of transactions that have no apparent economic or lawful purpose as stipulated in the regulations. Upon suspicion that any of the transactions or activities described in subsection (1) or any other transaction or activity could constitute or be related to money laundering or the proceeds of crime, a reporting institution shall report the suspicious or unusual transaction or activity to the Centre in the prescribed form immediately and, in any event, within seven days.

⁷⁸The Proceeds of Crime and Anti-Money Laundering Act 2009,s 16(2).

to be proved, it would still be very difficult to prove that disclosure was done with the intention of obstructing an investigation and therefore ultimately to defeat justice. A bank teller who comes across a suspicious transaction might want to contact the customer to perform a preliminary assessment of the transaction by subjecting the customer to some questions. This action might inadvertently tip off the customer. Would that be viewed as disclosure for purposes of this Act? The same teller might decide not to call the customer but instead discuss the matter with his supervisor not knowing the close friendship or relationship that exists between his supervisor and the customer. Would this be viewed as disclosure for purposes of this Act? The Act, through this provision failed to appreciate the various scenarios, circumstances and situations that can play out the moment a transaction is suspected to be a money laundering activity. Although well-meaning and intentioned, the practical challenges of enforcing this provision are glaring.

2.3.3 Misrepresentation

It is an offence for a person to make a false, fictitious or fraudulent statement or representation or make or provide any false document, knowing the same to contain any false, fictitious or fraudulent statement or entry, to a reporting institution or to a supervisory body or to the Financial Reporting Centre.⁷⁹ A person who is guilty of the offence of misrepresentation is liable to, in the case of a natural person, imprisonment for a term not exceeding 2 years or a fine not exceeding KES 1 Million or both and in the case of a body corporate, a fine not exceeding KES 5 Million or the amount of the value of the property involved in the offence, whichever is the higher.⁸⁰ This provision creates many challenges for reporting institutions. It is a

⁷⁹ *Ibid*, s 9

⁸⁰ *Ibid*, s 16(4)

requirement in many banks today to state on the source documentation the purpose for which one is effecting a standing order, an EFT (Electronic Funds Transfer) or an RTGS (Real Time Gross Settlement). Despite collecting this information, a bank is not able to immediately confirm the accuracy of the information provided by a customer and it is unlikely that a money launderer will declare the true purpose of the transaction. There is no legal requirement on the part of reporting institutions to confirm the truthfulness of the said information. The offence can only kick in once an investigation is conducted and the information is found to be false. The Act is, however, silent on whose responsibility it is to carry out the investigation. The Act also envisages a situation whereby a reporting institution would be passing over false information to the Financial Reporting Centre. According to the Act, such an institution would be committing an offence. However, proving such an offence would be a tall order. This is because the reporting institution would simply be transmitting what it has collected from its customers and the primary responsibility should remain with the customer.

The third and perhaps the most glaring shortcoming of this provision is to be found in the definition of the offence. Misrepresentation is a key element and feature of all fraudulent activity. The definition given under this provision is that of general fraud and is not unique to money laundering in any way whatsoever. Fraud is defined as the deliberate falsification, misrepresentation or concealment of facts to derive personal gain. A fourth shortcoming of this provision is the very lenient punishment prescribed for offenders. For a wildlife poacher or a drug trafficker, a fine of KES 1 million is too low to deter the offender.

2.3.4 Malicious Reporting

In order to guard against reporting false or misleading information, the Act makes it an offence for any person who wilfully gives information to the Financial Reporting Centre or an authorized

officer knowing such information to be false. Such a person is subject to be prosecuted and may be convicted of the offence of malicious reporting.⁸¹ The penalty for the offence of malicious reporting is the same as that of the offence of misrepresentation. There is a thin line between malicious reporting and reporting of suspicions that may turn out to be inaccurate or not factual. By prescribing prosecution for malicious reporting, whose definition is not provided, persons who may have a suspicion to report may be discouraged from reporting for fear of the report being labelled malicious.

2.3.5 Failure to Comply with the Provisions of the Act

A reporting institution commits an offence if it fails to comply with any of the requirements of sections 44,⁸² 45⁸³ and 46⁸⁴ of the Act. Section 44 of the Act requires reporting institutions to actively monitor and report money laundering activity. As earlier highlighted active continuous monitoring of transactions is not only complex but can be quite tedious and expensive. Due to the volumes involved, reporting institutions would probably have to adjust the reporting thresholds upwards to avoid flagging too many false positive transactions. By so doing, the institutions are likely to miss out on low value, less frequent transactions that might be of a money laundering nature. Balancing off the compliance requirements with the practicability of 100% monitoring of transactions is quite tricky. Since the Act is quiet on the parameters and

⁸¹ *Ibid*, s 11

⁸² Section 44 of the Act confers an obligation to a reporting institution to monitor and report suspected money laundering activity.

⁸³ Section 45(1) of the Act states that a reporting institution shall take reasonable measures to satisfy itself as to the true identity of any applicant seeking to enter into a business relationship with it or to carry out a transaction or series of transactions with it, by requiring the applicant to produce an official record reasonably capable of establishing the true identity of the applicant. An individual is expected to produce either a birth certificate; a national identity card; a driver's licence; a passport; or any other official means of identification as may be prescribed. In the case of a body corporate, it is expected to furnish evidence of registration or incorporation; the Act establishing the body corporate; a corporate resolution authorizing a person to act on behalf of the body corporate together with a copy of the latest annual return submitted in respect of the body corporate in accordance with the law under which it is established; and/or any other item as may be prescribe. In the case of a government department, a letter from the accounting officer should be provided.

⁸⁴ A reporting institution has an obligation to establish and maintain customer records.

levels of monitoring expected of a reporting institution i.e. daily, weekly, monthly or sample monitoring, profiled customer monitoring or 100% monitoring, reporting institutions devise their own rules and do what they can according to the specific circumstances. It would therefore be very difficult to sustain a charge against a reporting institution for violating this section of the Act.

According to Section 46(1), a reporting institution is required to carry out thorough due diligence procedures prior to accepting an individual or an entity as a customer. Such due diligence is to be aided by the production of official identity records such as birth certificates, national identity cards, passports and driving licences. In the case of an entity, a certificate of incorporation together with other company documents must be availed. This measure to ensure that the true identity of clients or customers is established prior to the formation of a business relationship is commendable. The problem it creates, however, for reporting institutions is that the authenticity of the documents availed by applicants cannot be ascertained by the reporting institutions without the help of the government agencies that issue those documents. The bureaucracy associated with those government agencies is that such information would take very long to be relayed and received and this therefore hinders and affects business. The competition in the banking industry for example is stiff and a bank might find it hard to keep a potential customer waiting for extended periods of time while their identity is verified.

2.3.6 Conveyance of Monetary Instruments to or from Kenya

The Act makes it an offence for a person to wilfully fail to report the conveyance of monetary instruments into or out of Kenya or materially misrepresent the amount of monetary

instruments.⁸⁵ The Act is couched in mandatory terms demanding that a person intending to convey monetary instruments in excess of an amount prescribed in the second schedule of the Act to or from Kenya should report the particulars concerning that conveyance to a person authorized by the regulations.⁸⁶ The second schedule requires a person who transports monetary instruments of US \$ 10,000 or its equivalent in Kenya Shillings or any other currency into or out of Kenya to declare, in a prescribed form, at the port of entry or exit. The penalty for this offence is a fine not exceeding 10% of the amount of the monetary instruments involved in the offence.⁸⁷ The glaring deficiency in this provision is that it only envisaged hard tangible currency. In this era of plastic cards and mobile money, people rarely carry hard cash when travelling due to the risks associated with carrying money. They would most probably load cash onto Visa or Mastercards which they would expend in the form of electronic cash and carry the balance still in electronic cash upon their return. This provision is therefore outdated and out of touch with the realities of the day.

2.3.7 Misuse of Information

This offence is closely connected to the offence of tipping off under Section 16 of the Act. Any person who knows or ought to reasonably have known that information has been disclosed under the provisions of Part II of the Act⁸⁸ or that an investigation is being, or may be, conducted as a result of such a disclosure and directly or indirectly alerts, or brings information to the attention of another person who will or is likely to prejudice such an investigation, commits an offence

⁸⁵ The Proceeds of Crime and Anti-Money Laundering Act 2009, s 12(3).

⁸⁶ *Ibid*, s 12(1)

⁸⁷ *Ibid*, s 16(3)

⁸⁸ Part II of the Act relates to the operations of the Financial Reporting Centre.

under section 13 of the Act. The penalty for this offence is the same as the penalty for the offence of tipping off.

This provision of the law is in itself very vague. Proof of knowledge is not tangible and it may be impossible to get proof that a person knew or should have known that information has been disclosed. Prosecution for this kind of offence would also be very difficult granted the thresholds of proof that have to be met.

2.3.8 Failure to Comply with an Order of the Court and Hindering a Person in Performance of Functions under the Act

It is an offence under the Act for a person to intentionally refuse or fail to comply with an order of the court.⁸⁹ In addition, the Act makes it an offence for a person who hinders a receiver, a police officer or any other person in the exercise, performance or carrying out of their powers, functions or duties under the Act.⁹⁰ Whereas one may appreciate the reason why this offence was contemplated, sustaining a successful charge for this offence would be an arduous task. Firstly, because the meaning and definition of “hinder” is not provided. Legal provisions should leave no room for misinterpretation and maneuver. In considering the act of hindering, it is not clear whether reference is being made to physical hindrance through physical restraint, emotional and psychological hindrance by way of blackmail, threats and intimidation or even motivational hindrance by way of bribery and corruption. Going by the ambiguity currently contained in this provision, proving hindrance would be almost impossible.

⁸⁹ The Proceeds of Crime and Anti-Money Laundering Act 2009, s 14. Section 16(4) of the Act provides that if a natural person contravenes this provision, he is liable to imprisonment for a term not exceeding two years, or a fine not exceeding one million shillings, or to both. On the other hand, if a body corporate contravenes this provision, it is liable to pay a fine not exceeding five million shillings or the amount of the value of the property involved in the offence, whichever is the higher.

⁹⁰ *Ibid*, s 15

2.4 The Financial Reporting Centre

The Act establishes the Financial Reporting Centre which is a body corporate with the legal powers and privileges bestowed upon bodies corporate.⁹¹ The membership of the Centre consists of a Director and a Deputy Director,⁹² other officers and staff.⁹³ The principal role of the Centre is to formulate policies that enhance the identification of the proceeds of crime and establish measures to combat money laundering.⁹⁴ The Centre whose headquarters are in Nairobi⁹⁵ is mandated, *inter alia*, to: receive and analyse reports of unusual or suspicious transactions made by a reporting institution; send reports which raise reasonable grounds that the transaction is suspicious to the appropriate law enforcement authorities; inspect documents in any reporting institution during ordinary business hours and send the information to the appropriate law enforcement authorities, intelligence agency or supervisory body if the information raises reasonable grounds to suspect that a transaction involves proceeds of crime or money laundering; instructing any reporting institution to facilitate any investigation undertaken or to be undertaken by the Centre; compile statistics and records and make recommendations to the Minister; design training requirements and train reporting institutions on the provisions of the Act; provide information relating to the commission of an offence to any foreign financial intelligence unit or appropriate foreign law enforcement authority; on the basis of mutual agreement and reciprocity enter into any agreement or arrangement, in writing with a foreign financial intelligence unit; set anti-money laundering policies in consultation with the Board; maintain proper books of

⁹¹ *Ibid*, s 21. The Centre has perpetual succession and a common seal and shall be capable, in its corporate name to sue and be sued; taking, purchasing or otherwise acquiring, holding or disposing of movable and immovable property; entering into contracts and doing or performing such other things or acts necessary for the proper performance of its functions under this Act which may lawfully be done by a body corporate.

⁹² *Ibid*, s 25(1)

⁹³ *Ibid*, s 31

⁹⁴ *Ibid*, s 23 (1)

⁹⁵ *Ibid*, s 22

account; engage in any lawful activity aimed at promoting its objectives; and have all the powers necessary or expedient for the proper performance of its functions.⁹⁶ The Centre became formally operational on 12th April, 2012. With effect from 10th October, 2012, the Central Bank of Kenya notified banks, financial institutions, non-bank institutions, mortgage finance companies and forex bureaus to report all suspicious transactions to the Centre now that it is fully operational.

Despite the perception that the Centre is fully operational and in spite of the enormous powers bestowed on it, the Centre has failed to deliver any impactful measures in the form of policy or guidelines and its presence is yet to be felt. Indeed, many of the anti-money laundering guidelines currently being used by financial institutions are those that were formulated and disseminated by the Central Bank of Kenya before the Center was established. There is concern that the Centre is unable to deliver on its mandate due to capacity and resource handicaps. Firstly, the Centre lacks qualified and skilled personnel to drive its agenda. Qualified personnel would put in place robust systems and procedures to aid in the collection, analysis, assessment and channeling of reports to the respective law enforcement agents. Secondly, the Centre lacks investigative, prosecutorial and property seizure powers and is therefore highly dependent on the cooperation of the other government agencies in order to fulfill its mandate under the law. It merely acts as a conveyor belt- receiving reports and channeling them to the appropriate law enforcement agents. Thirdly, the Centre is constrained financially yet it is supposed to supervise and enforce compliance with the law by financial institutions that control multibillion assets in multiple jurisdictions. This situation creates a toothless bulldog kind of scenario. A fourth handicap experienced by the Centre is that the legal complications created by the deficiencies in law highlighted in 2.2 above have rendered the Centre ineffective. Many of the offences

⁹⁶ *Ibid*, s 24

prescribed in the Act are unsustainable due to vagueness, ambiguity and the difficulty posed in trying to prove them. Enforcing the law as it is currently is therefore an uphill task.

2.5 The Anti-Money Laundering Advisory Board

The Act establishes the Anti-Money Laundering Advisory Board (“The Board”). The membership of the board consists of the Permanent Secretary (now Principal Secretary) in the Ministry of finance, who shall also be the Chairperson of the Board; the Permanent Secretary (now Principal Secretary) in the Ministry of internal security; the Attorney-General; the Governor of Central Bank of Kenya; the Commissioner General, Kenya Revenue Authority; the Chairman of Law Society of Kenya; the Chief Executive Officer of the Institute of Certified Public Accountants of Kenya; and a Director who shall be the Secretary to the Board. After its establishment, the Board may co-opt such other persons as appear to it to have special knowledge or experience in anti-money laundering.⁹⁷ The functions of the Board shall be to advise the Director generally on the performance of his functions and the exercise of his powers under this Act and to perform any other duty as prescribed to be performed by the Board under this Act.⁹⁸

The main purpose and role of the Board as was envisaged by the Act was advisory. It is not clear the rationale that was used to determine persons who should sit on the Board as there appears to be no criteria other than holding of specific executive positions. It would have perhaps been more useful and viable if the Board members were subjected to a competitive process so as to bring on board persons with specialized knowledge, skills and expertise on matters of money laundering. Secondly reporting institutions comprise of entities in diverse industries such as

⁹⁷ *Ibid*, s 49(4)

⁹⁸ *Ibid*, s 50

saccos, insurance companies, telecommunication providers, casinos and holders of Mobile Virtual Network Operator (MVNO) licences yet these categories are not represented on the Board. The Terms of Reference for the Board also appear to be too general and vague and it is hard to decipher what exactly the members of the Board are required to do.

2.6 The Assets Recovery Agency

The Act establishes a body to be known as Assets Recovery Agency (“The Agency”) which shall be a semi-autonomous body under the office of the Attorney-General.⁹⁹ The Agency is headed by a Director appointed by the Attorney General.¹⁰⁰ The Act has mandated the Agency to carry out extensive roles, *inter alia*, to recover assets lost through crime or which is or forms part of the proceeds of the crime. The Act grants police officers and the Agency extensive information-gathering powers including powers of entry, search and seizure and provides for international assistance in investigations and proceedings relating to money-laundering.¹⁰¹ It is instructive to note that the Agency has not yet been set up. The Attorney General has recently requested the World Bank to assist in setting up of the Agency.¹⁰² It is therefore safe to state that there are no measures in place in Kenya to implement the freezing and confiscation of laundered funds and assets. It is my contention that the Agency is not currently sitting in the right office. Its purpose would have been better served if it was sitting in the office of the Director of Public Prosecutions or under the Police, specifically under the Economic Crimes Unit of the Criminal Investigations Department. The latter will facilitate its role of investigations while still allowing it to prosecute successfully investigated cases.

⁹⁹ *Ibid*, s 53(1)

¹⁰⁰ *Ibid*, s 53(2)

¹⁰¹ Part VII-XII of the Act.

¹⁰² Mona K Doshi, ‘*Anti-money laundering laws Kenya country Guide for Thomson Reuters*’ (Chambers Global, 2012) p. 3.

2.7 Reporting Institutions

The Act stipulates the institutions which are required to report any suspected money laundering to the Centre. Reporting institutions include financial institutions and designated non-financial businesses such as casinos (including internet casinos), real estate agencies, dealing in precious metals, dealing in precious stones, accountants, who are sole practitioners or are partners in their professional firms and non-governmental organizations. The Minister on the advice of the Centre, may also declare such other business or profession in which the risk of money laundering exists.¹⁰³ Reporting institutions are obliged to monitor and report to the Centre suspected money laundering activities,¹⁰⁴ verify customer identity including that of existing customers,¹⁰⁵ establish and maintain customer records¹⁰⁶ and maintain internal reporting procedures.¹⁰⁷

Regulators and supervisory bodies such as the Central Bank of Kenya, the Insurance Regulatory Authority, the Betting and Licensing Board, the Capital Markets Authority, the Retirement Benefits Authority, the Institute of Certified Public Accountants of Kenya, the Estate Agents

¹⁰³ The Proceeds of Crime and Anti-Money Laundering Act 2009, s 1.

¹⁰⁴ *Ibid*, s 44. Section 44(1) of the Act stipulates that a reporting institution shall monitor on an ongoing basis all complex, unusual, suspicious, large or other transaction as may be specified in the regulations, whether completed or not, and shall pay attention to all unusual patterns of transactions, to insignificant but periodic patterns of transactions that have no apparent economic or lawful purpose as stipulated in the regulations.

¹⁰⁵ *Ibid*, s 45.

¹⁰⁶ *Ibid*, s 46. The records to be kept should include particulars sufficient to identify the name, physical and postal address and occupation (or where appropriate business or principal activity) of each person conducting the transaction or on whose behalf the transaction is being conducted, as well as the method used by the reporting institution to verify the identity of that person; the nature, time and date of the transaction; the type and amount of currency involved; the type and identifying number of any account with the reporting institution involved in the transaction; if the transaction involves a negotiable instrument other than currency, the name of the drawer of the instrument, the name of the institution on which it was drawn, the name of the payee (if any), the amount and date of the instrument, the number (if any) of the instrument and details of any endorsements appearing on the instrument and the name and address of the reporting institution and of the officer, employee or agent of the reporting institution who prepared the record.

¹⁰⁷ *Ibid*, s 47. A reporting institution shall establish and maintain internal controls and internal reporting procedures to identify persons to whom an employee is to report any information which comes to the employee's attention in the course of employment and which gives rise to knowledge or suspicion by the employee that another person is engaged in money laundering and directly report the matter to the Centre in the event that he determines that sufficient basis exists.

Registration Board and the Non-Governmental Organisations Co-ordination Board are also obliged to report suspicious activities to the Centre.¹⁰⁸

The Act enjoins a reporting institution to regularly monitor all complex, unusual, suspicious, high value or other transactions as may be specified in the regulations promulgated under the Act and shall pay attention to unusual patterns of transactions that have no apparent economic or lawful purpose as stipulated in the regulations.¹⁰⁹ Any of the above activities may be considered to be a suspicious transaction. The report should be made within 7 days of the date the suspicious transaction or activity occurred.¹¹⁰

With regard to cash transactions, the reporting threshold for reporting institutions is set at USD 10,000 or its equivalent in any other currency irrespective of whether or not such transactions are suspicious.¹¹¹ This means that a reporting institution would have to report to the Centre any cash transaction whose value is or exceeds USD 10,000 or its equivalent in any other currency. This reporting requirement creates a big burden for reporting institutions firstly because the transaction threshold is relatively low and would result in numerous transactions having to be reported. Secondly, it is not clear whether the regulators such as Capital Markets Authority and Central Bank of Kenya are bound by the same reporting threshold.¹¹² The supervisory bodies will ordinarily handle very high value transactions and the threshold of USD 10,000 would not make sense in their situation.

¹⁰⁸ *Ibid*, s 2 as read with the Second Schedule to the Act.

¹⁰⁹ *Ibid*, s 44 (1)

¹¹⁰ *Ibid*, s 44(2)

¹¹¹ *Ibid*, s 44(3) as read with the fourth schedule to the Act.

¹¹² *Ibid*, s 12(1) as read with the Second Schedule to the Act.

In order to achieve the objectives of this legislation, the Act makes laudable provisions by overriding any obligations of secrecy or disclosure imposed by any other law (save for few exceptions relating to advocate-client privilege) and grants reporting institutions which perform any act in good faith and in furtherance of their obligations under the Act immunity from legal proceedings.¹¹³

Though these provisions of the Act are bold and generous, they pose a great challenge for many reporting institutions such as estate agents, small accountancy firms, casinos and NGOs. This is because no clear guidance has been given to them on how they are to carry out their obligations to comply with the Act.¹¹⁴ There is no proper guidance on how, for instance, dealers in precious stones are expected to verify their customers. What kind of due diligence should they carry out? Would they be bound by the same due diligence requirements that a bank would have to carry out on its customers?

Small-size reporting institutions with limited resources will find it cumbersome to comply with the provisions of the Act and they might require additional financial and human resources to facilitate scrutiny of customer transactions, reporting of suspicions and ultimately full compliance with the Act. The biggest challenge to the reporting institution is how to balance client relationships which translate to business and compliance with the law.

The third shortcoming of the reporting requirement is that there is no evidence that the Centre or anybody else is monitoring whether or not reporting institutions are reporting what they should

¹¹³ *Ibid*, s 17. Section 18(1) upholds advocate-client confidentiality and states that, notwithstanding the provisions of section 17, nothing in this Act shall affect or be deemed to affect the relationship between an advocate and his client with regard to communication of privileged information between the advocate and the client.

¹¹⁴ Mona Doshi, 'Anti-money laundering laws Kenya country Guide for Thomson Reuters' (Chambers Global) p. 5.

be reporting. What has therefore happened is that we have a legal provision on paper that is neither adhered to nor enforced.

2.8 Requirement to Carry out Due Diligence

The Act enjoins a reporting institution to take reasonable measures to satisfy itself as to the identity of the applicant seeking to enter into a business relationship with it or carry out a transaction or series of transactions with it by requiring the applicant to produce appropriate identification documents listed in the Act which enables the reporting institution to establish the true identity of the applicant.¹¹⁵ Each reporting institution is required to undertake customer due diligence on its existing customers.¹¹⁶ The reporting institution is required to maintain customer accounts in the correct name of the account holder.¹¹⁷ A reporting institution is required to establish and maintain the name, physical address, postal address of its customer, nature, time and date of all transactions, type and amount of currency involved, type and number of the account, details of the negotiable instruments if any, details of the reporting institution and its employees who prepared the record.¹¹⁸ The records should be kept for a minimum period of 7 years from the date of completion of the transaction without prejudice to any other records required to be kept by or under any other written law.¹¹⁹

The reporting obligations shall apply to accountants when preparing or carrying out transactions for their clients when buying or selling real estate, managing client money, savings or securities accounts, organization of contributions for creation, operation or management of companies and creation, operation or management of buying and selling of business entities¹²⁰.

¹¹⁵ The Proceeds of Crime and Anti-Money Laundering Act 2009, s 45(1).

¹¹⁶ *Ibid*, s 45(2)

¹¹⁷ *Ibid*, s 46(2)

¹¹⁸ *Ibid*, s 46(3)

¹¹⁹ *Ibid*, s 46(4)

¹²⁰ *Ibid*, s 48

The import of these provisions is that all financial institutions are required to take reasonable measures to establish and verify the identity of all customers regardless of the risk associated with the customer or the transaction. The relevant Minister may make regulations providing for high risk customers or clients. However, these regulations have not been issued and this has delayed the realization of the benefits of this provision. Nevertheless, the challenges that are likely to be encountered by a reporting institution during carrying out of due diligence is the presentation by applicants of forged identity documentation. The reporting institutions fully rely on government agencies such as National Registration Bureau to confirm authenticity of identity documentation, a process that is not instantaneous. Secondly, of all the information that the Act requires the reporting institution to collect, only the identity information is likely to remain constant. This is because customers regularly change their physical and postal addresses. It is therefore not useful to collect documentation and information that is of an evolving nature. Perhaps the government should consider introducing a digitized Social Security number that uniquely identifies all persons and serves as a unique identifier.

Although on one hand Section 21(1) of the Act attempts to provide some protection to a whistle blower to provides information to the Centre with regard to money laundering activity, Section 21 (2) takes the protection away by providing that the veil of confidentiality shall be lifted for purposes of enabling the Centre carry out its functions or if a civil or criminal case is instituted with respect to the reported money laundering activity. By limiting the protection offered, the law deters potential whistleblowers from providing information for fear that their identities might be revealed.

2.9 The Proceeds of Crime and Anti-Money Laundering Regulations 2013

The Act has envisaged that regulations would be made setting out in detail the requirements of reporting institutions to exercise due diligence and take reasonable measures to satisfy themselves as to the true identity of any person seeking to enter into a business relationship with them, to establish and maintain records of transactions to report activities which they have reasonable grounds to believe are suspicious or unusual, to maintain internal reporting procedures to make employees aware of the laws in Kenya relating to money-laundering and to train employees in the recognition and handling of suspicious activities and to maintain an adequate anti-money laundering compliance programme.¹²¹

After the commencement of the Act, the Central Bank of Kenya published the Guidelines on Proceeds of Crime and Money Laundering (Prevention), 2008¹²² which set out guidelines for banks, financial institutions, non-bank financial institutions, mortgage finance, companies and forex bureaus to report to the Central Bank of Kenya suspicious transactions and to report cash transactions exceeding US \$ 10,000.00 on prescribed forms and carry out appropriate due diligence on customers.

The 2013 regulations under the Act have set out provisions on how reporting institutions are to be registered with the Centre, how to conduct customer due diligence, reporting of suspicious transactions, obligations of reporting institutions, requirement to train employees, cross-border conveyance of monetary instruments etc. These regulations compliment the provisions of the Act.

¹²¹ *Ibid*, s 134. See also the Proceeds of Crime and Anti-Money Laundering Regulations, 2013 available at: <http://frc.go.ke/legislation/category/regulations>, accessed 28th July 2013.

¹²² Central Bank of Kenya Guidelines on Proceeds of Crime and Money Laundering (Prevention) CBK/PG/08. Available at: http://www.imolin.org/doc/amlid/Kenya_Prudential%20Guidelines%20for%20Institutions%202006_Guideline%20on%20Proceeds%20of%20Crime%20and%20Money%20Laundering%20CBK_PG_08.pdf, accessed 28th July 2013.

2.10 Money Remittance Regulations 2013¹²³

Published in April 2013, these regulations cover both inbound and outbound money remittances. The intention of the regulations was to bring into mainstream financial sector the previously informal remittance systems such as Hawala. The regulations also bring into the realm of reporting institutions all previously unregulated money remittance establishments making them subject to and eligible to comply with the Act.

2.11 Conclusion

In conclusion, this chapter has discussed the background leading to the enactment of the Proceeds of Crime and Anti-money Laundering Act in Kenya and has also interrogated key provisions of the Act. While acknowledging that the enactment of this Act is a bold step in the development of measures to counter money laundering, the Chapter also highlights major weaknesses and deficiencies in the law that have made its enforcement both impractical and unenforceable due to logistical, financial and capacity constraints.

¹²³ Money Remittance Regulations 2013.

CHAPTER THREE
INTERNATIONAL AND REGIONAL ANTI-MONEY LAUNDERING INSTRUMENTS
AND INSTITUTIONS

3.1 Overview

The first two chapters highlighted the background of the research and critiqued the Proceeds of Crime and Anti-money Laundering Act as it exists currently. This chapter is dedicated to a discussion and analysis of international AML instruments, their historical development and the role they have played in the design and formulation of the current domestic AML law. The development of a set of norms designed to tackle money laundering, and, more generally, to boost a more effective punishment of acquisitive crime, has brought about a number of transformations that pertain to the way the law itself is shaped. The fight against money laundering is significant on two very important evolutions in the norm-making process, namely the influence of soft law and the international impetus for the creation of anti-money laundering law.¹²⁴ These evolutions are especially notable as they take place in field of law enforcement, traditionally considered the exclusive ‘playground’ of national courts and parliaments.¹²⁵

The fight against money laundering has been deeply influenced by a number of so-called ‘soft’ law instruments.¹²⁶ The term “soft law” refers to the lack of justiciability of the instruments in

¹²⁴ Guy Stessens, *Money Laundering: A New International Law Enforcement Model* (Cambridge University Press, 2002) p. 15.

¹²⁵ *Ibid.*

¹²⁶ Tadzysz Grachalla-Wesierski, ‘A Framework for Understanding “Soft Law” available at: <http://lawjournal.mcgill.ca/documents/30/1/wesierski.pdf>, accessed 26th August 2013. He states that soft law includes both legal and non-legal instruments. These instruments are characterized by the relatively large amount of discretion which is left to the party bound by the obligation. Although soft law norms are discretionary in nature, they are not without important legal and political effects. By its very presence, soft law promotes a trend to the

which the rules are enshrined (*instrumentum*), rather than to the content of the rules themselves (*negotium*). An important factor which explains the role of soft law in the fight against money laundering is the aversion to government interference financial institutions have often displayed.¹²⁷ The United Nations Commission on Crime Prevention and Criminal Justice stated that:

*“It could be said that policies and strategies against the laundering of the proceeds of crime should have as one of their prime objectives the creation of an atmosphere of consensus regarding the measures to be devised and implemented. The financial institutions should be parties to that process and consensus. It remains the prerogative of Governments to adopt and implement measures of a legislative and regulatory nature. Financial institutions should be consulted, however, in view of their immediate involvement, and should share the burden of efforts against the laundering of proceeds of crime.”*¹²⁸

It is safe to note that the contribution of international soft law instruments to the fight against money laundering is impressive. One of the earliest international initiatives undertaken in the field of money laundering was the Recommendation No. R (80)10 adopted by the Committee of Ministers of the Council of Europe on 27 June 1980 entitled ‘Measures against the transfer and safeguarding of the funds of criminal origin’. The Committee considered that the transfer of funds of criminal origin from one country to another and the process by which they are laundered through insertion in the economic system give rise to serious problems, encourage the

‘hardening’ of international relations. By its use and by subsequent practice, it may become subject to more effective interpretation.

¹²⁷ *Ibid.*

¹²⁸ United Nations Commission on Crime Prevention and Criminal Justice, Report on the second session (13rd -23rd April, 1993) available at: <http://www.unodc.org/documents/commissions/CCPCJ/N9405313.pdf> accessed 26th August, 2013.

perpetration of further criminal acts and thus cause the phenomenon to spread nationally and internationally. The Committee also passed a resolution to the effect that the banking system can play a highly effective preventive role, while the co-operation of the banks also assists in the repression of such criminal acts by the judicial authorities and the police.

3.2 The Basel Statement of Principles

The Basel Statement of Principles¹²⁹ was the first international instrument to address the issue of money laundering. The Basel Committee, which comprises the authorities charged with banking supervision of twelve Western countries, thought it found it necessary to take action against money laundering lest public confidence, and consequently the stability of banks, be undermined by adverse publicity as a result of inadvertent association of banks with criminals. Regardless of the fact that the primary function of banking supervision is to maintain overall the financial stability of the banking system rather than to ensure that individual financial transactions are legitimate, the supervisors thought that they could not stay indifferent to the use made of banks by criminals.¹³⁰

The Report on Prevention of Criminal use of the Banking System for the Purpose of Money-Laundering notes that banks and other financial institutions may be unwittingly used as intermediaries for the transfer or deposit of funds derived from criminal activity. Criminals and their associates use the financial system to make payments and transfers of funds from one account to another; to hide the source and beneficial ownership of money; and to provide storage

¹²⁹ The Basel Statement of Principles of 12 December 1988, issued by the Basel Committee on Banking Regulations and Supervisory Practices available at: <http://www.bis.org/publ/bcbs213.pdf>, accessed 27th August, 2013.

¹³⁰ The Report on Prevention of Criminal Use of the Banking System for the Purpose of Money –laundering, December, 1988 available at: <http://www.bis.org/publ/bcbssl37.pdf>, accessed 26th August, 2013.

for bank-notes through a safe deposit facility. These activities are commonly referred to as money-laundering.¹³¹

The report further notes that the steps that had hitherto been taken with the objective of preventing the banking system from being used as intermediaries for the transfer or deposit of funds derived from criminal activity were undertaken by judicial and regulatory agencies at national level. The increasing international dimension of organized criminal activity, notably in relation to the narcotics trade, prompted collaborative initiatives at the international level.¹³² One such initiative was undertaken by the Committee of Ministers of the Council of Europe in June, 1980. In its report,¹³³ the Committee of Ministers concluded that “...*the banking system can play a highly effective preventive role while the co-operation of the banks also assists in the repression of such criminal acts by the judicial authorities and the police.*”

In recent years the issue of how to prevent criminals laundering the proceeds of crime through the financial system has attracted increasing attention from legislative authorities, law enforcement agencies and banking supervisors in a number of countries.¹³⁴ The Basel Committee, while recognizing that the primary function of banking supervision is to maintain the overall financial stability and soundness of banks rather than to ensure that individual transactions conducted by bank customers are legitimate, also noted that despite the limits in some countries on their specific responsibility, all members of the Committee firmly believe that banking supervisors cannot be indifferent to the use made of banks by criminals.¹³⁵ The Committee then concludes that banking supervisors have a general role to encourage ethical

¹³¹ *Ibid.*

¹³² *Ibid.*

¹³³ Measures against the Transfer and Safeguarding of Funds of Criminal origin, recommendation No. R(80)10 adopted by the Committee of Ministers of the Council of Europe on 27th June, 1980.

¹³⁴ *Ibid.*

¹³⁵ *Ibid.*

standards of professional conduct among banks and other financial institutions. The Committee then goes ahead to make a general statement of ethical principles which encourage banks' management to put in place effective procedures to ensure that all persons conducting business with their institutions are properly identified; the transactions that do not appear legitimate are discouraged; and that cooperation with law enforcement agencies is achieved.

The Statement of Principles outlines some basic policies and procedures that banks' managements should ensure are in place within their institutions with a view to assisting in the suppression of money-laundering through the banking system, national and international. The Statement of Principles seeks to reinforce best practices among banks and, specifically, to encourage vigilance against criminal use of the payments system, implementation by banks of effective preventive safeguards and cooperation with law enforcement agencies. The basic policies outlined are:

3.2.1 Customer identification

Banks are encouraged to make reasonable efforts to determine the true identity of all customers requesting the institutions' services. This is with a view to ensuring that the financial system is not used as a channel for criminal funds. Particular care should be taken to identify the ownership of all accounts and those using safe-custody facilities. All banks are encouraged to institute effective procedures for obtaining identification from new customers. It is proposed that it should be an explicit policy that significant business transactions will not be conducted with customers who fail to provide evidence of their identity.

3.2.2 Compliance with laws

This principle requires banks to ensure that business is conducted in conformity with high ethical standards and that the law and regulations pertaining to financial transactions are adhered to. Banks should not set out to offer services or provide active assistance in transactions which they have good reason to suppose are associated with money-laundering activities.

3.2.3 Cooperation with law enforcement authorities

This principle requires banks to cooperate fully with national law enforcement authorities to the extent permitted by specific local regulations relating to customer confidentiality. Care should be taken to avoid providing support or assistance to customers seeking to deceive law enforcement agencies through the provision of altered, incomplete or misleading information. Banks are required to take appropriate measures which are consistent with the law where they become aware of facts which lead to the reasonable presumption that money held on deposit derives from criminal activity or that transactions entered into are themselves criminal in purpose.

3.2.4 Adherence to the Statement

This principle requires all banks to formally adopt policies that are consistent with the principles set out in the Statement of Principles¹³⁶ and to ensure that all members of their staff concerned, wherever located, are informed of the bank's policy in this regard. In order to promote adherence to the principles, banks are required to implement specific procedures for customer identification and for retaining internal records of transactions. Even though the Statement is not a legal document and its implementation was anticipated to depend on national practice and law, it provides important guidelines on how banks and other financial institutions can contribute to

¹³⁶ Kerwer Dieter, 'Rules that many use: standards and global regulation' (October 2005) Governance (US). Vol. 18, Issue 4, p. 616.

tackling the problem of money-laundering. Whatever the legal position in different countries, the Committee considered that the first and most important safeguard against money-laundering is the integrity of banks' own managements and their vigilant determination to prevent their institutions becoming associated with criminals or being used as a channel for money laundering. It will be demonstrated how the Committee's considerations and principles outlined in the Statement of Principles have informed or influenced the development of anti-money laundering laws.

3.3 United Nations Convention Against Illicit Traffic in Narcotic Drugs and Psychotropic Substances

As the international drug trafficking and the tremendous amounts of related money entering the bank system were very high, the United Nations, through the United Nations Drug Control Programme (UNDCP) made the first move through an international agreement to combat drug trafficking and money laundering. This effort was seen in the adoption of the United Nations Convention Against Illicit Traffic in Narcotic Drugs and Psychotropic Substances. The Convention came into force on 11th November, 1990 and Kenya gave its accession on 19th October 1992.¹³⁷ It deals primarily with provisions to combat the illegal drug trades and related law enforcement issues.

The Preamble to the Convention outlines the issues that motivated the introduction of the Convention. These include a recognition of the link between illicit traffic and other related organized criminal activities which undermine the legitimate economies and threaten the stability, security and sovereignty of States, and the awareness that illicit traffic generates large

¹³⁷ United Nations Convention Against Illicit Traffic in Narcotic Drugs and Psychotropic Substances available at: https://treaties.un.org/pages/ViewDetails.aspx?src=TREATY&mtdsg_no=VI-19&chapter=6&lang=en, accessed 28th August, 2014.

financial profits and wealth enabling transnational criminal organizations to penetrate, contaminate and corrupt the structures of government, legitimate commercial and financial business, and society at all its levels.

The purpose of the Convention is to promote co-operation among the Parties so that they may address more effectively the various aspects of illicit traffic in narcotic drugs and psychotropic substances having an international dimension. In carrying out their obligations under the Convention, the Parties are required to take necessary measures, including legislative and administrative measures, in conformity with the fundamental provisions of their respective domestic legislative systems.¹³⁸

Article 3(1) of the Convention requires each party to adopt such measures as may be necessary to establish as criminal offences under its domestic law, when committed intentionally, *inter alia*, the conversion or transfer of property, knowing that such property is derived from any offence or offences of illicit traffic of narcotic drugs and psychotropic substances established in accordance with Article 3(1) (a), or from an act of participation in such offence or offences, for the purpose of concealing or disguising the illicit origin of the property or of assisting any person who is involved in the commission of such an offence or offences to evade the legal consequences of his actions¹³⁹ and the concealment or disguise of the true nature, source, location, disposition, movement, rights with respect to, or ownership of property, knowing that such property is derived from an offence or offences of illicit traffic of narcotic drugs and psychotropic substances established in accordance with Article 3(1) (a), or from an act of participation in such

¹³⁸ United Nations Convention Against Illicit Traffic in Narcotic Drugs and Psychotropic Substances, Article 2(1).

¹³⁹ *Ibid*, Article 3(1) (b) (i).

an offence or offences.¹⁴⁰ These statements allude to money laundering, particularly the laundering of proceeds of illicit traffic in drugs and psychotropic substances.

Article 5(1) of the Convention requires each Party to adopt such measures as may be necessary to enable confiscation of, inter alia, proceeds derived from offences established in accordance with Article 3(1) or property the value of which corresponds to that of such proceeds.¹⁴¹ Each Party is further required to adopt such measures as may be necessary to enable its competent authorities to identify, trace, and freeze or seize proceeds, property, instrumentalities or any other thing referred to in Article 5(1) for the purpose of eventual confiscation.¹⁴²

Perhaps most importantly with regard to relevance to the present discourse, Article 5(3) of the Convention provides that in order to carry out the measures referred to in the article, each Party shall empower its courts or other competent authorities to order that bank, financial or commercial records be made available or be seized. A Party shall not decline to act under the provisions of this paragraph on the ground of bank secrecy.

The Convention was intended to deal with offences of trafficking of drugs and psychotropic substances, and does not therefore deal with money laundering in the broader sense. However, to the extent that money laundering is a component of the wider process of drug trafficking, the Convention deals with aspects of money laundering. The provisions of the Convention in this regard have been influential not only in the passing of national laws on drug trafficking but also in the formulation of legislation aimed at combating money laundering.

¹⁴⁰ *Ibid.*, Article 3(1) (b) (ii).

¹⁴¹ *Ibid.*, Article 5(1) (a).

¹⁴² *Ibid.*, Article 5(2).

3.4 The 1990 Council of Europe Convention on Laundering, Search, Seizure and Confiscation of the Proceeds of Crime

The text of this convention was drafted by a limited committee within the European Committee for Crime Problems (ECCP) of the Council of Europe. Although Kenya is not one of the forty eight signatories to the Convention,¹⁴³ the Convention constitutes the first international binding legal instrument that focuses exclusively on money laundering. Like the United Nations Convention Against Illicit Traffic in Narcotic Drugs and Psychotropic Substances, it deals only with the repressive fight against money laundering and it contains a number of substantive criminal law provisions, as well as mechanisms for international co-operation in criminal matters. The Council of Europe Convention, however, differs from the United Nations Convention Against Illicit Traffic in Narcotic Drugs and Psychotropic Substances in that its scope is not limited to drug proceeds, but in principle encompasses the proceeds from any offence. The drafters of the Council of Europe Convention nevertheless attempted to use, as far as possible the same terminology as the United Nations Convention Against Illicit Traffic in Narcotic Drugs and Psychotropic Substances.

The Convention was opened for signature on 8th November, 1990 and is open to all states, including states who are not members of the Council of Europe. Therefore it is not bestowed with the epithet 'European Convention'.

¹⁴³ The 1990 Council of Europe Convention on Laundering, Search, Seizure and Confiscation of the Proceeds of Crime available at: <http://conventions.coe.int/Treaty/Commun/ChercheSig.asp?NT=141&CM=&DF=&CL=ENG> accessed 28th August, 2014.

Article 2(1) of the Convention requires each party to adopt such legislative and other measures as may be necessary to enable it to confiscate instrumentalities and proceeds or property the value of which corresponds to such proceeds.

Article 6(1) of the Convention provides for laundering offences. It provides that each party shall adopt such legislative and other measures necessary to establish as offences under its domestic law, when committed intentionally:

- (a) the conversion or transfer of property, knowing that such property is proceeds, for the purpose of concealing or disguising the illicit origin of the property or of assisting any person who is involved in the commission of the predicate offence to evade the legal consequences of his actions;
- (b) the concealment or disguise of the true nature, source, location, disposition, movement, rights with respect to, or ownership of, property, knowing that such property is proceeds; and, subject to its constitutional principles and the basic concepts of its legal system;
- (c) the acquisition, possession or use of property, knowing, at the time of receipt, that such property was proceeds; and
- (d) participation in, association or conspiracy to commit, attempts to commit and aiding, abetting, facilitating and counselling the commission of any of the offences established in accordance with this article.

The Convention recognizes the need for international cooperation in combating money laundering and makes provisions with regard to international cooperation in Chapter III of the Convention.¹⁴⁴ The general principles of international cooperation are that the Parties shall co-

¹⁴⁴ The 1990 Council of Europe Convention on Laundering, Search, Seizure and Confiscation of the Proceeds of

operate with each other to the widest extent possible for the purposes of investigations and proceedings aiming at the confiscation of instrumentalities and proceeds and each Party shall adopt such legislative or other measures as may be necessary to enable it to comply, under the conditions provided for with requests for confiscation of specific items of property representing proceeds or instrumentalities, as well as for confiscation of proceeds consisting in a requirement to pay a sum of money corresponding to the value of proceeds and for investigative assistance and provisional measures with a view to either form of confiscation.¹⁴⁵

3.5 The EC Council Directive of 10 June 1991 on the Prevention of the Use of the Financial System for the Purpose of Money Laundering

The genesis of the European Money Laundering Directive effectively illustrates the effects of the two movements that were outlined: the influence of other legal norms than criminal law and the internationalization of the legislative process. Although the directive, as its name suggests, relates only to the prevention of money laundering and not to the repression of money laundering, its legal basis has nevertheless been fiercely disputed.

The preamble of the directive cites two provisions of the Treaty Establishing the European Economic Community. The cited provisions are Article 57(2) provides for the co-ordination of provisions concerning the taking-up and pursuit of activities as self-employed persons and Article 100(a) which allows for measures for the approximation of the legislative, regulatory and administrative provisions pertaining to the establishment and functioning of the single market. These particular provisions are mentioned since in the absence of such measures, money launderers were likely to take advantage of the freedom of movement of capital and of the

Crime, Articles 7 to 35.

¹⁴⁵ *Ibid*, Article 7.

freedom to supply financial services which follow from the introduction of the integrated financial area.¹⁴⁶

Article 1 of the Directive defines money laundering to mean the following conduct when committed intentionally:

- (a) the conversion or transfer of property, knowing that such property is derived from criminal activity or from an act of participation in such activity, for the purpose of concealing or disguising the illicit origin of the property or of assisting any person who is involved in the commission of such activity to evade the legal consequences of his action;
- (b) the concealment or disguise of the true nature, source, location, disposition, movement, rights with respect to, or ownership of property, knowing that such property is derived from criminal activity or from an act of participation in such activity;
- (c) the acquisition, possession or use of property, knowing, at the time of receipt, that such property was derived from criminal activity or from an act of participation in such activity; and
- (d) participation in, association to commit, attempts to commit and aiding, abetting, facilitating and counselling the commission of any of the actions mentioned in the foregoing paragraphs.

Knowledge, intent or purpose required as an element of the abovementioned activities may be inferred from objective factual circumstances. In addition, money laundering shall be regarded as such even where the activities which generated the property to be laundered were perpetrated in the territory of another Member State or in that of a third country.

¹⁴⁶ The EC Council Directive of 10 June 1991 on the Prevention of the Use of the Financial System for the Purpose of Money Laundering, second paragraph.

Article 2 of the Directive provides that Member States shall ensure that money laundering as defined in the Directive is prohibited.

The Directive requires Member states to ensure that credit and financial institutions require identification of their customers by means of supporting evidence when entering into business relations, particularly when opening an account or savings accounts, or when offering safe custody facilities.¹⁴⁷

The Directive further requires Member States to ensure that credit and financial institutions examine with special attention any transaction which they regard as particularly likely, by its nature, to be related to money laundering.¹⁴⁸

Article 6 of the Directive then requires Member States to ensure that credit and financial institutions and their directors and employees cooperate fully with the authorities responsible for combating money laundering by informing those authorities, on their own initiative, of any fact which might be an indication of money laundering, and by furnishing those authorities, at their request, with all necessary information, in accordance with the procedures established by the applicable legislation.

Pursuant to Article 7 of the Directive, Member States shall ensure that credit and financial institutions refrain from carrying out transactions which they know or suspect to be related to money laundering until they have apprised the authorities referred to in Article 6.

The original proposal of the Commission on prevention of the use of the financial system for the purpose of money laundering also contained an obligation for Member States to provide criminal sanctions for money laundering. This obligation was subsequently watered down to an obligation to prohibit money laundering. As the community lacks legislative jurisdiction to lay

¹⁴⁷ *Ibid*, second paragraph, Article 3(1)

¹⁴⁸ *Ibid*, second paragraph, Article 5

down criminal sanctions, Article 2 of the Directive requires only that money laundering shall be prohibited and Article 14 of the Directive does not specify what kind of sanctions should be applied for infringements of measures to be adopted pursuant to the Directive.

When adopting the directive, the representatives of the governments of the Member States issued a statement in which they refer to United Nations Convention Against Illicit Traffic in Narcotic Drugs and Psychotropic Substances and the Money Laundering Convention. They explicitly state that the description of money laundering contained in Article 1 of the directive derives its wording from the relevant provisions of these conventions and ‘undertake to take all necessary steps by 31st December, 1993 at the latest to enact criminal legislation enabling them to comply with their obligations under these instruments’. The inability to provide for criminal sanctions was thus circumvented by an intergovernmental statement attached to the Directive committing to legislate on the criminal offence.

All these factors led to the conclusion that, notwithstanding its seemingly preventive outlook, the directive is an integral part of the international law enforcement regime concerning money laundering. The first report of the Commission on the implementation of the Money Laundering Directive warrants this conclusion. The Commission explicitly acknowledges that the directive has influenced domestic criminal law, as all Member States have chosen to implement the prohibition of money laundering which follows from Article 3 of the directive, through criminal law.¹⁴⁹ Kenya is not a member state of this EC Council Directive.

¹⁴⁹ *Ibid.*

3.6 The International Convention Against Transnational Organised Crime (The Palermo Convention)

In order to expand the effort to fight international organized crime, the United Nations adopted the International Convention Against Transnational Organised Crime. This Convention contains a broad range of provisions to fight organized crime and commits countries that ratify this Convention to implement its provisions through passage of domestic laws.¹⁵⁰ The Convention went into force on the 29th September, 2003, having been signed by 147 countries and ratified by 82 countries. Kenya gave its accession on 16th June, 2004.¹⁵¹ Its AML provisions adopt the same approach previously adopted by the Financial Action Task Force on Money Laundering (FATF) in its Forty Recommendations on Money Laundering.

The purpose of this Convention is to promote co-operation to prevent and combat transnational organized crime more effectively.¹⁵² The Convention includes 41 Articles and is the most important international document that has special view to transnational organized crime. The Convention declares that parties to the Convention will carry out their obligations under the Convention in a manner consistent with the principles of sovereign equality and territorial integrity of States and that of non-intervention in the domestic affairs of other States. Nothing in the Convention entitles a State Party to undertake in the territory of another State the exercise of

¹⁵⁰ The International Convention Against Transnational Organised Crime (The Palermo Convention), Article 5.

¹⁵¹ Available at: https://treaties.un.org/Pages/ViewDetails.aspx?src=TREATY&mtdsg_no=XVIII-12&chapter=18&lang=en, accessed 28th August, 2014.

¹⁵² The International Convention Against Transnational Organised Crime (The Palermo Convention), Article 1.

jurisdiction and performance of functions that are reserved exclusively for the authorities of that other state by its domestic law.¹⁵³

The Convention defines money laundering as intentional conversion or transfer of property knowing that such property is proceeds of crime, for the purpose of concealing or disguising the illicit origin of the property or of assisting any person who is involved in the commission of the predicate offence to evade the legal consequences of his actions. The concealment or disguise of the true nature, source, location, disposition, movement, rights with respect to, or ownership of property, knowing that such property is the proceeds of crime; and subject to those constitutional principles and the basic concept of its legal system.¹⁵⁴ The acquisition, possession or use of property, knowing at the time of receipt, that such property is the proceeds of crime; by participation in association or conspiracy to commit and aiding, abetting, facilitating and counseling the commission of any offences established in accordance with this article.¹⁵⁵ The Convention widely extends laundering offences as compared with the provisions of the Vienna Convention and includes all crimes, not only drug crimes.

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

Kenya is a member of the Eastern and Southern Africa Anti-money Laundering Group (ESAAMLG). ESAAMLG was launched at a meeting of Ministers and high-level representatives in Arusha, Tanzania, on 26th -27th August, 1999. A memorandum of understanding (MoU) based on the experience of the FATF and other FATF-style regional bodies was agreed to at that meeting. Following the signature of the MoU by seven of the potential members, ESAAMLG

¹⁵³ *Ibid*, Article 4.

¹⁵⁴ *Ibid*, Article 6.

¹⁵⁵ *Ibid*, Article 7.

came into formal existence. All members are Commonwealth countries which have committed to the FATF Forty Recommendations. The group held its first meeting on 17th -19th April, 2000 in Dar es Salaam, Tanzania. Following the events of 11th September, 2001, ESAAMLG expanded its scope to include the countering of terrorist financing. The group currently has 16 member states most of who have struggled and lagged behind in implementing the recommendations of Financial Action Task Force (FATF).

The purpose of the Eastern and Southern Africa Anti-Money Laundering Group (ESAAMLG) is to combat money laundering by implementing the FATF Recommendations. This effort includes coordinating with other international organisations concerned with combating money laundering, studying emerging regional typologies, developing institutional and human resource capacities to deal with these issues, and coordinating technical assistance where necessary. ESAAMLG enables regional factors to be taken into account in the implementation of anti-money laundering measures. ESAAMLG members participate in a self-assessment process to assess their progress in implementing the FATF Forty Recommendations. The ESAAMLG Secretariat is located in Dar es Salaam, Tanzania. ESAAMLG became an Associate Member of the FATF in June 2010. The 16 member states have come up with a Post Evaluation Implementation Plan (PEIP) aimed at enabling them to implement the core and key recommendations. Among the things the member states have agreed to do is to: allocate resources efficiently and effectively, identify and assign a lead agency responsible for implementation; and set out realistic completion dates for key outputs and recommendations.

3.8 Conclusion

This Chapter has outlined the major historical international instruments on money laundering. The next chapter sets to compare the anti-money laundering legislation in Kenya to similar AML

laws in South Africa. The discussion will focus on identifying key and critical elements of the legal, regulatory and institutional anti-money laundering frameworks in South Africa that Kenya can borrow to enhance its own AML law.

CHAPTER FOUR
A COMPARATIVE ANALYSIS OF THE ANTI MONEY LAUNDERING
LEGISLATION IN KENYA VIS- A- VIS SIMILAR LAWS IN SOUTH AFRICA AND
CANADA

4.1 Overview

This chapter provides a comparative analysis of anti-money laundering legal regime in Kenya as compared to that in South Africa and that in Canada. Whereas Canada is a developed country with an advanced financial services sector and a current GDP of 51,206 USD per capita,¹⁵⁶ South Africa is a developing country with a less advanced financial services sector and a GDP of 7,352 USD per capita.¹⁵⁷ Both countries have been waging war against money laundering for close to two decades, Canada having promulgated its first anti-money laundering legislation, Proceeds of Crime (Money Laundering) Act, in 1991 and South Africa, the Prevention of Organised Crime Act in 1998. Both countries have also established institutions and agencies to enhance compliance with the law and to aid in the prevention and early detection of money laundering schemes.

A critical examination of the legal provisions and institutional operations of the two countries will help identify key aspects of the legal and institutional frameworks currently in place in Canada and South Africa that Kenya can borrow to enhance its own anti- money laundering legal regime.

¹⁵⁶ Available at: www.tradingeconomics.com/canada/gdp, accessed 26th August, 2014.

¹⁵⁷ Available at: www.tradingeconomics.com/southafrica/gdp accessed 26th August, 2014.

4.2 Combating Money Laundering: The Case of the Republic of South Africa

The Republic of South Africa is a developing country located in a region where the economy remains primarily cash-based. It has a first-world banking sector characterized by well-established infrastructure and technology, but limited participation¹⁵⁸ and a growing demand for financial services. A priority of the government is to ensure that individuals currently outside the bracket of those using formal financial services, particularly potential low-income customers, can access and, on a sustainable basis, use financial services being offered by registered financial services providers and which are appropriate to their needs.¹⁵⁹

Major profit-generating crimes in South Africa include fraud, theft, corruption, racketeering, precious metals smuggling, abalone poaching, Nigerian-type economic/investment frauds and pyramid schemes¹⁶⁰ with increasing numbers of sophisticated and large-scale economic crimes and crimes through criminal syndicates. South Africa remains a transport point for drug trafficking. Corruption also presents a problem.¹⁶¹ Analysis indicates that foreign nationals are using South African nationals, mostly women, to help them send money gained from illegal activities to foreign countries. In addition, there is a significant black market for smuggled and stolen goods.

Other trends in money laundering are based on investment frauds through pyramid schemes and fraud cases through fake cheques. Funds are noted to have been laundered through lawyers or

¹⁵⁸ Over 60% of the adult population was excluded from any formal financial services in 1994.

¹⁵⁹ Mutual Evaluation Report on Anti-Money Laundering and Combating the Financing of Terrorism of the Republic of South Africa, (February 2009) available at: <http://www.treasury.gov.za/publications/other/Mutual%20Evaluation%20Report%20-%20Executive%20Summary%20AntiMoney%20Laundering%20and%20Combating%20the%20Financing%20of%20Terrorism%202009.pdf>, accessed 17th September, 2013.

¹⁶⁰ Investment clubs, known as stokvels, have been used cover for pyramid schemes. In some instances, nominee structures have been exploited by criminals who intend to launder illicit funds for mixing them with legitimate assets held on someone's behalf. Available at: <http://www.knowyourcountry.com/southafrica111.html>, accessed 17th September, 2013.

¹⁶¹ *Ibid.*

other service providers, purchasing of properties, establishment of shell companies and home businesses. The authorities also pointed to an increase in the sophistication and scale of economic crime and crimes through criminal syndicates. South Africa remains a significant transport point for drug trafficking. South Africa authorities are committed to pursuing this issue through a range of initiatives such as the introduction of measures to entrench good governance and transparency, the establishment of government agencies to investigate and recover funds lost by the state through corruption, passing legislation addressing corruption in the private and public sectors and instituting criminal prosecutions in appropriate cases.¹⁶²

South Africa has demonstrated a strong commitment to implementing the country's AML/CFT systems which has entailed close co-operation and co-ordination between a variety of governmental departments and agencies. In 1998, the country promulgated the Prevention of Organised Crime Act and thereafter, implemented the Financial Intelligence Centre Act.¹⁶³ In 2004, South Africa approved the Protection of Constitutional Democracy against Terrorist and Related Activities Act.¹⁶⁴ This Act is the overarching national anti-terrorism legislation, criminalizing terrorist financing and contains measures to freeze terrorist related funds in line with international obligations.

This chapter discusses the legislative and institutional framework put in place in the Republic of South Africa to address money laundering. The chapter seeks to interrogate whether Kenya's laws on money laundering have any gaps which can be addressed through drawing from the best practices in the Republic of South Africa.

¹⁶² *Ibid.*

¹⁶³ Financial Intelligence Centre Act.

¹⁶⁴ This Act is the overarching national anti-terrorism legislation, criminalizing terrorist financing and contains measures.

4.2.1 Criminalisation of Money Laundering

South Africa has criminalised money laundering in three separate provisions of the Prevention of Organised Crime Act (POCA),¹⁶⁵ which cover the conversion or transfer, concealment or disguise, possession, acquisition of property in a manner that is largely consistent with the 1988 United Nations (UN) Convention against Illicit Traffic in Narcotic Drugs and Psychotropic Substances (Vienna Convention) and the 2000 UN Convention against Transnational Organised Crime (Palermo Convention). However, acquisition, possession or use of the proceeds of unlawful activities does not apply to the person who committed the predicate offence. South Africa adopts an all crimes approach which covers a range of 7 offences in each of the 20 designated categories of offences. There is also a broad range of ancillary offences to the money laundering offences. Liability for money laundering extends to both natural and legal persons, and proof of knowledge can be derived from objective factual circumstances. The penalties for money laundering are a fine not exceeding ZAR 100 million or imprisonment for a period not exceeding 30 years.¹⁶⁶

4.2.2 Criminalisation of Terrorist Financing

Terrorist financing is criminalized under Section 4 of the Protection of Constitutional Democracy against Terrorist and Related Activities Act (POCDATARA).¹⁶⁷ This Act is comprehensive and

¹⁶⁵ Prevention of Organised Crime Act, Act No. 121 of 1998. See sections 4, 5 and 6 of the Act.

¹⁶⁶ *Ibid*, s 8.

¹⁶⁷ Protection of Constitutional Democracy against Terrorist and Related Activities Act, Act No. 33 of 2004. This is an Act to provide for measures to prevent and combat terrorist and related activities; to provide for an offence of terrorism and other offences associated or connected with terrorist activities; to provide for Convention offences; to give effect to international instruments dealing with terrorist and related activities; to provide for a mechanism to comply with United Nations Security Council Resolutions, which are binding on member States, in respect of terrorist and related activities; to provide for measures to prevent and combat the financing of terrorist and related activities; to provide for investigative measures in respect of terrorist and related activities; and to provide for

criminalises the collection or provision of property with the intention that it be used for the purpose of committing a terrorist act, or by a terrorist organisation or individual terrorist for any purpose. The term property is broadly defined, and there is no requirement that the property actually be used to carry out or attempt a terrorist act, or be linked to a specific terrorist act.¹⁶⁸ Terrorist financing is also a predicate offence for money laundering. A broad range of ancillary offences also apply to the terrorist financing offence. The maximum penalty, which can apply to natural or legal persons, for conviction of a terror financing offence in the case of a sentence to be imposed by a High Court or a regional court, is a fine not exceeding R100 million or to imprisonment for a period not exceeding 15 years. In the case of a sentence to be imposed by any magistrate's court, to a fine not exceeding R250, 000, 000 or to imprisonment for a period not exceeding five years.¹⁶⁹

4.2.3 Confiscation, Freezing and Seizing of Proceeds of Crime

The relevant law provides for both criminal forfeiture based on conviction and civil forfeiture which is not dependent on a conviction.¹⁷⁰ Overall, the confiscation and forfeiture regime is being effectively implemented, with the statistics demonstrating that the value of the proceeds confiscated is high. The Asset Forfeiture Unit in the National Prosecuting Authority administers and implements the freezing and forfeiture provisions of the POCA which apply to a broad range of proceeds (both direct and indirect) and property of corresponding value. Additionally, the Criminal Procedure Act¹⁷¹ provides for the search, seizure, forfeiture and disposal of the

matters connected therewith.

¹⁶⁸ The term "property" means money or any other movable, immovable, corporeal or incorporeal thing and includes any rights, privileges, claims and securities and any interest therein and all proceeds thereof.

¹⁶⁹ Protection of Constitutional Democracy against Terrorist and Related Activities Act, s 18 (c).

¹⁷⁰ Prevention of Organised Crime Act, s 13.

¹⁷¹ Criminal Procedure Act, Act No. 51 of 1977.

instrumentalities of crime.¹⁷² Any property which may be subject to confiscation or civil forfeiture may be frozen by means of an *ex parte* application.

The provisions of POCDATARA also allow authorities to freeze assets concerning property in respect of which there are reasonable grounds to believe that the property is owned or controlled by or on behalf of, or direction of any entity which has committed, attempted to commit, participated in or facilitated the commission of a specified offence.¹⁷³ The National Director of Public Prosecutions may make an *ex parte* application to a judge in chambers for a freezing order where there are reasonable grounds to believe that the property is related to terrorism. In practice, such a freezing order may be obtained in a matter of hours, is of indefinite duration and may be obtained without commencing a criminal investigation or prosecution in South Africa.

4.2.4 The Financial Intelligence Centre

There is established the Financial Intelligence Centre (“the Centre”) as the national centre for receiving, analysing and disseminating information on suspected money laundering and terrorist financing. The Centre was created under the Financial Intelligence Centre Act (the FIC Act)¹⁷⁴ and became operational on 3rd February, 2003. The Centre has sufficient operational independence and autonomy, and is free from undue influence or interference. The Centre is created as a statutory body with legal personality bestowed with general powers of a body corporate.¹⁷⁵ It is located within the Ministry of Finance and accountable to the Minister for

¹⁷² *Ibid*, s 19-36

¹⁷³ Protection of Constitutional Democracy against Terrorist and Related Activities Act, s 23 as read with section 26 of Prevention of Organised Crime Act.

¹⁷⁴ Financial Intelligence Centre Act, Act No. 38 of 2001.

¹⁷⁵ *Ibid*, s 5. The Centre has the power to determine its own staff establishment and the terms and conditions of employment for its staff within a policy framework determined by the Minister; appoint employees and seconded personnel to posts on its staff establishment; obtain the services of any person by agreement, including any state department, functionary or institution, to perform any specific act or function; acquire or dispose of any right in or to property, but rights in respect of immovable property may be acquired or disposed of only with the consent of the Minister; open and operate its own bank accounts; insure itself against any loss, damage, risk or liability; perform legal acts or institute or defend any legal action in its own name; engage in any lawful activity, whether alone or

Finance. The Centre is an institution outside the public service but within the public administration (as envisaged in Section 195 of the Constitution of the Republic of South Africa) Its mandate was expanded to include the detection of terrorist financing when POCDATARA was passed in the Parliament and amended the FIC Act in 2005. Its specific functions include: inform, advise and cooperate with investigating authorities, supervisory bodies, the South African Revenue Service and the intelligence services; monitor and give guidance to accountable institutions, supervisory bodies and other persons regarding the performance by them of their duties and their compliance with the provisions of the Act; and retain the information gathered to in the manner and for the period required by the Act.

As an administrative body under the Ministry of Finance, the Centre does not have any investigative powers. Rather, its intelligence is meant to support the existing investigative bodies and other role players in the intelligence and criminal justice system. Its principle objective is to assist in identifying the proceeds of unlawful activities, and combating ML, FT and related activities.¹⁷⁶ The other objectives of the Centre include: making information collected by it available to investigating authorities, the intelligence services and the SARS to facilitate the administration and enforcement of South Africa's laws; and exchanging information on money laundering activities and similar offences with similar bodies in other countries.¹⁷⁷

together with any other organisation in the Republic or elsewhere, aimed at promoting its objectives and do anything that is incidental to the exercise of any of its powers.

¹⁷⁶ *Ibid*, s 3 (1). The Centre is registered as a Section 3(a) entity in terms of the Public Finance Management Act, 1999. This means that while the Centre is regarded as an independent entity within the government, it is not bound by the same rules that apply to government departments. Section 3(a) of the Public Finance Management Act provides the Centre with a degree of independence in regards to its functioning, developing its own remuneration framework, policies, staffing and skills requirements, and other policies

¹⁷⁷ *Ibid*, s 3 (2).

The Centre is headed by the Director who is appointed by the Minister for Finance.¹⁷⁸ The Director is the chief executive officer and accounting authority of the Centre in terms of the PFMA which means that the Director is responsible for the formation, development and management of the Centre's administration and the control and maintenance of discipline of the Centre's staff.¹⁷⁹ The sources of the Centre's funds are restricted by law to money appropriated annually by Parliament for the purposes of the Centre, any government grants made to it and any other money legally acquired by it. The Centre may accept donations only with the prior written approval of the Minister.¹⁸⁰ Section 12 of the FIC Act requires that all staff are security vetted before they may be employed by the Centre. In addition, all staff at the Centre are required to sign an oath of secrecy upon contracting to work for the Centre. This is a clear demonstration that the Centre is a well-structured, funded and staffed FIU that is functioning properly.

The Act enjoins any person who carries on a business, manages, or is employed by such business to report to the Centre the suspicious and unusual transactions concerning money laundering and terrorist financing.¹⁸¹

4.2.5 Reporting suspicious transactions

Financial institutions or accountable institutions covered by the FIC Act are prohibited from establishing a business relationship or concluding a single transaction with a customer before establishing and verifying the customer's identity, and the identity of any person acting on behalf of the customer or on whose behalf the customer is acting.¹⁸² Accountable institutions are also

¹⁷⁸ *Ibid*, s 6.

¹⁷⁹ *Ibid*, s 6 and 10.

¹⁸⁰ *Ibid*, s 14.

¹⁸¹ *Ibid*, s 29(1).

¹⁸² Financial Intelligence Centre Act, s 21(1).

required to establish and verify the identity of all customers with whom it had entered into a business relationship before the FIC Act was promulgated.¹⁸³

Financial secrecy provisions do not inhibit implementation of the FATF standards. Accountable institutions are required to keep records of information pertaining to customer identification and transactions whenever they establish a business relationship or conclude any transaction. The records may be kept in electronic form.¹⁸⁴ Such records must be kept for at least five years from the date on which the business relationship is terminated (in the case of a business relationship) or transaction was concluded.¹⁸⁵

In order to curb money laundering, transactions with no apparent business or lawful purpose must be reported to the Centre. However, accountable institutions are not expressly required to pay special attention to transactions based on complexity, size or unusual patterns, or to business relationships and transactions with persons from or in countries which do not or insufficiently apply the FATF Recommendations.¹⁸⁶

It is fair to note that the legal framework on anti-money laundering in the Republic of South Africa presents a broad reporting regime in which all financial institutions and businesses (not just accountable institutions) are required to report suspicious transactions. Overall, the STR reporting regime is being implemented effectively. All suspicious transactions must be reported to the Centre, including attempted transactions, regardless of amount. No criminal or civil action may be brought against a person who files an STR in good faith, and tipping-off is prohibited.¹⁸⁷

Additionally, accountable institutions are required to file Terrorist Property Reports (TPRs) with

¹⁸³ *Ibid*, s 21(2).

¹⁸⁴ *Ibid*, s 22.

¹⁸⁵ *Ibid*, s 23.

¹⁸⁶ *Ibid*, s 29.

¹⁸⁷ *Ibid*. The statistics show that during the 2007/2008 financial year, the Centre received 24 585 STRs. This is a 15% increase in comparison to the 2006/2007 financial year.

the Centre if they have knowledge that property in their possession or control is terrorist related.¹⁸⁸

Accountable institutions are required to formulate and implement internal rules concerning the establishment and verification of the identity of persons whom the institution must identify, the information of which record must be kept, the manner in which and place at which such records must be kept, the steps to be taken to determine when a transaction is reportable to ensure the institution complies with its duties under the Act and any such matters as may be prescribed.¹⁸⁹

Accountable institutions are required to appoint a compliance officer who is responsible for ensuring compliance by employees with the FIC Act. However, with the exception of the banking sector, the compliance officer need not be at the management level.¹⁹⁰ Although the FIC Act does not specifically address the issue of an independent, internal audit function, such requirements do exist in some of the separate financial institutions' legislation. There is no general requirement for financial institutions to put in place screening procedures to ensure high standards when hiring all employees. Accountable institutions are required to provide AML/CFT training.¹⁹¹

4.2.6 Supervision of Banking Institutions

The South African Reserve Bank (SARB) is responsible for supervising banking institutions and overseeing South Africa's exchange control regime-powers which it exercises through its

¹⁸⁸ *Ibid*, s 28 (a).

¹⁸⁹ *Ibid*, s 42.

¹⁹⁰ *Ibid*, s 43.

¹⁹¹ *Ibid*.

Banking Supervision Department and Exchange Control Department.¹⁹² The Financial Services Board (FSB) is responsible for supervising financial advisors and intermediaries including investment managers, the insurance industry, retirement funds, friendly societies, collective investment schemes, exchanges, central securities depositories and clearing houses. The Johannesburg Stock Exchange (JSE) is a licensed exchange and self-regulatory organisation which is responsible for supervising authorised users of the exchange. A limited number of financial institutions are not subject to AML/CFT supervision because they are not defined as accountable institutions pursuant to the FIC Act. As well, there is no designated supervisory authority for the several accountable institutions like Post bank and members of the Bond Exchange.

A natural person as well as a legal person (including directors and/or senior management of a financial institution who are responsible for the institution's contraventions or failures) are liable to criminal sanctions for violating the FIC Act.¹⁹³ The maximum penalties for offences relating to violations of CDD, record keeping and reporting requirements are imprisonment for 15 years or a fine of ZAR 10 million.¹⁹⁴ The other offences attract imprisonment for a period not exceeding 5 years or a fine not exceeding ZAR 1 million. There is no possibility to apply administrative sanctions directly for breaches of the FIC Act. Although the designated supervisors may apply some administrative sanctions, these are not directly applicable for AML/CFT violations and can generally only be applied if those AML/CFT deficiencies rise to

¹⁹² South African Reserve Bank Act, Act No. 90 of 1989, s 10.

¹⁹³ Chapter four of the Act provides a list of offences *inter alia*: failure to keep records, destroying or tempering with information, failure to give assistance to the Centre, failure to report suspicious or unusual cash transactions, unauthorized disclosure, failure to send report to the Centre, failure to report conveyance of cash into or out of Republic, failure to report electronic transfer, misuse of information...

¹⁹⁴ Financial Intelligence Centre Act, s 68 (1).

the level of undesirable business practices, safety and soundness issues, or fit and proper criteria.¹⁹⁵

4.2.7 Designated Non-Financial Business and Professions

The FIC Act applies the same standards to both financial and non-financial businesses and professions. The non-financial institutions are designated as accountable institutions and include attorneys, trust service providers, real estate agents, casinos and public accountants who carry on the business of rendering investment advice or investment brokering services.¹⁹⁶ The AML/CFT preventive measures generally apply to all accountable institutions in the same way, regardless of whether they are financial or non-financial institutions. The obligations to report activity suspected of being related to money laundering or terrorist financing, protection for reporting and the prohibition on tipping off apply to all designated non-financial businesses and professions.¹⁹⁷ The designated non-financial businesses and professions have authorities which supervise their operations regarding the AML/CFT inspections. For casinos, the designated AML/CFT supervisor is the National Gambling Board.¹⁹⁸ For estate agents and public accountants, the designated AML/CFT supervisors are the Estate Agency Affairs Board and the Public Accountants and Auditors Board (now the Independent Regulatory Board for Auditors) respectively.¹⁹⁹ For attorneys (and notaries), the Law Society of South Africa (LSSA) is the designated AML/CFT supervisor.²⁰⁰ However, only the four regional law societies have statutory inspection authority and enforcement power to supervise the conduct of attorneys. This situation

¹⁹⁵ *Ibid.*

¹⁹⁶ *Ibid.*, Schedule 1 lists both financial and designated non-financial businesses and professions as accountable institutions.

¹⁹⁷ *Ibid.*, Part 3.

¹⁹⁸ *Ibid.*, Schedule 2. Established under the National Gambling Act, Act No. 33 of 1996.

¹⁹⁹ *Ibid.* Established under the Estate Agents Act, Act No. 112 of 1976 and Public Accountants and Auditors Act, Act No. 80 of 1991 respectively.

²⁰⁰ *Ibid.*

has stalled implementation of AML/CFT requirements in the legal profession. South Africa should bring into effect as soon as possible provisions that will provide adequate authority for the DNFBP supervisors/monitoring bodies to inspect for and apply a range of sanctions that is effective, proportionate, and dissuasive for non-compliance with the FIC Act.

4.2.8 National and International Co-operation

The relevant authorities in the Republic of South Africa have established effective mechanisms to cooperate on operational matters to combat ML and FT. The Centre has mechanisms in place to exchange information and coordinate with the various stakeholders, and regulators and law enforcement agencies effectively and to cooperate effectively amongst themselves. South Africa has ratified international conventions on money laundering and terrorist financing for instance the Palermo Convention²⁰¹ and the Terrorist Financing Convention²⁰² and the Vienna Convention.²⁰³ It is instructive to note that South Africa has implemented the majority of the conventions' provisions.

South Africa adopts a flexible approach in dealing with mutual legal assistance requests, and is able to render a wide range of mutual legal assistance under the International Cooperation in Criminal Matters Act.²⁰⁴ It is able to render assistance without the need for a treaty or agreement and there is also no requirement for dual criminality or where the request is to obtain evidence, there is no requirement that judicial proceedings should have already been instituted before assistance can be rendered. Assistance is generally provided on the basis of an assurance of reciprocity, but this principle is not interpreted in an overly strict manner.²⁰⁵ Neither the

²⁰¹ Ratified on 20 February 2004.

²⁰² Ratified on 1 May 2003.

²⁰³ Acceded on 14 December 1998.

²⁰⁴ International Cooperation in Criminal Matters Act, Act No. 75 of 1996 available at: <http://www.info.gov.za/gazette/acts/1996/a75-96.htm>, accessed 24th September, 2013.

²⁰⁵ *Ibid*, Chapter 2.

International Co-operation in Criminal Matters Act nor the treaties impose restrictions against requests relating to fiscal matters.²⁰⁶ In addition, the International Cooperation in Criminal Matters Act provides for the confiscation and transfer of proceeds of crime or property of corresponding value through the execution of foreign confiscation orders,²⁰⁷ which are complemented by domestic provisions in the asset forfeiture regime under the POCA, and provisions in the CPA that are used to cover the search and seizure of instrumentalities intended for use in ML, FT and predicate offences.²⁰⁸

The Centre, law enforcement agencies, and supervisors are able to provide a wide range of international co-operation to foreign counterparts, and generally do so in a rapid, constructive, and effective manner. South Africa does not refuse co-operation on the ground that offences also involve fiscal matters. The provisions and practices apply to all criminal conduct including money laundering and terrorist financing.

4.2.9 Resources and Statistics

South African authorities have committed substantial and appropriate human and financial resources to the Centre, police, financial supervisors and prosecutors. The NPA has increased its staff by 27% over the past three years, and receives adequate funding. All competent authorities are required to maintain high professional standards, including standards concerning confidentiality, and receive adequate AML/CFT training.²⁰⁹ In addition, South Africa maintains comprehensive statistics regarding STRs received, analysed, and disseminated, and statistics relating to financial supervisory cooperation. Although this practice is laudable, South African authorities should record and maintain more detailed statistics of money laundering

²⁰⁶ *Ibid.*

²⁰⁷ International Cooperation in criminal Matters Act, s 20.

²⁰⁸ *Ibid.*

²⁰⁹ *Ibid.*

investigations, prosecutions and convictions, so as to be able to more effectively assess the effectiveness of South Africa's AML/CFT system. South Africa should also keep comprehensive statistics of mutual legal assistance and extradition matters. Finally, South Africa should review the effectiveness of its systems for combating money laundering and terrorist financing on a regular basis.²¹⁰

4.3 Combating Money Laundering: The Case of Canada

Canada has a lot of similarities with South Africa, particularly with regard to the advanced financial services sector. Canada is a developed country with a current GDP of 1825.10 billion USD²¹¹ and a population of 35,163,430 people.²¹² Like South Africa, it has a first-world banking sector characterized by well-established infrastructure and technology. Indeed Canada's financial services sector is both diverse and remarkably secure. In 2011, the World Economic Forum rated Canada's banking system the soundest in the world.²¹³ No major Canadian banks failed during the financial crisis of 2008-2009 and Bloomberg Markets magazine listed four Canadian banks among the ten strongest in the world.²¹⁴

Canada's thriving financial services sector includes banks, cooperatives, credit unions, insurance companies and brokers, pension fund managers, securities dealers and independent agencies.

²¹⁰ *Ibid.*

²¹¹ Available at: www.tradingeconomics.com/canada/gdp, accessed 26th August, 2014.

²¹² Available at: <http://worldpopulationreview.com/countries/canada-population> > accessed 26th August, 2014.

²¹³ World Economic Forum Global Competitiveness Report 2012.

²¹⁴ Bloomberg, Canadians Dominate World's 10 Strongest Banks (2012).

The Canadian financial sector is among the world's most well-regulated and is responsible for many international best practices. The World Bank ranks Canada fifth worldwide for its strength of investor protection.²¹⁵

The anti-money laundering legal and regulatory regime in Canada has undergone numerous changes to become what it is today. In 1991, the Proceeds of Crime (Money Laundering) Act was brought into force in Canada to give legal effect to the FATF Forty Recommendations by establishing record keeping and client identification requirements in the financial sector to facilitate the investigation and prosecution of money laundering offences under the Criminal Code of Canada and the Controlled Drugs and Substances Act.

In 2000, the Proceeds of Crime (Money Laundering) Act was amended to expand the scope of its application and to establish a financial intelligence unit with national control over money laundering. The unit is called FINTRAC. In December 2001, the scope of the Proceeds of Crime (Money Laundering) Act was again expanded by amendments enacted under the Anti-Terrorism Act with the objective of deterring terrorist activity by cutting off sources and channels of funding used by terrorists in response to 9/11. The Proceeds of Crime (Money Laundering) Act was renamed the Proceeds of Crime (Money Laundering) and Terrorist Financing Act.

In December of 2006, the Proceeds of Crime (Money Laundering) and Terrorist Financing Act was further amended, in part, in response to pressure from the FATF for Canada to tighten its money laundering and financing of terrorism legislation. The amendments expanded the client identification, record-keeping and reporting requirements for certain organizations and included new obligations to report attempted suspicious transactions and outgoing and incoming

²¹⁵ World Bank Doing Business Guide 2012.

international electronic fund transfers, undertake risk assessments and implement written compliance procedures in respect of those risks.²¹⁶The amendments also enabled greater money laundering and terrorist financing intelligence-sharing among enforcement agencies.

4.3.1 Criminalisation of Money Laundering

The Proceeds of Crime (Money Laundering) and Terrorist Financing Act defines a money laundering offence as an offence under subsection 462.31(1) of the Criminal Code. Money laundering in Canada is therefore criminalized under section 462.31 of the Criminal Code of Canada which provides that everyone commits an offence who uses, transfers the possession of, sends or delivers to any person or place, transports, transmits, alters, disposes of or otherwise deals with, in any manner and by any means, any property or any proceeds of any property with intent to conceal or convert that property or those proceeds, knowing or believing that all or a part of that property or of those proceeds was obtained or derived directly or indirectly as a result of the commission in Canada of a designated offence; or an act or omission anywhere that, if it had occurred in Canada, would have constituted a designated offence.²¹⁷ A person found guilty of the offence of money laundering is liable to imprisonment for a term not exceeding ten years.

Unlike the case in Canada, money laundering is not a recognized offence under the Penal Code in Kenya. The definition of money laundering is to be found solely in the Proceeds of Crime and Anti-money Laundering Act and this is a point of departure from the laws in Canada. Further, whereas a conviction for a money laundering offence in Canada attracts a punishment of ten

²¹⁶ Christine Duhaime, 'Canada implements world's first national digital currency law; regulates new financial technology transactions' (July 2014) available at: <http://www.duhaimelaw.com/2014/06/22/canada-implements-worlds-first-national-bitcoin-law> accessed 30th August, 2014.

²¹⁷ Criminal Code of Canada, s 462.31.

years imprisonment, the same offence attracts a jail term of fourteen years in Kenya with the option of a fine.²¹⁸

4.3.2 Criminalisation of Terrorist Financing

Financing of terrorist activity is criminalized under Section 83 of the Criminal Code in Canada. Section 83.03 of the Code provides that everyone who, directly or indirectly, collects property, provides or invites a person to provide, or makes available property or financial or other related services intending that they be used, or knowing that they will be used, in whole or in part, for the purpose of facilitating or carrying out any terrorist activity, or for the purpose of benefiting any person who is facilitating or carrying out such an activity, or knowing that, in whole or part, they will be used by or will benefit a terrorist group, is guilty of an indictable offence and is liable to imprisonment for a term of not more than 10 years.²¹⁹

Under the Kenya Proceeds of Crime and Anti-money Laundering Act, there is no mention of terrorist financing and neither is it mentioned in the Money Remittance Regulations of 2013. The Kenya Penal Code does not also recognize terrorism as a criminal offence and consequently it does not provide for terrorism financing.

4.3.3 Confiscation, Freezing and Seizing of Proceeds of Crime

The Canada Proceeds of Crime (Money Laundering) and Terrorist Financing Act does not provide for confiscation, freezing or seizing of proceeds of crime except for the seizure of monetary instruments and currency that has not been disclosed by persons crossing the border.

Section 12 (1) of the Proceeds of Crime (Money Laundering) and Terrorist Financing Act requires reporting of importation or exportation of currency or monetary instruments of a value

²¹⁸ Proceeds of Crime and Anti-money Laundering Act, s 17 (1) (a).

²¹⁹ Criminal Code of Canada, s 83.03.

equal to or greater than the prescribed amount.²²⁰ The prescribed amount under the Cross-border Currency and Monetary Instruments Reporting Regulations is 10,000 Canadian dollars.²²¹

4.3.4 The Financial Transactions and Reports Analysis Centre (FINTRAC)

The Financial Transactions and Reports Analysis Centre of Canada (FINTRAC) is the financial intelligence unit for Canada that was created in 2000 following amendment of the Proceeds of Crime (Money Laundering) Act. FINTRAC is an independent federal government agency that reports to the Minister of Public Safety and Emergency Preparedness and the Minister of Finance.

FINTRAC has four objectives:

- 1. To collect, analyse, assess and disclose information to assist in the detection, prevention and deterrence of money laundering and terrorist financing;*
- 2. To ensure that personal information under its control is protected from unauthorized disclosure;*
- 3. To enhance public awareness and understanding of matters related to money laundering; and*
- 4. To ensure compliance with the record keeping, verifying identity, reporting and registration requirements of the Proceeds of Crime (Money Laundering) and Terrorist Financing Act.*

FINTRAC occupies an important position in the constellation of organizations involved in Canada's fight against money laundering and terrorism. Each of these organizations has a particular relationship with FINTRAC. Due to the nature of its mandate, the Centre's work is

²²⁰ Proceeds of Crime (Money Laundering) and Terrorist Financing Act, s 12 (1).

²²¹ Cross-border Currency and Monetary Instruments Reporting Regulations, s 2 (1).

situated at the beginning of a process that starts with the reports to FINTRAC by financial institutions and intermediaries. With the assistance of specialized automated tools, skilled staff analyze the reported transactions and information from other sources to extract financial intelligence that would be relevant to the investigation or prosecution of money laundering offences, terrorist activity financing offences, and threats to the security of Canada.

Money laundering and terrorist financing cases can be extremely complex, often involving many players implicated in transnational and covert illicit activity. The investigations are often time and resource intensive. For this reason, the time between FINTRAC's initial disclosure and the conclusion of an investigation can be quite lengthy.

FINTRAC's core product is case-specific financial intelligence. FINTRAC is also well situated to provide strategic intelligence about trends and typologies of money laundering and terrorist financing. Because money laundering and terrorist financing are almost always transnational in character, and because an important part of FINTRAC's role is to exchange information with like bodies in other countries, it is also well placed to provide a strategic overview from an international perspective.

The Centre has signed information exchange agreements with certain foreign FIUs worldwide, enabling it to provide financial intelligence to its counterparts that can be crucial to investigations of cases involving the international movement of funds. Equally, it can receive information from these FIUs, which is useful to its own analysis.

When FINTRAC is satisfied that it has reasonable grounds to suspect that the information would be relevant to such investigations or prosecutions, it discloses this financial intelligence to law

enforcement and/or intelligence agencies. These agencies, where appropriate, conduct investigations, and if warranted, bring charges against the individuals involved. The recipients of the intelligence include Royal Canadian Mounted Police (RCMP), provincial and municipal police agencies, CSIS, CRA, CIC and foreign FIUs with which the Centre has a Memorandum of Understanding (MOU) for the exchange of information. Reports are also made to the Canada Border Services Agency in cases where the information may be relevant to determining if a foreign national is inadmissible to Canada under the Immigration and Refugee Protection Act, or relevant to investigating or prosecuting an offence of smuggling and to the Canadian Security Intelligence Service if FINTRAC has reasonable grounds to suspect that designated information would be relevant to threats to the security of Canada.

Since 30th December, 2008, FINTRAC has legislative authority to issue an administrative monetary penalty (AMP) to reporting entities that are in non-compliance with Canada's Proceeds of Crime (Money Laundering) and Terrorist Financing Act.

With regard to criminal penalties, FINTRAC may disclose cases of non-compliance to law enforcement when there is extensive non-compliance or little expectation of immediate or future compliance. Criminal penalties may include:

1. Failure to report suspicious transactions: up to \$2 million and/or 5 years imprisonment;
2. Failure to report a large cash transaction or an electronic funds transfer: up to \$500,000 for the first offence, \$1 million for subsequent offences;

3. Failure to meet record keeping requirements: up to \$500,000 and/or 5 years imprisonment;
4. Failure to provide assistance or provide information during compliance examination: up to \$500,000 and/or 5 years imprisonment; and
5. Disclosing the fact that a suspicious transaction report was made, or disclosing the contents of such a report, with the intent to prejudice a criminal investigation: up to 2 years imprisonment.

FINTRAC is not an investigative body and it does not have powers to gather evidence, lay charges, seize and freeze assets or create watch lists of suspected money launderers or terrorist financiers. Likewise, it does not investigate or prosecute suspected offences. It does, however, conduct reviews and audits of reporting entities and may assess penalties for violations of the Proceeds of Crime (Money Laundering) and Terrorist Financing Act. To the extent that the Kenya Financial Reporting Centre does not have investigative or prosecutorial powers, the two bodies function in a similar manner.

4.3.5 Reporting suspicious transactions

Section 3 of the Proceeds of Crime (Money Laundering) and Terrorist Financing Act highlights a key object of the Act as requiring the reporting of suspicious financial transactions and of cross-border movements of currency and monetary instruments.²²²

Section 7 of the Act makes it a requirement for banks and foreign banks, cooperative credit societies, savings and credit unions, life companies, loan companies, financial investments

²²² Proceeds of Crime (Money Laundering) and Terrorist Financing Act, s 3.

companies, foreign exchange dealers, casinos and precious metals to report to the Centre, every financial transaction that occurs or that is attempted and there are reasonable grounds to suspect that the transaction is related to the commission or the attempted commission of a money laundering offence or the commission or the attempted commission of a terrorist activity financing offence.²²³

The reporting institutions envisaged and outlined in the Proceeds of Crime (Money Laundering) and Terrorist Financing Act are varied and wide ranging covering all sectors that transact in money and money equivalents. Kenya appears to have borrowed from the Canada Act as it lists a similar portfolio of envisaged reporting institutions.

Tipping off is prohibited under Section 8 of the Act which carries a penalty of imprisonment not exceeding two years on conviction. Section 9.2 also prohibits enlisting of a person as a customer if his/her identity cannot be established. Section 6 of the Act requires reporting institutions to retain and verify records in accordance with the Proceeds of Crime (Money Laundering) and Terrorist Financing Regulations. Violating this provision attracts a penalty of \$50,000 or to imprisonment for a term of not more than six months or both.

A key departure from the Kenya Proceeds of Crime and Anti-money Laundering Act is the recognition of Politically Exposed Persons (PEPs) under Section 9.3 of the Canada Act. The Act defines a “politically exposed person” as a person who holds or has held one of the following offices or positions in or on behalf of a foreign state: head of state or head of government, member of the executive council of government or member of a legislature, deputy minister or equivalent rank, ambassador or attaché or counsellor of an ambassador, military officer with a

²²³ *Ibid*, s 7.

rank of general or above, president of a state-owned company or a state-owned bank, head of a government agency, a judge or leader or president of a political party represented in a legislature. This definition includes family members of such a person. The approval of senior management of the reporting institution is required before any dealings with a PEP are undertaken.

4.3.6 National and International Co-operation

The Act under Section 53.3 allows FINTRAC to share information and intelligence gathered with governments of foreign states, an international organization established by the governments of foreign states, or an institution or agency of a foreign state that has powers and duties similar to those of the Centre. This provision, however, requires the Director of FINTRAC to seek the consent of the Minister for Finance before making such a disclosure.

Section 56.1 (1) of the Act further provides that FINTRAC may disclose designated information to an institution or agency of a foreign state or of an international organization established by the governments of foreign states that has powers and duties similar to those of the Centre, if the Centre has reasonable grounds to suspect that the information would be relevant to the investigation or prosecution of a money laundering offence or a terrorist activity financing offence, or an offence that is substantially similar to either offence. There is, however, a proviso that requires the Minister to have entered into an agreement or arrangement with that foreign state or international organization regarding the exchange of such information.²²⁴

Kenya too has legal provisions that allow for exchange of information with international bodies on matters of anti-money laundering. Section 24 (2) (b) of the Kenya Proceeds of Crime and Anti-money Laundering Act provides that the Financial Reporting Centre shall exchange

²²⁴ *Ibid*, s 56.1 (1).

information with similar bodies in other countries regarding money laundering activities and related offences.²²⁵

4.4 Conclusion

Besides providing a comparative analysis of the anti-money laundering legal, institutional and regulatory framework in Kenya vis-a-vis Canada and South Africa, this chapter has provided insight and learning points for Kenya to explore as it seeks to enhance its anti-money laundering initiatives and agenda. There are significant differences between Kenya's approach to money laundering and terrorism financing and the approaches employed in South Africa and Canada. South Africa and Canada have the advantage of being more developed economically and socially than Kenya and consequently are more advanced in terms of technology and specialized expertise.

The issue of financial resources, for example, can be cited as one that has brought about the gaps identified at Kenya's Financial Reporting Centre with regard to human and technical resources. The South African intelligence centre, for instance, enjoys generous funding, is staffed with very competent staff and enjoys a lot of support from the accountable institutions. It has collated statistics that can be used to demonstrate that since its inception it has achieved commendable results. Canada on the other hand has been fighting money laundering since 1991 whereas Kenya enacted its first substantive anti-money laundering law in 2009, close to two decades later. The Canadian anti-money laundering regime is quite robust and sound with strong institutions and equally strong laws to support them.

²²⁵ Proceeds of Crime and Anti-money Laundering Act, s 24 (2) (b).

The purpose of this chapter was therefore to identify legal provisions and institutional modalities of operation that Kenya can borrow from the two jurisdictions to enhance its own legal provisions, build institutional capacity and promote compliance with the law.

The next chapter of this thesis makes specific recommendations for legal and institutional reform.

CHAPTER FIVE

RECOMMENDATIONS FOR LEGAL AND INSTITUTIONAL REFORM

5.1 Overview

My conclusion at the end of this research project is that the current anti-money laundering legal and regulatory framework in Kenya is inadequate to address the growing problem of money laundering. The inadequacy stems from weaknesses in legal provisions as well as institutional deficiencies. It is important to acknowledge that Kenya and indeed the world cannot eradicate money laundering 100%. It is also imperative to note that even Canada and South Africa who we seek to emulate are themselves not free from money launderers and money laundering activity. Developed states have to continuously explore areas of improvement to keep pace with the evolving money laundering trends,

The synchronized suicide attacks of 11th September, 2001, highlighted the critical role financial and logistical support networks play in the operations of international terrorist organizations. The challenge in tackling these networks, however, is that they are well-entrenched, sophisticated, and often shrouded in a veil of legitimacy (such as operating under the camouflage of purportedly charitable or humanitarian activity).²²⁶

It is imperative to note that even for the most developed countries in the globe, implementation and enforcement of anti-money laundering and anti-terrorist financing initiatives has not been easy. For example, a mutual evaluation conducted by FATF on Canada in 2008 highlighted the shortcomings enumerated below:

²²⁶ Matthew Levitt, 'Stemming the Flow of Terrorist Financing: Practical and Conceptual Challenges' (2003) available at: <http://www.washingtoninstitute.org/policy-analysis/view/stemming-the-flow-of-terrorist-financing-practical-and-conceptual-challenge>, accessed 30th August, 2014.

1. Canadian law that requires an intent mental element to prove the money laundering offence was inconsistent with the FATF Recommendations;
2. Canada did not have a sufficient number of prosecutions for money laundering offences’
3. Canada did not have a sufficient number of prosecutions for terrorist financing offences;
4. Canada’s and the UN’s lists of terrorists and terrorist organizations was not well communicated in Canada;
5. There were serious issues with respect to the effectiveness of FINTRAC because the number of staff is low, and law enforcement agencies had negative feedback on the value of disclosures by FINTRAC;
6. Police forces in Canada had financial and other constraints that limited their ability to investigate money laundering and terrorist financing activities. In the case of the RCMP, it focuses its efforts mainly on large, complex money laundering cases related to organized crime due to constraints on resources. The mutual evaluation recommended that judges and the courts be instructed on money laundering and terrorist financing generally;
7. Several entities that provided financing services were not caught by the anti-money laundering legislation, such as factoring arrangements, finance leasing services, businesses that issue credit cards, equipment financiers and providers of e-money and Internet services;
8. The required methods for reporting entities to ascertain identity were inadequate;
9. Canada had no legislative provisions to deal with politically exposed persons or correspondent banking relationships;
10. Canada did not have legislation to prevent bank secrecy;

11. Canada did not have legislation to record, monitor and report wire funds transfers above a certain threshold;

12. Canada had no requirement that complex large transactions be monitored by financial institutions;

13. FINTRAC performed an insufficient number of examinations of reporting entities except for banks;

14. The securities industry was minimally (if at all) supervised by provincial securities regulators. The same was found in connection with life insurance companies;

15. FINTRAC had not yet criminally charged reporting entities or their directors and officers;

16. Although illegal, Internet casinos were not caught by the anti-money laundering legislation in Canada (such casinos are only illegal if not conducted and managed by a provincial government under the Criminal Code);

17. Internet servers that provide services to illegal Internet casinos should be shut down by Canada;

18. The legislation applicable to casinos, real estate agents and accountants was not compliant with the FATF Recommendations;

19. FINTRAC could not effectively monitor the application of the legislation of non-financial reporting entities because of limited resources;

20. Casinos should be supervised more closely with on-site examinations;

21. Corporate registry systems do not permit persons to find out beneficial information;
and

22. Trust information should be made available to law enforcement agencies.

This Canadian situation demonstrates that the fight against money laundering and terrorist financing is an ongoing one and because money laundering and terrorism are evolving in nature, the legal and enforcement regime must move with speed and not lag behind.

The Financial Action Task Force on Money Laundering (FATF) has, in fact, laid the groundwork for establishing a baseline of international standards for combating terrorist financing. FATF, the inter-governmental body co-chaired by the United States and Spain and focused on developing and promoting national and international policies to combat money laundering, issued a list of eight “special recommendations” on curbing terrorist financing as a starting point for governments, as well as a report offering guidance to financial institutions on detecting the techniques and mechanisms used in the financing of terrorism.

The Financial Action Task Force’s eight special recommendations²²⁷ are:

- a. Ratifying and implementing UN instruments;
- b. Criminalizing the financing of terrorism and associated money laundering;
- c. Freezing and confiscating terrorist assets;
- d. Reporting suspicious transactions related to terrorism;
- e. Formalizing greater international cooperation through treaties or other Agreements;
- f. Licensing and registering businesses engaged in alternative forms of remittance;
- g. Requiring accurate and meaningful originator data for wire transfers; and
- h. Reviewing the adequacy of laws regulating non-profit organizations.

²²⁷ *Ibid.*

5.2 Reforming the law

5.2.1 Definition of money laundering and aiding offences

The definition of money laundering under the Proceeds of Crime and Anti-money Laundering Act is covered under Sections 3, 4, 5 and 8. The definition is lengthy, too wide and too general and is therefore open to misinterpretation. Money laundering is also not defined as an offence under any other law in Kenya despite being an offshoot or consequential offence ensuing from other crimes such as terrorism, drug trafficking and poaching.

Borrowing from the Canada example and pursuant to the first of the forty 2003 FATF recommendations and second of the eight special FATF recommendations,²²⁸ Kenya should consider amending the Penal Code to include money laundering as an offence and to elevate it to the realm of other criminal acts stipulated in the Penal code.

Besides prescribing sanctions for laundering of money whose source is criminal in nature, the Proceeds of Crime and Anti-money Laundering Act should be revised to also take into account and address the use of legitimately acquired money to fund illegal activity such as terrorism and wildlife poaching. Another key handicap of the Proceeds of Crime and Anti-money Laundering Act as it stands presently is that it is more reactive than proactive. It prescribes sanctions for events occurring after the fact but makes no provisions that can enhance and facilitate the detection of planned money laundering so that it is forestalled before it occurs. The Act in Section 45 (2) allows seven days within which a suspected money laundering event should be escalated to the Financial Reporting Centre.²²⁹ The problem with this allowance is that within

²²⁸ Available at: <http://www.fatf-gafi.org/media/fatf/documents/FATF%20Standards%20-%2040%20Recommendations%20rc.pdf>, accessed 4th September, 2014.

²²⁹ Proceeds of Crime and Anti-money Laundering Act, s 45 (2).

seven days, money that is undergoing laundry can move in a very complex and intricate web to the point of losing trail. Kenya should consider revising the Act to allow momentary freezing of funds suspected to be undergoing laundry and to shorten the time period within which a reporting institution must escalate the incident. This may help to forestall a money laundering eventuality.

Profiling and closer monitoring of Politically Exposed Persons and terrorism suspects is key for timely detection of money laundering activity. It is a requirement of FATF that every cooperating country and territory retains and regularly updates a Politically Exposed Persons (PEPs) list. Unfortunately, the Proceeds of Crime and Anti-money Laundering Act has no provision on maintenance of a PEPs list.

5.2.2 Stricter penalties for terrorist financing

Terrorism and terrorist financing are prohibited in Kenya under the Prevention of Terrorism Act of 2012. Section 4 of the Act provides that a person who carries out a terrorist act commits an offence and is liable, on conviction, to imprisonment for a term not exceeding thirty years.²³⁰ Where a person carries out a terrorist act which results in the death of another person, such person is liable, on conviction, to imprisonment for life.²³¹ Terrorism financing under Section 6 however carries a lesser punishment of twenty years imprisonment. It is not clear why the financiers of terrorism are treated with leniency and yet they are the facilitators and engines of terrorism without whose help terrorism may not occur.

²³⁰ Prevention of Terrorism Act 2012, s 4 (1).

²³¹ *Ibid*, s 4 (2).

According to Matthew Levitt in *Stemming the flow of terrorist financing: practical and conceptual challenges*, “terrorists raise funds through a variety of businesses, criminal enterprises, and front organizations, each of which is significant in its own right, and all the more so when applied in tandem. Purportedly charitable and humanitarian organizations, however, have played a particularly disturbing role in terrorist financing and present an especially sensitive challenge, as authorities are faced with a difficult task of discerning between legitimate charity organizations, those unknowingly hijacked by terrorists who divert funds to finance terrorism, and others proactively engaged in supporting terrorist groups.”²³²

5.2.3 Classification and risk profiling for reporting institutions

Part 1, Section 5 of the Proceeds of Crime (Money Laundering) and Terrorist Financing Act clearly outlines the institutions that are subject to the reporting requirements of the Act. They include: authorized foreign banks within the meaning of Section 2 of the Bank Act in respect of their business in Canada, or banks to which that Act applies; cooperative credit societies, savings and credit unions and *caisses populaires* regulated by a provincial Act and associations regulated by the Cooperative Credit Associations Act; life companies or foreign life companies to which the Insurance Companies Act applies or life insurance companies regulated by a provincial Act; companies to which the Trust and Loan Companies Act applies; trust companies regulated by a provincial Act; loan companies regulated by a provincial Act; persons and entities authorized under provincial legislation to engage in the business of dealing in securities or any other financial instruments or to provide portfolio management or investment advising services, other than persons who act exclusively on behalf of such an authorized person or entity; persons and

²³² Matthew Levitt, ‘*Stemming the Flow of Terrorist Financing: Practical and Conceptual Challenges*’ (2003) available at: <http://www.washingtoninstitute.org/policy-analysis/view/stepping-the-flow-of-terrorist-financing-practical-and-conceptual-challenge>, accessed 30th August, 2014.

entities engaged in the business of foreign exchange dealing, of remitting funds or transmitting funds by any means or through any person, entity or electronic funds transfer network, or of issuing or redeeming money orders, traveller's cheques or other similar negotiable instruments except for cheques payable to a named person or entity; persons and entities engaged in a business, profession or activity described in regulations made under paragraph 73(1)(a); persons and entities engaged in a business or profession described in regulations made under paragraph 73(1)(b), while carrying out the activities described in the regulations; casinos, as defined in the regulations, including those owned or controlled by Her Majesty; departments and agents of Her Majesty in right of Canada or of a province that are engaged in the business of accepting deposit liabilities, that sell money orders to the public or that sell prescribed precious metals, while carrying out the activities described in regulations made under paragraph 73(1)(c); and for the purposes of section 7, employees of a person or entity referred to in any of paragraphs (a) to (l).

In addition to Part 1 of the Act, Sections 2.1 to Section 8 of the Proceeds of Crime (Money Laundering) and Terrorist Financing Suspicious Transaction Reporting Regulations provides greater detail in respect of application of Part 1 of the Act by describing the various activities and sub sectors which will be considered as being reporting institutions as outlined in Part 1 of the Act. For example, Section 5 of the Proceeds of Crime (Money Laundering) and Terrorist Financing Suspicious Transaction Reporting Regulations provides that every dealer in precious metals and stones that engages in the purchase or sale of precious metals, precious stones or jewellery in an amount of \$10,000 or more in a single transaction, other than such a purchase or sale that is carried out in the course of, in connection with or for the purpose of manufacturing jewellery, extracting precious metals or precious stones from a mine or polishing or cutting

precious stones, is subject to Part 1 of the Act. This provision brings into the ambit of precious stones dealers anyone or any entity that carries out a single precious metals transactions whose value is \$ 10,000 and above.

The Kenya Proceeds of Crime and Anti-money Laundering Act on the other hand defines a reporting institution as a financial institution and designated non-financial business and profession.²³³ The Act further defines “designated non-financial businesses or professions” as: casinos (including internet casinos); real estate agencies; dealing in precious metals; dealing in precious stones; legal professionals and accountants, who are sole practitioners or are partners in their professional firms; such other business or profession in which the risk of money laundering exists as the Minister may, on the advice of the Centre, declare.²³⁴ This list of designated non-financial businesses and professions is not exhaustive and omits key players in the commercial world such as accountants, foreign exchange bureaus and mobile money transfer agencies.

Kenya should therefore consider expanding the list of reporting institutions to factor in players in the money markets who have been omitted in the two classifications currently provided for in the Act.

5.2.4 Due diligence requirements

Section 46 and 47 of the Proceeds of Crime and Anti-money Laundering Act require all reporting institutions to verify the identity of the customers and to establish and maintain customer records. Section 46 in particular requires a reporting institution to carry out thorough due diligence procedures prior to accepting an individual or an entity as a customer. Such due diligence is to be aided by the production of official identity records such as birth certificates, national identity cards, passports and driving licences. Whereas this is a commendable provision

²³³ Proceeds of Crime and Anti-money Laundering Act, s 2.

²³⁴ *Ibid*, s 2.

for purposes of enforcing KYC requirements as required by the FATF 40 recommendations, it poses a great challenge for reporting institutions which have to rely entirely on other government departments to validate authenticity of identification documents and particulars.

The Proceeds of Crime and Anti-money Laundering Act does not provide in detail the steps or procedures that a reporting institution should undertake or follow to satisfy itself that the documents availed by a potential customer are genuine and valid. The law leaves it upon the reporting institution to decide the means by which it will verify the identity of an incoming customer thereby creating a loophole in the manner in which such verification is to be undertaken.

The Canada Proceeds of Crime (Money Laundering) and Terrorist Financing Regulations under Section 53 requires all reporting institutions to ascertain the identity of every person with whom the person or entity conducts a transaction. The Proceeds of Crime (Money Laundering) and Terrorist Financing Regulations further prescribe the measures to be undertaken when dealing with a PEP including timelines for reporting and extra measures to ascertain that the transaction undertaken by a PEP is not a money laundering event.

In line with recommendation 6 of the forty FATF recommendations,²³⁵ Kenya, in the Proceeds of Crime and Anti-money Laundering Act, does not make provision for handling of Politically Exposed Persons. The Act should be revised to factor in the risk exposure posed by PEPs and prescribe measures to handle PEP transactions.

²³⁵ Available at: <http://www.fatf-gafi.org/media/fatf/documents/FATF%20Standards%20-%2040%20Recommendations%20rc.pdf>, accessed 4th September, 2014.

5.2.5 Formulation of regulations to complement the law

Whereas the Proceeds of Crime and Anti-money Laundering Act in Section 134 (1) envisaged that the Minister would formulate regulations to compliment the Act²³⁶, so far none has been formulated and the only regulations in place at the moment are the Proceeds of Crime and Anti-money Laundering Regulations 2013 and the Money Remittance Regulations 2013 both of which were formulated by the Central Bank of Kenya. Presently, Canada has five regulations that compliment various provisions of the Proceeds of Crime (Money Laundering) and Terrorist Financing Act by acting as guidelines on mandatory requirements to enhance and facilitate compliance with the law. The five regulations are:

1. The Proceeds of Crime (Money Laundering) and Terrorist Financing Suspicious Transaction Reporting Regulations which prescribes the entities that are subject to Part I of the Act, the information that must be in a suspicious transaction report and a terrorist property report, the time limits and the format of the reports and the "designated information" which FINTRAC can disclose;

2. The Proceeds of Crime (Money Laundering) and Terrorist Financing Regulations which prescribes customer identification requirements, record keeping requirements, transactions that must be reported (such as large cash transactions, electronic funds transfers and casino disbursements) and compliance regime requirements;

3. The Cross-Border Currency and Monetary Instruments Reporting Regulations which defines "monetary instruments", prescribes the reporting threshold at \$10,000 and prescribes the form and manner for reporting to CBSA;

²³⁶ Proceeds of Crime and Anti-money Laundering Act, s 134 (1).

4.The Proceeds of Crime (Money Laundering) and Terrorist Financing Registration Regulations which came into force on June 23 2008 and prescribes applications, notifications, clarifications and supplementary information for money services business (MSB) registration; and

5. The Proceeds of Crime (Money Laundering) and Terrorist Financing Administrative Monetary Penalties Regulations which came into force on December 30 2008 and sets out the specific violations and the classification of those violations as minor, serious or very serious.

There is need for Kenya, through the Minister of Finance, to put in place regulations that can help address some of the deficiencies that currently exist in the Act with respect to provision of proper reporting guidelines, due diligence performance guidelines, definition of vague terms, thresholds and timelines and categorization or classifications of reporting institutions depending on size and type of business and industry or sector of institution. In particular, guidelines should be formulated to address the following:

- a) Reporting requirements to define and categorize the various reporting institutions according to risk profile, size and nature of business and the different thresholds for reporting. This guideline should also clearly spell out what is reportable, the timelines for reporting and the format for reporting to standardize practice across the reporting institutions;
- b) Preparation, maintenance and close monitoring of Politically Exposed Persons, suspected terrorists and other persons of interest;
- c) Instituting of proactive measures to enhance early detection of planned or intended;

- d) Submission by the reporting institutions to the Financial Reporting Centre of periodical audit reports of their compliance levels with the Act. At the moment, there is no enforcement mechanism to ensure that all reporting institutions are carrying out due diligence as required and monitoring transactions going through their systems for suspicious elements;
- e) Thresholds for proving of predicate money laundering offences such as tipping off and obstructing justice. The provisions of the Act as they stand presently make it very difficult to prove an offence of tipping off or obstructing justice;
- f) Due diligence and the need to know your customer before and during the subsistence of a customer-institution relationship. Although the Act prescribes a due diligence requirement, there is no guidance on how the particulars of customers should be collected, verified and stored and this has created a loophole on enforcement;
- g) Standards and thresholds to be used in distinguishing a malicious report from an erroneous report. The law does not provide any clear guidance on differentiating between the two; and
- h) Conveyance of monetary instruments from Kenya and into Kenya. The guideline should clearly spell out that conveyance may be physical or electronic to take into account the onset of electronic funds transfer and online banking. Kenya should also consider revising the limit from USD 10,000 to a higher amount.

The Proceeds of Crime and Anti-money Laundering Act does not guarantee persons who report money laundering activity any protection in the event of civil or criminal litigation. This in itself negates the spirit of the provision whose purpose must have been to encourage reporting by removing fear of victimization and reprisals. Kenya should consider revising the Act to offer

absolute protection to persons who report suspected money laundering activity whether or not it materializes. This is because a person or group of persons against who such a report is made may never get to know of the report if it turns out to be a clean transaction and consequently, such a person or group of persons would have suffered no harm.

The KES 1 million fine prescribed for money laundering offenders is unrealistically low granted that the typical money launderer is a drug trafficker, politician, terrorist or poacher. The negligible amount cannot serve to deter money laundering.

5.3 Institutional reform

The Proceeds of Crime and Anti-money Laundering Act currently provides for the establishment of two institutions, namely the Financial Reporting Centre and the Assets Recovery agency. Although the Financial Reporting Centre became operational in April 2012, it continues to operate below capacity with less than 10 employees. The Asset Recovery Agency on the other hand is yet to be operationalized.

5.3.1 The Financial Reporting Centre

The Financial Reporting Centre became operational on 12th April, 2012. The Proceeds of Crime and Anti-money Laundering Act does not afford the Financial Reporting Centre any investigative or prosecutorial powers. As a result, the Centre is highly dependent on other institutions such as the Police and the Director of Public Prosecutions office to execute its mandate fully. Money laundering offences require detailed and sometimes intensive investigations that may extend long periods of time as networks and patterns are established. Relying on other entities to dedicate the time and financial resources required to undertake such

investigations may be futile and that might explain why Kenya has not seen a single case of a successfully prosecuted money laundering case. Kenya should consider revising the Act to give the Financial Reporting Centre some investigative powers to enable them move with speed and investigate incidents as soon as they are brought to their attention by reporting institutions.

Just like the Financial Reporting Centre, the Financial Transactions and Reports Analysis Centre of Canada does not have investigative powers. Nevertheless, the investigative agencies in Canada are better equipped in terms of numbers, technology and finances to conduct speedy investigations with faster outcomes. According to the FINTRAC Annual Report 2013, 20 million suspicious transactions reports were received by the Centre for assessment.²³⁷ By applying sophisticated analytical techniques to the data holdings, FINTRAC is able to identify emerging characteristics, trends and patterns used by criminals to launder money or fund terrorist activities. This intelligence is then shared domestically and internationally in the form of classified assessments, briefs and reports that identify threats, risks and vulnerabilities.²³⁸

5.3.2 The Anti-money laundering Advisory Board

The Anti-money laundering Advisory Board is established under Section 50 of the Proceeds of Crime and Anti-money Laundering Act. Although the Act spells out the role and mandate of the Board as being advisory in nature²³⁹, the nature of the advice to be given is not stated and the provision is therefore very vague. The criteria used to determine the composition of the Board also leaves a lot to be desired as it doesn't seem to be based on skill, expertise or experience. Kenya should consider revising the law to provide for inclusion in the Advisory Board of individuals well versed with money laundering matters and who can inject some specialized anti-

²³⁷ FINTRAC annual report 2013.

²³⁸ *Ibid*

²³⁹ Proceeds of Crime and Anti-money Laundering Act. s 51.

money laundering skill and expertise into the Advisory Board to enhance performance and capacity of the Financial Reporting Centre.

5.3.3 The Assets Recovery Agency

Section 54 of the Proceeds of Crime and Anti-money Laundering Act envisaged establishment of the Assets Recovery Agency.²⁴⁰ This Agency which was envisaged to be a semi-autonomous body under the office of the Attorney General has not been set up. Its main mandate is to confiscate, seize and recover assets procured from proceeds of crime.

Granted the huge mandate bestowed upon this agency and the fact that it is totally dependent on the outcome of investigations conducted by other law enforcement agencies such as the Police, Kenya should consider revising the law to place the agency as a unit under the Police or the office of the Director of Public Prosecutions.

5.4 Conclusion

The anti-money laundering crusade which was in the beginning just a concept has now gained momentum across the globe. In order to access the global money markets and play in the global commercial arena, developing countries such as Kenya, which is considered the hub for trade and finance in East Africa,²⁴¹ have no option but to comply with the requirements of the more developed nations as spearheaded by FATF. Kenya has taken a significant step in promulgating the Proceeds of Crime and Anti-money Laundering Act but a lot still needs to be done in terms of reforming the law and enhancing the capacities of the ensuing institutions.

The objective of this research was to assess the practicability of enforcing the proceeds of crime and anti-money laundering law in Kenya to curb money laundering and organized crime. The

²⁴⁰ *Ibid*, s 54 (1).

²⁴¹ Available at: <http://www.bankersacademy.com/resources/free-tutorials/324-aml-kenya> accessed 8th September, 2014.

thesis has demonstrated the inadequacies and weaknesses that have made effective and practical enforcement of the law difficult. To address the weaknesses, the study has outlined some of the measures, though not exhaustive, that can be undertaken to enhance the legal provisions of the Act in order to elevate the law to the point where compliance and enforcement will be easier and more practical.

The hypothesis of this study was that the Proceeds of Crime and Anti money laundering Act has not been effective at curbing money laundering and organized crime in Kenya and there is therefore need for law reform in this area. Since the enactment and coming into force of the law, there has not been any successful money laundering investigation or prosecution. The research hypothesis has been proved to be accurate.

I must point out that although adopting and implementing the recommendations outlined in this thesis may not completely cure the inadequacies of the law, the measures will definitely go a long way in creating and building institutional capacity, enhancing money laundering detection capabilities, promoting legal compliance and improving chances of successful prosecutions.

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