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White Paper

Malaysia - Insights into corporate risk: The impact of being non-compliant

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Managing corporate risk is more time-consuming than ever, especially for those risk managers trying to keep pace with the compliance industry. Regulatory frameworks are evolving into complex systems of rules and obligations that affect an ever-widening pool of entities and individuals. The costs for reporting organisations have been tremendous. A report published in 2018 by the International Federation of Accountants and the OECD said, that during the past five years, 51 percent of financial institutions have had to redirect resources from investment to risk management in order to comply with different regulations in multiple jurisdictions – this has cost these entities between 5 and 10 percent of their annual turnover.[1]

Corporate risk can be both jurisdictional and sectoral. Jurisdictional risks originate from geographical, economic and governmental specifics – a strategic geographic location with good transport links will facilitate trade, which then introduces the risk of trade-based money laundering. Open borders and weak border controls can result in customs violations, drug smuggling and human trafficking. Free movement of people can stimulate tourism, but it can also aid terrorism, including the relocation of foreign fighters. This threat has become more pronounced during the past five years due to the rise of the so-called Islamic State, which has attracted supporters from more than 80 countries.[2] If a country has a diversified financial sector, there are risks associated with financial crimes. As far as sectoral risks are concerned, compliance specialists and regulators agree about certain economic activities being inherently high-risk, such as precious metals trade, real estate and industries that are cash intensive. All these vulnerabilities must be taken into account by both businesses and regulators.

Risks in Malaysia

All these challenges apply to Malaysia. The country is one of Southeast Asia's most successful economies.[3] Since 2000, its real annual GDP has grown by 5.5 percent on average. Real income per capita has grown by nearly 6 percent per year.[4] Malaysia has taken advantage of its strategic geographical position to improve trade and transportation links. It has focused on diversification and sustainable growth, which allowed it to minimise the negative impact of the global financial crisis in 2008.[5] In March 2017, the country became among the first to launch a digital free trade zone.[6] Malaysia also provides visa-free entry to nationals from more than 160 states and its financial sector is very well integrated into the global financial system, which makes it more vulnerable to illegal activities from local offenders and international criminal networks. Additionally, Malaysia is a global leader in Islamic finance.[7] As with other south east Asian nations, part of the country's economic activities are traditionally cash-reliant and are conducted outside of the global financial system.[8]

In October 2018, the The Financial Action Task Force (FATF) acknowledged that Malaysia had taken serious measures to address gaps identified in its 2015 Mutual Evaluation Report.[9]
The latest edition of the International Narcotics Control Strategy Report, published by the United States Department of State in March 2019, however, defines Malaysia as a major money-

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[1] https://www.ey.com/Publication/vwLUAssets/EY_-_Expecting_more_from_risk_management/$FILE/EY-expecting-more-from-risk-management.pdf
[2] https://www.theguardian.com/world/2014/oct/30/foreign-jihadist-iraq-syria-unprecedented-un-isis
[3] https://www.gov.uk/government/publications/overseas-business-risk-malaysia/overseas-business-risk-malaysia
[4] https://www.imf.org/en/News/Articles/2019/06/23/sp062419-md-ingredients-for-malaysias-economic-prosperity#_edn1
[5] Ibid.
[6] https://www.thestar.com.my/tech/tech-news/2017/03/22/mdec-and-alibaba-launch-the-dftz
[7] https://www.state.gov/wp-content/uploads/2019/03/INCSR-Vol-INCSR-Vol.-2-pdf.pdf
[8] http://www.fatf-gafi.org/media/fatf/documents/reports/mer4/Mutual-Evaluation-Report-Malaysia-2015.pdf
[9] http://www.bnm.gov.my/files/publication/fsps/en/2018/cp03.pdf

laundering jurisdiction.[10] The Basel Institute on Governance, which publishes the yearly AML Index based on data from 15 publicly available sources such as the FATF, Transparency International, the World Bank and the World Economic Forum[11], ranked Malaysia 62nd out of 125 countries in its 2019 edition. This makes the country medium risk.[12] In the national risk assessment, Bank Negara Malaysia, Malaysia's central bank, identified fraud, smuggling (including customs and excise duties evasion), drug trafficking, tax crimes and bribery and corruption as the most prevalent crimes in the country. Banking institutions, money changers, non-bank remittance service providers and casinos are also classified as being inherently high risk.[13]

Legal Framework and Enforcement

The main anti-money laundering (AML) and counter-terrorist financing (CTF) legislation in Malaysia is The Anti-Money Laundering, Anti-Terrorism Financing and Proceeds of Unlawful Activities Act 2001 (AMLA). Initially, the AML/CTF framework applied only to financial institutions but between 2003 and 2010 it was extended to include non-financial institutions and risks in other sectors. AMLA has been amended multiple times since then to reflect new developments, for example the inclusion of provisions to combat terrorist financing after 9/11[14], and to expand the scope of activities that are subject to restrictions and penalties. These measures apply to both companies and individuals. Section 4 of AMLA stipulates that: "*any person who commits a money laundering offence shall on conviction be liable to imprisonment for a term not exceeding fifteen years and shall also be liable to a fine of not less than five times the sum or value of the proceeds of an unlawful activity or instrumentalities of an offence at the time the offence was committed or RM 5m, whichever is the higher.*"[15]

Bank Negara Malaysia data reveals that between 2015 and June 2017, the bank imposed total fines of RM 115.8 million.[16] For example, it imposed a RM 53.7 million fine on AmBank Group "*as a result of a breach of certain regulations under Section 234 of the Financial Services Act 2013 and Section 245 of the Islamic Financial Services Act 2013 by AmBank (M) Bhd and AmBank Islamic Bhd, respectively*". The bank agreed to pay the fine and agreed to allocate RM 24 million on average per year for training and systems that would enhance the robustness of its processes and reporting.[17] Bank Negara started publishing enforcement actions taken against non-compliant financial institutions and intermediaries, including all agencies and multinational corporations, in January 2018. Malaysia's Central Bank governor Tan Sri Muhammad Ibrahim, announced the move in October 2017, when he stated: *"We expect the financial system to adhere to the strong compliance and corporate governance standards. We have not hesitated to impose hefty fines when circumstances warranted such actions".*[18]

In his keynote speech at the Bank Negara Malaysia and the Malaysian Bar Joint National AML/CFT Conference held in August 2019 in Kuala Lumpur, Encik Adnan Zaylani Mohamad Zahid, assistant governor of the Central Bank of Malaysia, reiterated the bank's determination to keep up the pace. He highlighted how important it was for non-financial business professionals, and more specifically, lawyers, to comply with AML and CTF regulations. He also noted that during the past two years, the bank had held on-site examinations, awareness and engagement sessions and had shared data with stakeholders from the non-financial sector. But he pointed out that although progress had been made, overall AML/CTF compliance is still "*inadequate*", due

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[10] https://www.state.gov/wp-content/uploads/2019/03/INCSR-Vol-INCSR-Vol.-2-pdf.pdf
[11] https://www.baselgovernance.org/basel-aml-index/what-does-basel-aml-index-measure
[12] https://www.baselgovernance.org/basel-aml-index/public-ranking
[13] http://amlcft.bnm.gov.my/document/Malaysia_NRA.pdf
[14] https://www.nst.com.my/opinion/columnists/2018/07/394517/amla-extremely-powerful-legislation
[15] http://www.agc.gov.my/agcportal/uploads/files/004%20-%20ACT%20613%20KPI%202017%20%28TP%20LULUS%29%20130718.pdf
[16] https://www.nst.com.my/business/2017/10/287193/bnm-publish-enforcement-actions-starting-2018
[17] https://www.thestar.com.my/business/business-news/2015/11/24/ambank-group-fined-rm537mil-by-bank-negara
[18] https://www.nst.com.my/business/2017/10/287193/bnm-publish-enforcement-actions-starting-2018

mainly to the lack of awareness and understanding of the risks and obligations of the parties concerned.[19] Mr. Zahid also announced that Bank Negara Malaysia is finalising a revision to its Sector 5 Policy Document (or the AML/CFT Guidelines issued pursuant to the AMLA). The draft is open for consultations this September. Another important measure, intended as a warning for all reporting institutions, was that the regulator will penalise any non-compliance as of the beginning of 2020.[20]

Corporate risk in Malaysia is dependent on multiple factors, such as geography, business activities and jurisdictions of operation. With abuses of the global financial system becoming larger in volume and more sophisticated in execution, Malaysian lawmakers have expanded the scope of the responsibilities of reporting institutions, and regulators have adopted a policy of more transparency about the fines they impose and the rationale behind them. Financial losses and reputational risk have been two of the major consequences for those found guilty. It is yet to be seen how reporting institutions will adapt to the new environment and whether being labelled *"unscrupulous parties"*[21] will be enough to deter those looking to dodge compliance.

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[19] http://www.bnm.gov.my/index.php?ch=en_speech&pg=en_speech&ac=837
[20] Ibid.
[21] http://www.bnm.gov.my/index.php?ch=en_enforcement_action&pg=en_enforcement_action&lang=en#36