

# Excerpt of Draft HTR

## Suggested Edits from the Bank

Edits have not been agreed to by PwC and the changes reflected below are to aid our discussion

### E. Subsequent Events (to be updated)

During the week of May 19, 2008 PwC became aware of several issues that were not addressed in our presentations to the Regulatory Group on April 30, 2008 and May 1, 2008.

### Special-Written Operational Instructions

The Bank disclosed to PwC the existence of special-written operational instructions found in the "GSC (Global Service Center) Administrative Procedures 'Foreign Transfers' last modified on July 31, 2004". On May 22, 2008, Sullivan and Cromwell LLP provided us with the English translation of Section 1.3 of this document:

~~Banks located in countries designated by the U.S. as enemy countries hold their U.S. dollar accounts outside of the U.S. Upon receipt of U.S. dollar-denominated payment orders of which the ordering or receiving bank is such bank, use the cover payment method and not the one payment method.~~

~~The method for filling out vouchers is the same as in "Section 2 - Payments to Other Banks Located in Japan." However, exert care to avoid the funds being frozen by, among other means, providing our Bank as the ordering bank and not specifying the final receiving bank (the name of the enemy country) and the payment details, in payment orders directed to the U.S.~~

As a result of the cover payment method described above, the Bank's wire messages sent to the U.S. would not have included the names of the ordering bank or final receiving bank. Upon learning of these special-written operational instructions, PwC evaluated their impact on the HTR findings, and considered the following questions: (1) Did the use of cover payments impact the completeness of the HTR data? (2) How were these instructions developed and implemented? (3) Did other operating divisions of the Bank have similar instructions? (4) Did operations intentionally leave out information that would have resulted in an OFAC alert?

The Bank's cover payment method generally consisted of MT 103 messages between non-U.S. originating and receiving banks and cover MT 202 messages that were sent to the U.S. correspondent banks. As described in more detail in the Data, Preparations and Analysis section of this Report, whenever wire messages contained a common reference number the messages were linked together into a Case. The linked underlying MT 103 message to the cover MT 202 message would have included the bank information that was not sent to the US Banks. The Bank has informed PwC that the special-written operational instructions would not have impacted the data available for the HTR. While we agree in theory, had PwC know about these "SpecialWritten Operational Instructions" at the initial Phase of the HTR then we would have used a different approach for completing this project.

The remaining questions, ~~such as,~~ concerning the development, implementation and existence of similar special-written operational instructions procedures as well as the intentional omission of search terms are being investigated by the Bank's Internal Audit Office ("IAO") with the assistance of outside Japanese counsel. The potential impact from the findings from this investigation will need to be considered when evaluating this Report.

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06/11/2008

## Excerpt of Draft HTR

### Altered Wire Messages Resulting From HotScan Hits

The second issue occurred when supporting documentation from HotScan showed the search term hits for OFAC-sanctioned countries was found for nine Priority Cases. The concern was over how these transactions were processed after HotScan identification. These wires were stopped by the Bank's HotScan operations in Tokyo and either restructured as a cover payment (seven Cases) or the MT 103 message was cancelled and re-sent after the term(s) identified by the HotScan were removed (two Cases).

After PwC identified these re-sent messages in the Priority cases, an initial analysis of Allowable cases was performed to review cases that contained multiple MT 103 messages. This analysis found ten cancelled messages with the same issue as the Priority cases in that the message was resent after the search terms were removed. Case analysis for these ten transactions included the review of the cancelled messages with the HotScan alerts that were later removed and concluded that these ten cases were Allowable. The ten cancelled messages that were identified contained six transactions that were restructured using the cover payment method so that the MT 103 message containing the search terms was never sent to the U.S. and the remaining four transactions the MT 103 message was re-sent without the search terms.

Management explained to PwC that these cancelled wires were never dispatched and therefore not sent outside of BTMU-Tokyo. Further, Management believed that the HTR data captured all cancelled wire messages with the search terms that were later removed. The IAO investigation should address the compliance issue that resulted when the Bank's HotScan operation identified wire messages that were potentially restricted by OFAC, and returned them to be reworked by a Branch in Japan in an effort to circumvent OFAC HotScan checking.

PwC's discovery of the altered wire messages resulting from HotScan hits raised concern over the completeness of the data and resulted in the following question: If the original message was cancelled, was it included in the HTR data? In an effort to gain additional comfort that the original messages that contained the HotScan hits were included in the data provided to PwC, we requested (1) a HotScan-generated report for all hits during the HTR period and (2) supporting documentation for these cancelled messages. In response to this request, the Bank explained that a HotScan report was not available for the HTR period and provided us with supporting documentation for 91 cancelled messages. The bank represented that these 91 transactions were the entire population of wire messages that were blocked by the HotScan operation in Tokyo during the HTR. The bank indicated that there were more HotScan hits in addition to the 91 provided, but they were released or cleared. The Bank was unable to quantify the number of HotScan hits that were released during the HTR. PwC understands that HotScan can generate a "Hit Report", but BTMU did not use this feature until February 2008.

PwC found that all 91 wire transactions, including the cancelled and resent messages, were included in the data provided to PwC with the exception of one transaction that was covered by the Consigned Contract Data. These cancelled wire messages were found in the HTR data in their original state with the HotScan alert. Our review of HotScan search term hits for these 91 transactions found that 66 were within the scope of the HTR and the remaining 25 transactions either did not involve one of the six target countries or the transaction was not conducted in U.S. dollars.

In our April 30, 2008 and May 1, 2008 presentations to Regulatory Group, we reported that the number of total cases reviewed was 11,325. As a result of the analysis of additional

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**6/11/2008**

## Excerpt of Draft HTR

HotScan documentation the total cases reviewed increased to 11,330 and our number of Priority Cases increased by three. The additional priority cases were the result of wires transfers to Sudan and Burma that cleared through a U.S. bank and the original wire messages that contained the alerts were cancelled and resent without the HotScan alert. The details for these three priority cases (14234, 14235 and 14236) are described in Appendices I and J.

Separate from the analysis described above, there was one Case that changed from Priority to Allowable since the beneficiary bank was previously considered to be a branch of a US bank when it was in fact a subsidiary and therefore qualified for the U-Turn exemption. The total number of Priority Cases that was previously reported as 190 increased to 192, the net effect of the three additions and one subtraction.

### Data Processing

As a result of the review of the HotScan data additional cases were identified for investigation. One of the cases was flagged by HotScan on the word "Sudan". The wire was in the HTR population; however it was not identified as a Case. This was due to the tag 70 field of the MT 103 message containing a hyphen before the word Sudan. This text in the field was "Remittance Information/Regulatory Reporting-Sudan-Related-Business Accountability-Consultation".

Subsequent investigation showed that BTMU's ALT system merges two SWIFT message tags together into one field. These tags are tag 70 (Remittance Information) and tag 77B (Regulatory Reporting). Both of these tags are freeform text fields and were provided to PwC as the merged field. To annotate this data in the HTR population as the merged result of two message tags, the label "Remittance Information/Regulatory Reporting-" was inserted into the corresponding field in the HTR database. No extra space was put after the hyphen, resulting in the label being inserted directly next to the beginning of the text in the field.

As described in the Search Term Methodology section of this report, the Code matching approach uses a space before and after the search term. As the term Sudan was searched as Code, this Case was not identified due to the hyphen directly before Sudan. As of the date of publishing this report, we did not further investigate the contents of this field.

Another new case was identified resulting from the search term Sudan having a pound sign in front of the term (e.g., #SUDAN). Subsequent review of our project documentation indicated that ALT data was processed by the Bank into a more usable format by using code to convert UNIX linebreaks (carriage returns) into pound signs (#). As carriage returns were randomly dispersed throughout the data, in some instances # symbols appear embedded in terms that were split across two lines of text in the wire. The example #SUDAN is one of these cases and would have caused the Code search methodology not to work. As of the date of publishing this report, we did not further investigate the impact of carriage returns.

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**6/11/2008**

## Excerpt of Draft HTR

### Subsequent Events [INSERT]

During the week of May 19, 2008 PwC became aware of two issues that were not addressed in our presentations to the Regulatory Group on April 30, 2008 and May 1, 2008.

#### Cancelled Wire Messages

While PwC was responding to questions raised at the May 1, 2008 presentation to the Regulatory Group, supporting HotScan documentation for nine Priority Cases was analyzed. This documentation showed the HotScan hits for OFAC-sanctioned countries and the corresponding wire messages stopped by the Bank's HotScan operations in Tokyo. These stopped transactions were either restructured as a cover payment (seven Cases) or the MT 103 message was cancelled and re-sent after the term(s) identified by HotScan were removed (two Cases). In addition, based on our initial analysis, we identified ten additional non-Priority cases where it appeared that the initial MT 103 message had been modified or restructured.

PwC's discovery of the cancelled wire messages resulting from HotScan hits raised concern over the completeness of the data and resulted in the following question: If the original message that contained the HotScan hit was cancelled, was it included in the HTR data?

Management explained to PwC that these cancelled wires were never dispatched and therefore not sent outside of BTMU-Tokyo and that the HTR data captured all cancelled wire messages with the search terms that were later removed. In order to determine that the HotScan hits were included in the data provided to PwC, we requested (1) a HotScan-generated report for all hits during the HTR period and (2) supporting documentation for these cancelled messages. In response to this request, the Bank explained that a HotScan report was not available for the HTR period and provided us with supporting documentation for 91 cancelled messages. The bank represented to PwC that these 91 transactions were the entire population of wire messages that were blocked by the HotScan operation in Tokyo during the HTR.

PwC found that all 91 wire transactions, including the cancelled and re-sent messages, were included in the data provided to PwC with the exception of one transaction that was covered by the Consigned Contract Data.

#### Additional Cases

In our April 30, 2008 and May 1, 2008 presentations to Regulatory Group, we reported that the number of total cases reviewed was 11,325. As a result of the analysis of additional HotScan documentation, an additional five cases were identified for review and increased our total to 11,330. These five cases involved wire transfers to Sudan and Burma and cleared through a U.S. bank.

The review of the five cases resulted in three additional priority cases (14234, 14235 and 14236) that are described in Appendices I and J. In addition to these five Cases, there was one Case that changed from Priority to Allowable because the beneficiary bank had

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06/16/2008



## Excerpt of Draft HTR

been incorrectly identified as a foreign branch of a US bank instead of a subsidiary and therefore qualified for the U-Turn exemption. The total number of Priority Cases that was previously reported as 190 increased to 192, the net effect of the three additions and one subtraction.

### Written Operational Instructions

Shortly after the Bank disclosed to OFAC the existence of written operational instructions, PwC was provided a copy of the *GSC (Global Service Center) Administrative Procedures 'Foreign Transfers'*. Management's Report to OFAC included the following description:

*These instructions were mainly for U.S. dollar payment orders relating to vostro accounts of banks in countries sanctioned by the United States. The instructions were to use the cover payment method, to indicate our Bank as the ordering bank and not to include the name of the final receiving bank, so that the funds would not be frozen.*

Upon learning of these written operational instructions, PwC evaluated the use of cover payments on the completeness of the HTR data. The scope of the HTR did not include a forensic investigation or process review to understand the full impact of these written instructions on the operation of BTMU's international wire remittance and trade finance activity.

The Bank's cover payment method generally consisted of MT 103 messages between non-U.S. originating and receiving banks and cover MT 202 messages that were sent to the U.S. correspondent banks. As described in more detail in the Data, Preparations and Analysis section of this Report, whenever wire messages contained a common reference number the messages were linked together into a Case. The linked underlying MT 103 message to the cover MT 202 message would have included the bank information that was not sent to the US Banks. Alternatively, a cover MT 202 without mention of a search term and did not contain a common reference number would not have been linked to the underlying MT 103 message. Thus, this un-linked MT 202 message would not have been identified for detailed review. Based on the assumption that a common reference number was available, our understanding is that the written instructions would not have impacted the completeness of data available for the HTR and our methodology to process, search and review the HTR data was appropriate.

### Impact of the IAO Investigation

Management informed PwC that as a result of these subsequent events, BTMU's Internal Audit Office has initiated an investigation as described in Management's Report to OFAC. Their findings from this investigation need to be considered when evaluating this Report. PwC has forwarded our initial findings relating to cancelled wire messages to Management to be further analyzed as part of the Internal Audit Office investigation.

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#### Cancelled Wire Messages

~~While PwC was responding to questions raised at the~~ After the April 30 and May 1, 2008 presentations to the Regulatory Group, supporting HotScan documentation for ~~nine~~ Priority Cases was analyzed for quality control purposes. This documentation showed the HotScan hits for OFAC-sanctioned countries and the corresponding wire messages stopped by the Bank's HotScan operations in Tokyo. Through our analysis, we noted that ~~nine of these~~ stopped transactions were either restructured as a cover payment (~~six~~ sixteen Cases) or the MT 103 message was cancelled and re-sent after the term(s) identified by HotScan were removed (~~three~~ two Cases). In addition, based on our initial analysis, we identified ten additional non-Priority cases where it appeared that the initial MT 103 message had been modified or restructured.

PwC's discovery of the cancelled wire messages resulting from HotScan hits raised concern over the completeness of the data and resulted in the following question: If the original message that contained the HotScan hit was cancelled, was it included in the HTR data?

Management explained to PwC that these cancelled wires were never dispatched and therefore not sent outside of BTMU-Tokyo and that the HTR data captured all cancelled wire messages with the search terms that were later removed. In order to determine that the HotScan hits were included in the data provided to PwC, we requested (1) a HotScan-generated report for all hits during the HTR period and (2) supporting documentation for these cancelled messages. In response to this request, the Bank explained that a HotScan report was not available for the HTR period and provided us with supporting documentation for 91 cancelled messages. The bank represented to PwC that these 91 transactions were the entire population of wire messages that were blocked by the HotScan operation in Tokyo during the HTR.

PwC found that all 91 wire transactions, including the cancelled and re-sent messages, were included in the data provided to PwC with the exception of one transaction that was covered by the Consigned Contract Data.

#### Additional Cases

In our April 30, 2008 and May 1, 2008 presentations to Regulatory Group, we reported that the number of total cases reviewed was 11,325. As a result of the analysis of additional HotScan documentation, an additional five cases were identified for review and increased our total to 11,330. These five cases involved wire transfers to Sudan and Burma and cleared through a U.S. bank.

The review of the five cases resulted in three additional priority cases (14234, 14235 and 14236) that are described in Appendices I and J. In addition to these five Cases, there

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06/17/2008

## Excerpt of Draft HTR

was one Case that changed from Priority to Allowable because the beneficiary bank had been incorrectly identified as a foreign branch of a US bank instead of a subsidiary and therefore qualified for the U-Turn exemption. The total number of Priority Cases that was previously reported as 190 increased to 192, the net effect of the three additions and one subtraction.

### Written Operational Instructions

Shortly after the Bank disclosed to OFAC the existence of written operational instructions, PwC was provided a copy of the GSC (Global Service Center) Administrative Procedures 'Foreign Transfers'. Management's Report to OFAC included the following description:

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Upon learning of these written operational instructions, PwC evaluated the use of cover payments on the completeness of the HTR data. The scope of the HTR did not include a forensic investigation or process review to understand the full impact of these written instructions on the operation of BTMU's international wire remittance and trade finance activity.

The Bank's cover payment method generally consisted of MT 103/202 messages between non-U.S. originating and receiving banks and cover MT 202 messages that were sent to the U.S. correspondent banks. As described in more detail in the Data, Preparations and Analysis section of this Report, whenever wire messages contained a common reference number the messages were then linked together into a Case. The linked underlying MT 103/202 messages to the cover MT 202 message would have included the bank information that was not sent to the US Banks. ~~Alternatively, a cover MT 202 without mention of a search term and did not contain a common reference number would not have been linked to the underlying MT 103 message. Thus, this un-linked MT 202 message would not have been identified for detailed review. Based on the assumption that a common reference number was available, our understanding is that the written instructions would not have impacted the completeness of data available for the HTR, and our methodology to process, search and review the HTR data was appropriate.~~

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06/17/2008

# Excerpt of Final HTR

## E. Subsequent Events

During the week of May 19, 2008 PwC became aware of some issues that were not addressed in our presentations to the Regulatory Group on April 30, 2008 and May 1, 2008.

### Canceled Wire Messages

After the April 30 and May 1, 2008 presentations to the Regulatory Group, supporting HotScan documentation for Priority Cases was analyzed for quality control purposes. This documentation showed the HotScan hits for OFAC-sanctioned countries and the corresponding wire messages stopped by the Bank's HotScan operations in Tokyo. Through our analysis, we noted that nine of these stopped transactions were restructured as a cover payment (4 cases), or the MT 103 message was canceled and re-sent after the term(s) identified by HotScan were removed (4 cases), or were restructured as a cover payment and the search term removed in the MT 103 (1 case). In addition, based on our initial analysis, we identified ten additional non-Priority cases where it appeared that the initial MT 103 message had been modified or restructured. PwC's discovery of the canceled wire messages resulting from HotScan hits raised concern over the completeness of the data and resulted in the following question: If the original message that contained the HotScan hit was canceled, was it included in the HTR data?

Management explained to PwC that these canceled wires were never dispatched and therefore not sent outside of BTMU-TKY and that the HTR data captured all canceled wire messages with the search terms that were later removed. In order to determine that the HotScan hits were included in the data provided to PwC, we requested (1) a HotScan-generated report for all hits during the HTR period and (2) supporting documentation for these canceled messages. In response to this request, the Bank explained that a HotScan report was not available for the HTR period and provided us with supporting documentation for 91 transactions. The bank represented to PwC that these 91 transactions were the entire population of wire messages that were blocked by the HotScan operation in Tokyo during the HTR.

PwC found that all 91 wire transactions, including the canceled and re-sent messages, were included in the data provided to PwC with the exception of one transaction that was covered by the Consigned Contract Data.

### Additional Cases

In our April 30, 2008 and May 1, 2008 presentations to Regulatory Group, we reported that the number of total cases reviewed was 11,325. As a result of the analysis of additional HotScan documentation, an additional five cases were identified for review and increased our total to 11,330. These five cases involved wire transfers to Sudan and Burma and cleared through a U.S. bank.

The review of the five cases resulted in three additional priority cases (14234, 14235 and 14236) that are described in Appendix I. In addition to these five Cases, there was one Case that changed from Priority to Allowable because the beneficiary bank had been incorrectly identified as a foreign branch of a US



## Excerpt of Final HTR

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Upon learning of these written operational instructions, PwC evaluated the use of cover payments on the completeness of the HTR data. The scope of the HTR did not include a forensic investigation or process review to understand the full impact of these written instructions on the operation of BTMU's international wire remittance and trade finance activity.

The Bank's cover payment method generally consisted of MT 103/102 messages between non-U.S. originating and receiving banks and cover MT 202 messages that were sent to the U.S. correspondent banks. As described in more detail in the *Data Preparation and Analysis* section of this Report, whenever wire messages contained a common reference number the messages were then linked together into a Case. The linked underlying MT 103/102 messages to the cover MT 202 message would have included the bank information that was not sent to the US Banks. We have concluded that the written instructions would not have impacted the completeness of data available for the HTR and our methodology to process and search the HTR data was appropriate.

### Impact of the IAO Investigation

Management informed PwC that as a result of these subsequent events, BTMU's Internal Audit Office has initiated an investigation as described in Management's Report to OFAC. Their findings from this investigation need to be considered when evaluating this Report. PwC has forwarded our initial findings relating to canceled wire messages to Management to be further analyzed as part of the Internal Audit Office investigation.

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