

# U.S. Rep. Frank Joins Critics of SEC List Linking Companies, Rogue States



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By Matt Squire

U.S. Representative Barney Frank urged the Securities and Exchange Commission to eliminate from its Web site or make changes to a list aimed at identifying companies that have business dealings with countries that sponsor terrorism.

In a letter sent to SEC Chairman Christopher Cox on Thursday, Frank, chairman of the House Financial Services Committee, said the list unfairly includes companies that have divested, or have negligible business dealings, in these countries.

The list, published on the SEC's Web site on June 25, includes any companies with references in their annual reports to the five countries that the U.S. State Department has labeled sponsors of terrorism—Cuba, Iran, North Korea, Sudan and Syria. Critics say that, without including further analysis, such a list is misleading.

"It is a significant concern to me that by developing its list without any clear criteria, the SEC's efforts will dilute the effectiveness of publicizing the names of companies that do have material investments in the economies of rogue states," wrote Frank.

Frank, a Massachusetts Democrat, joins a growing number of opponents to the initiative, including an international banking trade group that represents banks named on the list that say they are being unfairly associated with rogue countries.

The Institute of International Bankers (IIB) issued letters to the SEC and the U.S. Treasury on July 6 requesting that the list be discontinued until the agencies review it for consistency with U.S. policy. Lawrence Uhlick, chief executive of the group, said in the letters that without accounting for the degree in which the companies have business dealing in the countries, the list is unfair, highly prejudicial and could have a negative effect on competition in the U.S.

## 'Sloppy Work'

The creation of the list "is positively sloppy work" by the SEC, said a former banking regulator. "Just because someone has a word in a 300-page SEC filing, they get on some list," the former regulator said. "Shouldn't the SEC have read that paragraph where the word appears to see if they want to put it on there?"

The list includes a number of high-profile international financial institutions, including, Bank of Tokyo – Mitsubishi, Credit Suisse Group, HSBC Holdings, ABN Amro Holdings, and Deutsche Bank.

HSBC, which was listed as having business dealing in all five sanctioned countries, is aware of being on the SEC list, said spokeswoman Linda Recupero. "The issue is the fact that we are not doing anything illegal or breaking any regulatory requirements. ... We take our obligations to prevent any sort of terrorist financing or money laundering very seriously," she said.

Recupero said the SEC's list "is not fully representative of what the facts are, so it can certainly be misinterpreted."

The SEC's initiative could reflect an effort to exert some influence on the debate among regulators on how to monitor for terrorist financing, the former banking regulator said.

Furthermore, the SEC's work could be an attempt to pressure companies to end their ties with countries deemed to be hostile to the interests of the U.S. government, said Ross Delston, of GlobalAML.com, a Washington, D.C.-based compliance consulting firm. "This is a classic case of attempting to use 'guilt by association as an instrument of foreign policy,'" he said.

## Disclaimer

The SEC said in a June 25 statement that the list outlines the relevant portions of the companies' annual report "to insure proper context," and being on the list doesn't mean "the company directly or indirectly supports terrorism or is otherwise engaged in any improper activity."

However, Delston said, "the SEC's disclaimer is not much for companies to hide behind, and may in fact have the opposite effect, by linking these companies with terrorism, while disclaiming any intention to do so."

An SEC spokesman declined to comment on the issue.

The SEC list also puts U.S. banks under pressure from both a compliance and reputational standpoint, said the former regulator, by pushing them to search through lengthy annual reports for the context in which the references to sanctioned countries was made. Furthermore, as a due diligence aid, the list pales in effectiveness compared with the process of screening against sanctioned entities identified by the Office of Foreign Assets Control (OFAC), the former regulator said.

"It is a huge burden that came to us from an agency that doesn't have the authority to make us do this, and if we don't comply then

we've been willfully blind," said the former regulator. "By doing this [the SEC is] exposing us. If we don't do it we could end up with legal problems; we could end up with reputational issues; and it could blindside us from an area that we don't normally look for."

Those concerns are misplaced, said Ken Bryant, managing director of consulting firm Bryant & Associates. The list should be used as a due diligence tool and not be considered as legally mandated set of rules, he said. "The SEC is not stupid," said Bryant. "They are not saying immediately drop and close your account with Deutsche Bank. They are saying, 'You ought to be aware if you are not already,' and you should have been already. The SEC is not going to tell you to drop your relationship, because it doesn't know your relationship."

The former regulator disagreed, "It's not a good due-diligence tool because it hasn't been vetted," he said. "They are making us spend time researching for a bank that is not on the OFAC list. If they want to use this as a due diligence tool, there is a process in place that works. I don't want to go through a 300-page SEC filing and find out where Bank of Tokyo Mitsubishi said something about Cuba."

#### **Other Lists**

Other compliance experts say that the banking industry has been waiting for more guidance from the U.S. government to help them combat potential sources of terrorist financing. Section 326 of the Patriot Act requires banks to have a customer verification program that checks against "lists of known or suspected terrorists or terrorist organizations provided to the financial institution by any government agency." However, the U.S. government has yet to issue such lists.

Until the government issues a list of potential terrorist organizations, the U.S. will have significant holes in its ability to combat terrorist financing at the banking level, said Delston.

"At least the SEC had the guts to produce the list," said Bryant. "They are trying to give you a heads up, but if you're in the financial services industry it's your responsibility to be doing this on your own. And if you did your due diligence and knew your customer, you already know what the extent of your customer's relationship is in that country."