The voice of banking & financial services

16 September 2011

MLR.review@hmtreasury.gsi.gov.uk

The Money Laundering Review
Room 3.15, HM Treasury
1 Horse Guards Road
London SW1A 2HQ

Dear Sirs,

Review of the Money Laundering Regulations 2007: the Government response and further consultation

The BBA is the leading association for the UK banking and financial services sector, speaking for 223 banking members from 60 countries on the full range of UK or international banking issues and engaging with 37 associated professional firms. Collectively providing the full range of services, our member banks make up the world's largest international banking centre, operating some 150 million accounts and contributing £50 billion annually to the UK economy.

We welcome publication of the Government response to the Review of the Money Laundering Regulations 2007 and the further consultation on proposed changes to the Regulations. In particular, we welcome the Government's commitment to ensuring that the UK financial system is a hostile environment for money laundering and terrorist finance, while minimising the burden on business and maintaining the UK's position internationally. We agree with the Government's approach to this review which is based on assessing where the Regulations are working well and identifying areas for improvement.

We are a little surprised at the timing of the proposed changes in the light of the other international work which will require additional changes to the anti-money laundering framework. Both the FATF review of its standards and the European Commission's plans for a 4th Anti-Money Laundering Directive will be likely to call for significant additional changes to certain important aspects of the regime, including the requirements on PEPs, beneficial ownership, wire transfers and data protection. While the potential changes being considered by HM Treasury as part of this review may have a more limited impact if they are introduced, they could still mean that our members will have to make alterations to their systems and procedures. We also suggest that there may be a need to assess some of the information sharing proposals referenced in question 16 below for compatibility with the Human Rights Act 2000 and the Data Protection Act 1998.

We have commented in the attached Annex on the specific questions raised in this consultation, and we would also like to provide the following comments on the further general issues that HM Treasury has highlighted.

1. The burden on business

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We note that the Government would welcome further information on the costs faced by individual businesses as a result of the Regulations. In our response to the Review of the Money Laundering Regulations (dated 18 December 2009), we pointed out some of the difficulties for businesses of disaggregating the costs of anti money laundering work from the broader financial crime legislative and regulatory obligations. We believe that there is little in the consultation that would result in a direct increase in costs incurred by businesses. However, we would again urge HMG to remain mindful of the cumulative impact of reforms

2. UK strategy for financial crime

We continue to believe that there is a gap in the Government's financial crime strategy whereby there is an absence of an objective analysis of the true extent of financial crime and money laundering. We would encourage HM Treasury together with other relevant government departments to provide an up to date strategy and framework within which the appropriateness of legislative and enforcement measures can be evaluated. In the light of the current re-organisation of the UK regulatory structure and the formation of new agencies involved in tackling financial crime, the development of an effective strategy would be a timely initiative.

3. The risk based approach

We understand that HM Treasury has made it a priority to help change business practice from a "tick-box" to a properly risk based approach. We strongly support the risk based approach though our members have acknowledged the complexity attached, especially for large internationally active banks.

In terms of supervising the risk based approach, our members have reported that supervisors (and the FSA in particular) have consistently adopted a view which appears to conflict with the essentials of the risk based approach. For example, the risk based approach must involve financial institutions putting into practice their own policy and standards according to the risk assessment they have carried out. This will be unique to each financial institution. During the course of regulatory visits, our members have noted that supervisors have expectations that all firms will adopt the same standards and practices. This is unrealistic and not achievable within a risk based approach that is genuinely tailored to the business profile and risks of a particular financial institution.

4. Customer due diligence

We note the comment that "some customers of regulated businesses were critical of a perceived absence of a risk-based approach at the customer facing end of some businesses. Examples include banks demonstrating little flexibility in their requirements for proof of identity in some low risk circumstances, often citing incorrectly their obligations under the Regulations. The Government opposes such practice and encourages financial institutions not unfairly to exclude legitimate customers, particularly vulnerable members of society, from financial services."

As above, we would point out that the current supervisory approach put in place by regulators has tended to become more prescriptive and is a "comply or explain" stance which does not enable firms to implement a risk based approach. This is particularly relevant to the FSA's proposed Financial Crime Guide with its stance on good and poor practice.

The narrow focus and applicability of some of the proposals could be interpreted as sending a mixed message as to the Government's commitment to a risk based approach. Similarly, the proposal to remove criminal penalties could be interpreted as being at odds with the objective of driving an effective regime. There should still be clear consequences for negligence or incompetence.

5. Consent and related legislation

We are pleased to see the recognition given by the Government to the need to consider the Regulations alongside other related legislation, notably the Proceeds of Crime Act 2002. We note the general comment that “Banks and accountants are generally in favour of the current approach”. We would, once again, point to the serious and significant deficiencies and issues on the POCA consent and fungibility issues.

We hope that our comments are helpful and will inform this further consultation by HM Treasury, and we would, of course, be happy to provide further comment should this be required.

Yours sincerely,

Catriona Shaw
Director Financial Crime

General questions raised in the consultation

1. Do you agree that the options are compatible with our international commitments, the FATF Recommendations and EU Directive, and are they otherwise free of legal difficulties?

BBA Comment: as already noted, we are aware that changes to the AML framework and requirements are looming as a result of the FATF review of its standards and the work underway within the European Commission on a 4th AML Directive. While the options as set out may be compatible with current international commitments, these are likely to change in the near future.

2. In policy terms are the options appropriate and consistent with our broader priorities for an effective and proportionate AML regime?

BBA Comment: it is difficult to comment on the effectiveness or proportionality of the AML regime in the absence of either a current strategy or an analysis of the true extent of financial crime and money laundering. Although the number of SARs submitted to the authorities rises year by year, it would be unwise to attribute this to any rise in money laundering activities.

3. Will the proposals result in more or less costs for business and other interested parties? In particular, further views will be welcome on estimating the costs/benefits to individual businesses.

BBA Comment: the proposals appear to have less impact on banks than on other regulated sectors. We are unable to provide cost/benefit information but we do not believe tat the changes proposed would have a material cost impact to business.

Specific consultation questions

1. Should the existing criminal sanctions be wholly or partly repealed?

BBA Comment: our members had mixed views on this question. Some have argued strongly that criminal sanctions should remain as they help maintain the focus that is required from all staff who work in financial services and not only the MLROs and Compliance Officers. Others have stated their support for the concept of removing criminal sanctions while recommending that the Government consider the message that a whole repeal may send regarding its resolve to create a hostile environment for money laundering and terrorist finance. Some would recommend that specific offences are considered on a case by case basis and the potential impact and increased risk carefully assessed.

2. Should new powers be granted to supervisors allowing them to order or require actions by businesses to mitigate the potential negative impacts from the loss of criminal sanctions?

BBA Comment: we do not believe that the loss of criminal sanctions should trigger a need to grant new powers to supervisors. The powers in current legislation and the existing supervisory powers appear to us to be adequate. Overall, the message must be about proportionality and that any new regime should also be practically workable and fair. There was a concern expressed that the protections within the criminal justice system (including the current burden of proof for criminal offences) would shift to the civil standard, and may encourage civil enforcement action in circumstances where criminal action could not or would not be taken.

3. Do you agree that the current distinction between Parts 1 and 2 of Schedule 3, e.g. for reliance purposes, should now be removed?

BBA Comment: No strong views expressed either way, though generally our members reported taking a cautious approach to reliance.

4. Should a debt purchaser be able to rely on CDD previously performed by the seller in this situation?

BBA Comment: one response recommended that a principles based approach be taken which is relevant in the context of the transaction. For example, in the case where a retail loan originator bundles loans for sale, or in the corporate context where loans are traded in the secondary market as investments, we agree that a debt purchaser should be able to rely on CDD previously performed by the seller considering that no client relationships are formed with the obligor.

In the mergers and acquisition context, one bank recognised that the buyer would need to satisfy itself that KYC checks had been conducted to an acceptable standard and certain conditions met, including for example, checking when te seller conducted the CDD to ensure it is current and relevant.

5. Should there be a general de-minimis exclusion for very small businesses (for example those with below €15,000 VAT-exclusive turnover per annum), or a reduction in the requirements placed on such businesses?

BBA Comment: our members broadly supported having a general de-minimis exclusion. They did point out the possible unintended consequences such as the migration of risk to smaller firms once criminals identified the opportunity presented by such exclusion. There would in parallel be a risk of multiple businesses being set up to meet the exclusion criteria and avoid being caught by the Regulations. It may be that the difference in risk level would best be reflected by the intensity of supervisory approach instead. There would also be a need to ensure that the costs involved in introducing this exemption and ensuring that it was complied with and did not adversely impact overall compliance with the Money Laundering Regulations 2007 are not proportionate to the regulatory burden it would remove.

6. Do you agree that non-lending credit institutions should be exempt from the Regulations?

BBA Comment: broadly speaking, yes.

7. Do you agree UK estate agents who arrange for the sale and purchase of overseas property by their clients should be regulated?

BBA Comment: yes, we believe that they should be regulated.

8. Safe Custody

"Safe custody services" are regulated activities, but "safe custody" is not otherwise defined in detail. The FSA has developed a definition that refers to "secure storage suitable for high-value physical items like jewellery or documents of title". This definition is designed not to capture businesses like furniture depositories.

Do you agree that "safe custody services" should be more clearly defined, and if so, how?

BBA Comment: our members expressed differing views. Some did not have a strong view, while others felt that it is very important to distinguish between those businesses that exist solely to provide safe custody services and those regulated institutions that offer a safe storage facility in addition to their 'core' business. Some UK high street banks will offer 'safe custody' services for existing customers to store important documents (deeds, wills etc) or small locked boxes. This type

of service is generally no longer promoted and as such it should exclude businesses where 'safe custody' services are not their primary businesses.

Some commented on the difficulty around reaching an agreed definition, and our members did not like the suggested definition that the FSA has developed. We understand that the FSA has made an assessment that the level of risk of money laundering around safe custody services is high. We have seen no substantive evidence on how the FSA has reached this assessment. As far as the safe custody services that are provided by our members are concerned, we do not accept that they involve a high risk of money laundering.

9. Do you agree that all previous criminal conduct should be considered under the fit and proper test for MSB's?

BBA Comment: One of our members strongly supported this, stating that it would align HMRC's practice with existing FSA practice with regard to the fit and proper test for FSA approved persons.

10. Do you agree a right of appeal should be introduced for decisions under the fit and proper test by HMRC?

BBA Comment: yes, if this is aligned with other rights to appeal under other legislation**.**

11. Should supervisors be given new powers to impose penalties for the unreasonable failure to allow a supervisor to enter their businesses premises?
12. Should there be penalties for the unreasonable failure to provide information?

BBA Comment: these proposals would appear to be sensible, subject to clear and prior provision of guidance as to what would be deemed unreasonable.

13. Should supervisors be given additional powers to enforce the payment of fees or charges payable under a supervisory arrangement, for example by ensuring all supervisors have powers to de-register a business where there is sustained non-payment?

BBA Comment: these proposals would appear to be sensible, with similar safeguards as in Regulation 42.

14. Should supervisors be given strengthened powers to de-register a business, where a registration has been obtained by other than bona fide means, or no longer serves the public interest?

BBA Comment: currently Regulation 32 allows this for the FSA or the OFT. Is this proposing that these powers be extended to other authorities?

15. Should supervisors have clear powers to make enquiries of persons who reasonably appear to be relevant persons?

BBA Comment: yes.

16. Should the ability of supervisors to exchange information with each other for the purposes of discharging their AML supervisory functions be strengthened if necessary by the creation of 'gateways' to allow for the exchange of information?

BBA Comment: we support this proposal in principle, subject to appropriate safeguards being provided such as defining the information that can be shared and circumstances where prior agreement of the business might be sought. Ultimately, the Regulations and data protection legislation should be aligned and the Regulations include the necessary provisions and conditions

that would enable supervisors to perform such an exchange or the use of the proposed gateways in compliance with the Data Protection Act 1998.

17. Should HMRC or other supervisors have powers to limit or prescribe the language used by regulated businesses to describe the relationship with their AML supervisor (for example to make it clear that supervision applies only to money laundering compliance)?

BBA Comment: yes, we support this proposal.