

RESPONSE TO CUTTING RED TAPE REVIEW

THE EFFECTIVENESS OF THE UK'S AML REGIME

EXECUTIVE SUMMARY

The British Bankers' Association (BBA) is pleased to contribute to this important review. This paper builds upon the dialogue the BBA has facilitated between the Better Regulation Executive (BRE) and the BBA Money Laundering Advisory Panel, as well as the separate session we hosted with smaller banks. We have welcomed the proactive approach of the BRE to engagement with our membership and look forward to further constructive dialogue.

Anti Money Laundering and Counter Terrorist Financing (AML/CTF) is of course not a precise "science" and as such, there will be situations where measures taken may cause delays and frustrations to legitimate customers. Equally not every financial criminal can be detected by banks AML/CTF controls. However, the banking industry does take the view that the time is right to consider fundamental reforms to the AML/CTF framework because:

- The costs of financial crime compliance for the British banking industry have gone beyond a "tipping point" in comparison with the AML/CTF benefits being accrued.
- AML/CTF can impact on the service provided to some legitimate individual customers.
- AML/CTF can be a factor in regard to access to banking for businesses.

A new strategic approach is needed that ensures the UK's collective financial crime prevention and investigation resources are better targeted so that criminals are locked out of the banking system whilst banks can support good business to flourish. Reforms to the regulatory and supervisory framework can provide much needed reductions in unnecessary "red-tape" but also crucially promote strengthened responses to the highest priority risks, including through improvements to financial crime controls in other sectors.

The BBA recognises this review is focused on AML/CTF regulation and supervision and as such we have not commented in too much detail on other matters such as legislation and law enforcement capabilities. The BBA has though provided a copy of our response to the SARs regime review and we would be happy to provide commentary on these aspects.

We do though think it is important as a starting point for the review to be set in the wider context, including the costs of AML/CTF efforts compared to the outcomes arising:

Snapshot of the costs of AML/CTF efforts

- **BBA members are spending at least £5 Billion annually collectively¹** on core financial crime compliance including enhanced systems and controls and recruitment of staff (not including the direct costs from fines AML/CTF breaches). The BBA understands that around 2000 new UK AML roles were created in the banking industry in the past year.
- **In 2014, 82 per cent of the 354,186 Suspicious Activity Reports (SARs) submitted to the NCA were from banks²**, far higher than the levels in most major financial centres. Banks also responded over the past year to around 100,000 requests for bank account information from Government bodies. The total cost to banks from financial crime reporting is not known but many firms have established dedicated teams.
- **The Government has established an Economic Crime Command within the new National Crime Agency.**
- **The Home Office has intensified its policy focus on financial crime matters**, including legislative changes through a new Serious Crime Act.
- **A new Joint Money Laundering Intelligence Task Force is a pilot that is enhancing operational collaboration between banks and law enforcement.**

Outcomes being achieved

- **Bank boards have prioritised enhanced AML/CTF and Sanctions controls**, including by reducing their firm's exposure to high risk relationships and countries.
- **The NCA estimates that hundreds of billions of dollars are laundered through UK banks each year³** (despite the efforts of banks). The UK banking industry is not familiar with the basis for this estimate.

¹ Based on consultation with major banks

² SARs Annual Report 2014

³ UK National Risk Assessment of ML/TF, page 85

- **The law enforcement response to financial crime has been assessed as “*weak for an extended period of time*”.**⁴
- **The Public Accounts Committee expressed concerns over asset recovery**, noting that there could be £1,500m of confiscation order debt uncollected⁵.
- **The effectiveness of the supervisory regime for AML/CTF is seen as “*inconsistent*”.**
- **Supervisors and private sector representatives have “*criticised the SARs regime*”.**⁶
- **A report for the IMF noted significant scepticism around the efficacy of the global and national systems for tackling money laundering and terrorist financing**

Where do we go from here?

The BBA strongly urges the Government to consider a new overarching strategy, involving regulators, private sectors, law enforcement and NGOs. A cost-benefit analysis of the regime, alongside work to develop a common understanding of the highest priority risks, can provide the basis for a strategy that sets out how our collective resources can be most effectively deployed to respond to financial crime. **We recognise this is not a simple exercise and will take time but the banking industry is committed to supporting such efforts.**

The BBA membership recognises that reform to the regulatory/supervisory arrangements for AML will not in itself bring the fundamental system wide changes that are needed to truly ensure the UK is highly effective in tackling financial criminals. **But the banking industry recognises that a reformed regulatory and supervisory approach can be a core feature of a new overarching national strategy. We recommend the following activities are prioritised:**

⁴ UK National Risk Assessment of ML/TF, page 5

⁵ House of Commons Committee of Public Accounts, report on confiscation orders, 5th March 2014

⁶ UK National Risk Assessment of ML/TF, page 6

Recommendation 1: A high level dialogue between the banking industry, the FCA and relevant Government Departments to explore how better alignment can be achieved between the good practice guidance documents for banks on AML/CTF

Recommendation 2: Greater consistency in AML/CTF regulation and supervision of different sectors and globally

Recommendation 3: More regular engagement between the banking industry and key sectors on financial crime matters

Recommendation 4: Intensified banking industry/Government partnership, building on the JMLIT pilot, to better identify current and emerging risks

Recommendation 5: Exchanges of knowledge on best practice to support “future proofing” of emerging financial crime risks

Recommendation 6: Strengthened dialogue between smaller banks and the FCA

Recommendation 7: Attachments for staff in both banks and regulatory bodies (specific to financial crime)

More details on these suggestions are provided in the following sections. This paper is intended to provide the most constructive contribution on behalf of our membership. We stand ready to provide further input as required.

DETAILS

Recommendation 1: A high level dialogue to explore how better alignment can be achieved between the good practice guidance documents for banks on AML/CTF

The Joint Money Laundering Steering Group Guidance is highly valued by the banking industry and is recognised around the world as the most detailed information to support the practical implementation of AML and CTF requirements. Indeed, we are aware of a number of banking industry bodies in other countries that are looking to adopt the JMLSG model. BBA members have indicated their commitment to proactively contribute to work to update the JMLSG Guidance. Key areas of consideration will be the changing nature of banking, including digital banking, paperless services and eIDAS as well as the requirements of the new 4th EU Money Laundering Directive. Additionally other public policies and laws, such as the Immigration Act 2014, have impacted upon AML/CTF policies and procedures by firms and need to be considered.

BBA members have noted the recent updates to the FCA Financial Crime Guide. BBA members also recognise the efforts by the FCA to better reflect banking industry feedback on changes to the Guide. The BBA has also welcomed the strengthened dialogue we have had with the FCA Financial Crime Policy Team in recent years. However, whilst the FCA and the banking industry are in agreement at a strategic policy level that a risk based approach to financial crime is most effective, there can be differences of view on the practical application. Recent FCA Thematic Reviews have set out “good practice” examples for banks for addressing financial crime in these areas. However, the risk areas identified are often generalised, may not be appropriate to banks with different business models and do not appear to have been underpinned by detailed risk assessment work.

The effect of the changes to the FCA Financial Crime Guide has been to push banks into devoting resources into areas that could have been deemed lesser priority by banks if they were able to apply a true risk based approach. (see BBA responses to Thematic Reviews <https://www.bba.org.uk/policy/financial-crime/anti-money-laundering/> .) Additionally the FCA statement in 2015 on “de-risking”⁷ in the view of the BBA membership rather confused a number of issues and was seen by some to undermine the flexibility that would properly be afforded to banks to adopt a risk based approach. **The banking industry would therefore welcome discussions to promote a closer common understanding with the FCA on the practical application of the Risk Based Approach.**

Over and above the two guidance documents mentioned above, there is a pressing need to guard against an ever increasing volume of AML/CTF supplementary guidance being produced through differing Governmental Departments. Just one recent example includes the intended production of new guidance by HMRC to support new tax compliance obligations and objectives. It will cost the government more to produce ‘stand-alone’ supplementary guidance. It also increases risk, including risks relating to inconsistent guidance, increased costs of compliance for BBA members and an increased likelihood of differing levels of supervision and oversight by relevant Governmental departments.

Overall, BBA members feel the time is right for a high level dialogue involving the banking industry, the JMLSG, the FCA and relevant Government Departments to explore how better alignment can be achieved between the good practice guidance documents for UK banks on AML/CTF.

⁷ “De-risking: Banks’ management of money-laundering risk - FCA expectations”, 27th April 2015

Recommendation 2: Promote better consistency in AML/CTF regulation and supervision across all relevant sectors in the UK

Banking industry

Most BBA members, especially those operating internationally, need to consider their financial crime compliance policies and procedures through a global lens. BBA members have noted that a number of international bodies have issued guidance or similar materials relating to AML/CTF. This includes the revised FATF Standards, FATF Guidance and Guidance from the Bank for International Settlements (known as the Basel Committee). Regulators in major financial centres have also issued their own guidance (or similar materials) relating to AML/CTF. The European Supervisory Authorities have also recently issued a consultation on proposed new EU AML Guidelines, a new EU National Risk Assessment is being developed and the Basel Committee is also consulting on potential new Guidance on account opening and correspondent banking. **BBA members find the volume of AML/CTF guidance documents emanating from international bodies adds yet more and perhaps unnecessary complexity to their consideration of AML/CTF policies and procedures. However, of greater concern is the lack of consistency between the guidance provided by the international bodies.**

Banks subject to UK AML regimes are also subject to regulations in other jurisdictions and to a range of international AML guidelines. Lack of alignment between these various regimes causes major problems for banks looking to implement financial crime controls to an organisation-wide standard. In order to meet regulatory expectations in all jurisdictions in which they operate, the organisation-wide standard must be set at the level of the highest individual standard in every category. This leads the bank to adopt higher standards in some jurisdictions than is demanded by the local regulator, leaving the bank at a competitive disadvantage and potentially in legal jeopardy. In the UK, this could, for example, hamper a bank's attempts to work with the regulator to develop a risk-based approach to communities at risk from financial exclusion. It is therefore in the interests of the UK government and banks for there to be no misalignment between international guidance and individual regulatory regimes in each jurisdiction.

BBA members are of the view that the UK Government should promote better alignment and/or consistency in AML guidance for banks internationally.

Other sectors

The effectiveness of supervision and regulation of businesses in certain sectors is an important consideration for banks. There has though been recent public commentary over the quality of AML/CTF regulation supervision in some sectors. **Most starkly the National Risk Assessment of AML/CTF stated in regard to Money Service Businesses:**

“Failure to implement the regulations effectively leaves the [MSB] sector vulnerable to exploitation by criminals seeking to launder funds. MSBs face particular implementation challenges with regard to conducting adequate customer due diligence (CDD), record keeping, transaction monitoring, and the appropriate application of simplified due diligence (SDD) on customers.”

*“MSBs may be supervised by both HMRC (under the regulations) and the FCA (under the Payment Services Regulations 2009). **This means there is a potential for different supervisory approaches to be deployed to a sector that is deemed to be a target for criminals and therefore vulnerable to being used as conduits for money laundering and terrorist financing.**”*

Overall the National Risk Assessment paints a concerning picture of the regulation and supervision of a number of sectors subject to the UK Money Laundering Regulations and of the quality of AML/CTF controls in businesses in these sectors. This is of great concern to the banking industry as weaknesses in these sectors increase the risks posed to banks and also the extent (and therefore burden) of due diligence that needs to be applied to businesses in these sectors. Banks have taken an increasingly cautious approach to ensure that in doing business they are not exposed to disproportionate levels of financial crime risk compared to the benefits accrued from their business activities. This approach is being taken not just in the UK but in most major financial centres

The BBA would urge the Government to take urgent steps to improve the AML/CTF regulation and supervision of these sectors and to promote higher quality compliance by businesses, in the UK and globally.

Recommendation 3: More regular dialogue between the banking industry and key sectors on financial crime matters

The BBA has been pleased to facilitate dialogue between our members and other sectors on financial crime and access to banking matters, as well as participating in Government hosted meetings. Key sectors we have engaged with include:

- MSB sector
- Charity sector
- Digital Currency sector
- Credit Union sector
- Defence Companies
- Financial Technology firms
- English Language Colleges

These activities have allowed practical actions to develop, that can support partnership efforts to strengthen financial crime compliance measures and access to banking. Examples of practical measures take include:

- The BBA worked with the Joint Disasters Emergency Committee to produce guidance on “Getting aid to Syria”
- The BBA has engaged with the International Chamber of Commerce and the Bankers Association for Finance and Trade to produce materials to help banks and their customers to address risks associated with Trade Based Money Laundering

- The BBA has issued guidance for key sectors on how to apply for banking services
- ABCUL, the representative body for Credit Unions, provided to the BBA a briefing note for banks explaining the regulatory and legal basis of credit unions.
- English UK provided a document for BBA members explaining how its members were implementing new immigration requirements
- Dialogue is underway on whether market leading Money Service Businesses could become involved in banking industry information sharing arrangements for financial crime

The BBA will be working with the Law Society and the Consultative Committee of Accountancy Bodies to develop further engagement between our respective memberships. These efforts will support the sharing of knowledge between these sectors on financial crime matters. **The BBA would support the involvement of Government in the efforts we are undertaking to improve the dialogue between our membership and other sectors.**

Recommendation 4: Intensified partnership, building on the JMLIT pilot, to support banks and the public sector to identify emerging risks

The BBA has been pleased to play a central role in promoting partnership working between the UK Government and the banking industry to improve information sharing on financial crime, including through the new Joint Money Laundering Intelligence Task Force (JMLIT). The JMLIT has provided real benefits including:

- earlier financial crime prevention
- improved awareness across banks of financial crime risks
- information to underpin money laundering investigations
- A better relationship between banks, law enforcement and the FCA including greater commonality of view on the highest priority risks

The 6 month review of the JMLIT has demonstrated that further value could be gained through legislation and consistent supporting guidance to allow more widespread and confident information sharing. Additionally better communication activities could lead to strengthened engagement across the banking industry and law enforcement.

We understand the scope of this review is to examine the effectiveness of supervision. However, the BBA membership is of the view that the JMLIT can play a positive role in the development of a better collective understanding of the highest priority financial crime risks as a basis for a far more proportionate, targeted and ultimately effective AML/CTF system. The involvement of the FCA in the JMLIT has been very positive and much welcomed by the banking industry- helping to improve the relationship between the regulator and BBA members. **The BBA membership would support the JMLIT moving to a permanent status.**

Recommendation 5: Exchanges of knowledge on best practice to support “future proofing”

The financial crime risks and challenges posed to banks can change quickly. The digitalisation of financial services is bringing huge customer benefits but also AML/CTF considerations for firms. New criminal techniques, geo political/economic factors and new public policy matters can also alter the risks that banks need to consider.

The banking industry sees “future proofing” against emerging risks and challenges as essential to effective financial crime risk management. This allows appropriate controls to be put in place at an early stage that balance financial crime controls with other objectives such as financial inclusion and good customer service. Effective “Future Proofing” of course requires a range of activities by individual banks. However, roundtable discussions hosted by the BBA that have brought together banks, regulators, law enforcement on specific thematic issues have proven extremely valuable. **The BBA will be happy to share our programme of roundtable meetings on best practice for 2016 and to explore involvement by relevant Government bodies.**

Recommendation 6- Intensified dialogue between smaller banks and the FCA

Smaller banks that we consulted to develop this paper response described the challenges they face in meeting regulatory expectations for AML/CTF compliance. Whilst generally speaking smaller banks feel that the FCA Financial Crime Guide is quite useful, concerns were expressed around inconsistent views from the FCA on specific issues- small banks provided an example where 3 different firms had been provided with 3 differing views on a specific technical compliance point. Additionally smaller banks feel that their “voice” is insufficiently taken into account by the FCA on financial crime matters and believe that real value could be accrued from more regular dialogue with the FCA.

Smaller banks welcome the stronger focus of the BBA in representing the views and requirements of this segment of the banking industry, including in engagement on with the FCA. However, smaller banks have made 2 suggestions that could improve their dialogue with the FCA:

- **A dedicated contact point within the FCA for queries/engagement with smaller banks on financial crime compliance matters**
- **A new forum for policy engagement between the FCA and smaller banks on financial crime compliance matters (perhaps 2 x annual meetings)**

Recommendation 7: Attachments for staff in both banks and regulatory bodies (specific to financial crime)

The banking industry has sought over the past 2 years to increase the mutual understanding between law enforcement and banks of the respective drivers and requirements for addressing financial crime. The BBA and our member banks have provided a number of briefings to NCA staff in London and outside London on financial crime matters, as well as more generally on banking. Banks have seconded staff to Government bodies and a new program has been launched by the BBA to allow law enforcement staff to spend time in banks. These initiatives are helping to build relationships and experience at

more junior levels between banks and law enforcement financial crime specialists. When this is combined with the initiative of the Home Secretary and banks CEOs to promote senior level collaboration through the Serious and Organised Crime Financial Services Forum, this will provide for a far more constructive long term relationship between law enforcement and the banking industry on financial crime matters.

A number of BBA members have commented that there may be scope for considering similar arrangements to support FCA and bank staff to build their experience of the respective approaches to financial crime compliance, perhaps through short term attachments. The BBA would be pleased to engage with the FCA/Government on this.