TOPIC **23**

Anti-money-laundering

LEARNING OBJECTIVES

People working within the financial services sector can find themselves unwittingly aiding and abetting financial crime simply by processing transactions on behalf of clients. To discourage involvement in money laundering activities the penalties for individuals of failing to comply with the law in this area can be severe. It is therefore essential that you understand the rules that may apply to your daily work. In this topic our main focus is on money laundering, although we will also look briefly at the provisions of the Bribery Act 2010.

By the end of this topic you should have an understanding of:

- what money laundering is;
- the provisions of the Proceeds of Crime Act 2002;
- the provisions of the EU's Money Laundering Directives;
- the FCA's role in preventing money laundering;
- the penalties for breaching money-laundering offences;
- the provisions of the Bribery Act 2010.

This topic covers the Unit 2 syllabus learning outcomes U4.1–4.9.

THINK . . .

If you already work in financial services, you might be aware of the role of the money laundering reporting officer, or MLRO; you might also have carried out customer due diligence procedures to confirm a customer's identity.

If you don't yet work in financial services, you might have heard of money laundering in relation to crime reports in the media, or in TV and film dramas.

To start you off on this topic, think about what kind of customer behaviour might make you suspicious. Money launderers don't turn up with a large bag marked "swag" – it is a sophisticated crime – but frontline financial services staff identify thousands of potentially suspicious transactions every year and thus play a key role in crime prevention.

23.1 What is money laundering?

Money laundering involves filtering the proceeds of any kind of criminal activity (including terrorism) through a series of accounts or other financial products in order to make such funds appear legitimate or to make their origins difficult to trace. It will generally not be easy to spot someone who is trying to launder money; criminals carrying out money laundering will use sophisticated techniques. Examples of where the financial services industry has been used in an attempt to launder money include:

- opening an account with a small initial deposit and then adding large sums in cash;
- making an investment into a collective investment which is then encashed within a short period of time;
- arranging a mortgage or loan that is then quickly paid off using cash.

A significant proportion of transactions that are identified as suspicious take place in banks and reports of suspicious transactions also come in from building societies, finance companies, credit card providers, money service businesses such as bureaux de change, accountants, tax advisers, solicitors and estate agents, among others.

Financial services firms have a legal duty to take steps to mitigate the risk of money laundering; in the UK, the key legislation is the Proceeds of Crime Act 2002, the Terrorism Act 2000 and the EU's Money Laundering Directives transposed into UK law.

THE NATIONAL CRIME AGENCY

The National Crime Agency (NCA) works to combat serious and organised crime. Although it is a UK body, it works in partnership with law enforcement agencies internationally; the nature of serious and organised crime makes such cross-border co-operation essential. Its National Economic Crime Centre is responsible for tackling money laundering, fraud, bribery and corruption, and counterfeiting of currency.

23.2 What are the requirements of the Proceeds of Crime Act 2002?

Under the Proceeds of Crime Act 2002, there are three principal money laundering offences.

FIGURE 23.1 PRINCIPAL MONEY LAUNDERING OFFENCES

Concealing criminal property	Arranging	Acquiring, using or possessing
• Criminal property is property that a person knows, or suspects, to be the proceeds of any criminal activity • It is a criminal offence to conceal, disguise, convert or transfer criminal property	Arranging occurs when a person becomes involved in a process that they know or suspect will enable someone else to acquire, retain, use or control criminal property (where that other person also knew or suspected that the property derived from criminal activity)	It is a criminal offence for a person to acquire, use or possess any property when that person knows or suspects that the property is the proceeds of criminal activity

23.2.1 Failure to disclose

All suspicions of money laundering must be reported to the authorities. The Proceeds of Crime Act 2002 introduced the requirement for a person to disclose information about money laundering if they have reasonable grounds for knowing or suspecting that someone is engaged in money laundering.

23.2.2 Tipping off

It is also an offence to disclose to (ie tip off) a person who is suspected of money laundering that an investigation is being, or may be, carried out.

23.3 How does the Terrorism Act 2000 relate to money laundering?

The Terrorism Act 2000 defines ‘terrorism’ as the use or threat of serious violence against a person or serious damage to property or electronic systems, with the purpose of influencing a government, intimidating the public or advancing a political, religious or ideological cause.

The Act specifically mentions as an offence “the retention or control of terrorist property, by concealment, removal from the jurisdiction, transfer to nominees or in any other way” – in other words, money laundering.

‘Terrorist property’ is defined as:

- money or other property that is likely to be used for terrorism purposes;

- proceeds of the commission of acts of terrorism;
- proceeds of acts carried out for the purposes of terrorism.

23.4 What are the Money Laundering Regulations?

The key EU legislation relating to money laundering is the Money Laundering Regulations, which implement the EU's Money Laundering Directives.

23.4.1 Third Money Laundering Directive

The EU's Third Money Laundering Directive (2005) repealed and consolidated two earlier directives. The Directive defines money laundering in some detail. It comprises "the following conduct when committed intentionally:

- the conversion or transfer of property, knowing that such property is derived from criminal activity or from an act of participation in such activity, for the purpose of concealing or disguising the illicit origin of the property or of assisting any person who is involved in the commission of such activity to evade the legal consequences of his action;
- the concealment or disguise of the true nature, source, location, disposition, movement, rights with respect to or ownership of property, knowing that such property is derived from criminal activity or from an act of participation in such activity;
- the acquisition, possession or use of property, knowing, at the time of receipt, that such property was derived from criminal activity or from an act of participation in such activity;
- participation in, association to commit, attempts to commit and aiding, abetting, facilitating and counselling the commission of any of the actions mentioned in the foregoing paragraphs".

Three more important definitions are included, in order to clarify this definition of money laundering:

- **property** is assets of every kind, tangible or intangible, movable or immovable, as well as legal documents giving title to such assets;
- **criminal activity** is a crime as specified in the Vienna Convention (the United Nations Convention Against Illicit Traffic in Narcotic Drugs) and any other criminal activity designated as such by each member state;
- **criminal property** is defined as property that consists, directly or indirectly, wholly or in part, of a benefit from criminal conduct, where the alleged offender knows or suspects that it constitutes a benefit.

The Directive specifies that money laundering that takes place within the EU will be treated under EU money laundering rules, even if the activities that generated the property to be laundered took place in a non-EU country.

23.4.2 Fourth Money Laundering Directive

In response to recommendations made by the Financial Action Task Force (FATF), the European Commission adopted a fourth Money Laundering Directive on 26 June 2015. The provisions of the directive were implemented in the UK in June 2017 and the Money Laundering Regulations and the Proceeds of Crime Act were updated. The aim was to strengthen the anti-money-laundering (AML) regime.

Key elements of the Money Laundering Regulations 2017 include:

- a requirement to adopt a risk-based approach to the implementation of AML measures such as customer due diligence (ie to understand the nature of the threats faced and devote most resources to the areas of greatest risk). A relevant person must produce a written AML risk report and translate its findings into written policies to be approved by the firm's senior management;
- a widened definition of 'politically exposed persons', including those holding prominent positions in their home country. Politically exposed people are those individuals who, because of their position, are considered to be more vulnerable to corruption;
- the introduction of a new criminal offence. An individual found guilty of recklessly making a statement in the context of money laundering that is false or misleading may face a fine and/or a maximum two-year jail sentence.

The fourth Money Laundering Directive also:

- includes 'tax crimes' within EU legislation for the first time;
- strengthens co-operation between member states;
- increases transparency around the beneficial ownership of legal entities – each member state must maintain a central register of the beneficial owners of legal entities (beneficial owners are those who own or control 25 per cent of a legal entity).

In the UK, legislation requiring businesses to maintain a register of individuals having significant control came into effect in April 2016. This had to be strengthened as it only applied to companies, not to other legal entities such as trusts and therefore did not fully meet the requirements of the Fourth Money Laundering Directive.

The Money Laundering and Transfer of Funds (Information) (Amendment) (EU Exit) Regulations 2018, published on 13 November 2018, ensures that the UK's anti-money-laundering regime and counter-terrorism financing legislation continues to work effectively even though the UK withdrew from the EU.

23.4.3 Fifth Money Laundering Directive

The Fifth Money Laundering Directive came into force in the UK on 10 January 2020. The scope of the new directive was broadened to include additional entities, such as virtual currency providers, art traders for transactions of €10,000 or more and estate agents acting as intermediaries for properties let at €10,000 per month.

It also introduced changes regarding electronic money, including:

- A new maximum monthly payment transaction limit of €150 for non-reloadable payment instruments, and where the maximum amount stored electronically exceeds €150, they are now subject to customer due diligence (CDD) measures. The threshold has been reduced from €250 to €150.
- Remote payment transactions that exceed €50 are subjected to customer due diligence measures. The threshold has been reduced from €100 to €50.

The directive also introduced changes to customer due diligence and beneficial ownership registers, such as:

- The identification and verification of customers must be based on documents, data or information from a reliable and independent source, which should also include electronic identification means that have been approved by national authorities.
- Any member of the public has the right to access beneficial ownership information held in the register for corporate and other legal entities. Access is no longer limited to persons who can demonstrate legitimate interests.
- Implementing requirements to harmonise the enhanced due diligence (EDD) measures for entities across member states to apply to business relationships with high risk third countries (Deloitte, 2018).

The UK has opted out of the Sixth Money Laundering Directive (implemented in the EU in June 2021) as many of its requirements are already covered in existing UK law. However, any UK regulated business in the financial sector operating in the EU must comply.

FINANCIAL ACTION TASK FORCE

The Financial Action Task Force (FATF) is an inter-governmental organisation established in 1989 to co-ordinate the international fight against money laundering. In 2001, the remit of the FATF was expanded to include terrorist financing. It is a policy-making body: it does not become involved in law enforcement (that is the responsibility of local authorities in individual countries, such as the National Crime Agency in the UK). In addition to member nation states, the European Commission and the Gulf Co-operation Council also belong to the FATF.

The work of the FATF falls into four main areas:

- identifying trends in money-laundering methods;
- setting the standards for national anti-money-laundering programmes;
- evaluating the extent to which individual countries have implemented the standards;
- identifying high-risk jurisdictions (countries it considers not to have adequate anti-money-laundering measures).

To find out more about the FATF, you can visit:

www.fatf-gafi.org/en/home.html

23.5 Customer due diligence

One of the most important elements in the financial service industry's action against money laundering is the process of confirming the identity of customers, referred to as 'customer due diligence' or CDD. CDD is required in relation to transactions that are seen as higher risk. Figure 23.2 summarises the circumstances in which evidence of identity is required.

FIGURE 23.2 CIRCUMSTANCES REQUIRING IDENTIFICATION PROCEDURES TO BE CARRIED OUT

New business relationship

When entering into a new business relationship (particularly when opening a new account, or selling a new investment or policy).

Occasional transaction exceeding €15,000

When the value of an 'occasional' transaction exceeds €15,000, whether as a single transaction or as a series of linked transactions. Note that for a business trading in goods and services the threshold is €10,000.

Life assurance policies

When the value of annual premiums exceeds €1,000, or €2,500 for single premiums.

Suspicion

In every case where there is suspicion of money laundering or terrorist financing. If there is suspicion that the applicant may not be acting on their own behalf, reasonable measures must be taken to identify the person on whose behalf the applicant is acting.

Doubts

Where there are doubts about proof of identity that has previously been obtained.

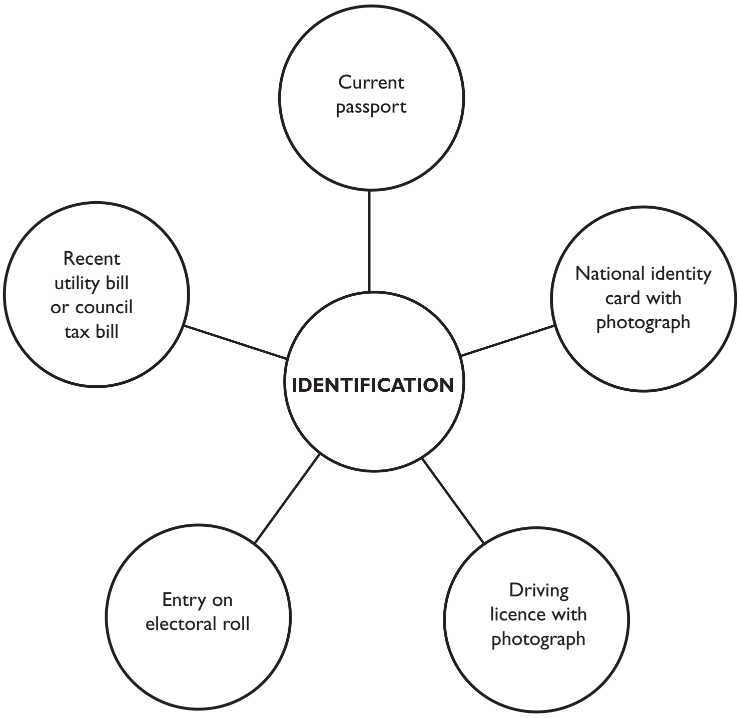
Change of circumstances

Where a change in the circumstances of an existing customer requires new evidence to be obtained.

If a client is introduced to the firm by a financial intermediary or another authorised firm, it is permissible for the firm to rely on identification carried out by the intermediary or other firm. This is important to, for instance, financial advisers and mortgage advisers. Under the terms of the Money Laundering Regulations 2017, an intermediary must provide the customer with the due diligence information it has obtained.

The definition of what constitutes satisfactory evidence of identity is rather vague – evidence should be reasonably capable of establishing that the applicant is the person they claim to be, to the satisfaction of the person who obtains the evidence. Acceptable forms of identification are shown in Figure 23.3.

FIGURE 23.3 ACCEPTABLE FORMS OF IDENTIFICATION



23.5.1 Preventing financial exclusion

Some people's personal circumstances are such that they are unable to provide any of the documents included in Figure 23.3. For instance, a person who has never travelled abroad, does not drive a car and is not responsible for household bills may well be unable to produce a passport, driving licence or utility bill bearing their name. Nevertheless, it is important that people in these situations are not denied access to appropriate financial services. In such circumstances, the FCA considers that a firm may accept, as evidence of the customer's identification, a letter or statement from a person in a position of responsibility (such as a solicitor, doctor or minister of religion) who knows the client.

RECORD-KEEPING REQUIREMENTS

Institutions must keep appropriate records in respect of customer due diligence for use as evidence in any investigation into money laundering. This means that:

- evidence of identification must be retained until at least five years after the relationship with the customer has ended;

- supporting evidence of transactions (in the form of originals or copies admissible in court proceedings) must be retained until at least five years after the transaction was executed.

Remember also that there are record-keeping requirements that relate to COBS (see Topic 21), and we will look in Topic 24 at the requirements in relation to the UK GDPR.

23.5.2 Credit reference agencies

Anti-money-laundering checks are often carried out by credit reference agencies on behalf of financial institutions. While the search leaves an anti-money-laundering ID footprint, this will not show up in a credit search, nor will it affect an individual's ability to obtain credit.

23.6 What is the role of the FCA?

The FCA has an operational objective to ensure the integrity of financial markets. To help achieve this, the FCA requires that all authorised firms must have systems and controls in place which mitigate the risk that the firms may be used to commit financial crime, including money laundering.

The FCA details its requirements in the Senior Management Arrangements, Systems and Controls (SYSC) section of the Handbook and requires that all authorised firms:

- establish accountabilities, procedures and systems to minimise the risk of money laundering;
- give responsibility for anti-money-laundering systems and controls to a senior manager;
- appoint a money laundering reporting officer (MLRO) (see section 23.6.1);
- have a documented risk policy related to money laundering;
- give regular training to staff about what is expected of them under the money-laundering rules, including the consequences for the firm and for themselves if they fail to comply;
- educate their staff about potential problems;
- take reasonable steps to ensure that procedures are up to date and reflect any findings contained in periodic reports on money-laundering matters

issued by the government, by the Financial Action Task Force (FATF) and the FCA's own guidance on financial crime;

- requisition a report at least once in each calendar year from the MLRO;
- take appropriate action to strengthen its procedures and controls to remedy any deficiencies identified by the report.

The FCA expects that firms have procedures in place to ensure that individuals working within the firm:

- report suspicious circumstances by completing 'suspicious activity reports' (SARs);
- refrain from alerting persons being investigated.

The FCA has the power to take enforcement action against firms and to impose sanctions on them for non-compliance with Money Laundering Regulations.

When assessing a firm's compliance with its money-laundering requirements, the FCA will take into account the extent to which the firm has followed the:

- **Joint Money Laundering Steering Group's guidance notes** for the financial sector – these describe the steps that firms should take to verify the identity of their customers and to confirm the source of their customers' funds;
- **publications of the FATF** – these highlight any known developments in money laundering and any deficiencies in the money-laundering rules of other jurisdictions;
- **FCA's own guidance on financial exclusion** – see section 23.5.1.

JOINT MONEY LAUNDERING STEERING GROUP

The Joint Money Laundering Steering Group is made up of the leading UK trade associations in the financial services industry. Its aim is to promote good practice in countering money laundering and to give practical assistance in interpreting the UK money-laundering regulations. This is primarily achieved by the publication of guidance notes.

FACTFIND

If you are interested in finding out more about the FCA's guidance to firms on preventing financial crime, go to:

www.handbook.fca.org.uk/handbook/FCG.pdf

You might also find the following link useful:

www.handbook.fca.org.uk/handbook/SYSC/6/3.html

23.6.1 What is the role of the MLRO?

Each firm must appoint a money laundering reporting officer (MLRO) with responsibility for co-ordinating all the firm's AML activities. The MLRO must be a person of 'appropriate seniority'.

All members of staff must make a report to the MLRO if they know or suspect that a client is engaged in money laundering. The MLRO will then determine whether to report this to the National Crime Agency, using known information about the financial circumstances of the client and the nature of the business being transacted. Such reports are known as 'suspicious activity reports' (SARs).

At least once in each calendar year senior management of the firm must requisition a report from the MLRO. This report must:

- assess the firm's compliance with the Joint Money Laundering Steering Group guidance notes;
- indicate how Financial Action Task Force findings have been used during the year;
- provide information about reports of suspected money-laundering incidents submitted by staff during the year.

A firm's senior management must consider this report and must take any action necessary to solve any problems identified.

23.6.2 What training is required?

Training should be given on a regular basis throughout the time that an individual handles transactions that could facilitate money laundering.

FIGURE 23.4 AML TRAINING REQUIREMENTS

Firms must ...

- Take appropriate measures to make employees aware of money-laundering procedures and legislation
- Provide training in the recognition and handling of money-laundering transactions

Staff must be made aware of ...

- The law relating to money laundering
- The firm's procedures and staff individual responsibilities
- The identity of the firm's MLRO and what their responsibilities are
- How any breach of money-laundering rules can impact on the firm and on themselves, ie the consequences of committing what may be a criminal act

PENALTIES FOR MONEY-LAUNDERING OFFENCES

The FCA can discipline firms and individuals for breaches of money-laundering rules, as described in section 23.6. It also has the power to prosecute anyone who breaks the Money Laundering Regulations established under UK law to give effect to the EU Money Laundering Directives.

Anyone convicted under the Proceeds of Crime Act 2002 of concealing, arranging or acquiring (see section 23.2) could be sentenced to up to 14 years' imprisonment or an unlimited fine, or both. The offence of failing to disclose or of tipping off carries a prison sentence of up to five years or an unlimited fine, or both.

A partner or director who fails to comply with money laundering regulations can be fined, receive up to two years in prison (or both) or be subject to appropriate civil penalties.

23.7 The Bribery Act 2010

The Bribery Act 2010, which came into effect in July 2011, created an offence of offering, promising or giving "financial or other advantage" to another where the advantage is intended to bring about improper performance by another person of a relevant function or activity, or to reward such improper performance.

An offence is also deemed to have been committed if the person offering, promising or giving the advantage knows (or simply believes) that acceptance of the advantage itself constitutes improper performance.

IMPROPER PERFORMANCE

Performance that amounts to a breach of an expectation that a person will act in good faith, impartially or in accordance with a position of trust.

The test used is what a reasonable person in the UK would expect of a person performing the relevant function or activity.

The offence applies to bribery relating to any function of a public nature, connected with a business, performed in the course of a person's employment or performed on behalf of a company or other body.

The function or activity may be carried out either in the UK or abroad, and need have no connection with the UK.

The Act also makes it an offence to request, agree to receive, or accept "financial or other advantage", where the person requesting the 'bribe' performs their function or activity improperly (or intends to) as a result of the 'reward' requested or received.

The maximum penalty in the UK for an individual convicted of a bribery offence is an unlimited fine and imprisonment for up to ten years.

THINK AGAIN ...

Now that you have completed this topic, how has your knowledge and understanding improved? For instance, can you:

- name the three principal money laundering offences?
- explain what is meant by 'failure to disclose' and 'tipping off'?
- describe the role of the money-laundering reporting officer?
- explain the circumstances in which you would be required to carry out customer due diligence?
- outline the offences and penalties under the Bribery Act?

Go back over any points you don't understand and make notes to help you revise.

Test your knowledge before moving on to the next topic.

References

Deloitte (2018) *The 5th anti-money laundering directive* [pdf]. Available at: www2.deloitte.com/content/dam/Deloitte/uk/Documents/financial-services/deloitte-uk-fs-5th-anti-money-laundering-directive.pdf

Test your knowledge

?

Use these questions to assess your learning for Topic 23. Review the text if necessary.

Answers can be found at the end of this book.

1) If a staff member of a financial services organisation were to be accused of 'arranging' under the Proceeds of Crime Act 2002, it could mean that they:

   a) had knowingly become involved in the process of converting criminal property.

   b) personally owned the proceeds of criminal activity.

   c) had unwittingly failed to report a potentially suspicious transaction.

   d) had personally used the proceeds of criminal activity.

2) Transferring criminally obtained money through different accounts is an offence only if the funds derive from drug dealing or terrorist activity. True or false?

3) The FATF's role is to establish a broad policy framework at an international level for the prevention of money laundering. True or false?

4) In order to be required to report a transaction to the money laundering reporting officer, a member of staff first needs to:

   a) be certain that the person is involved in money laundering.

   b) advise the person that they may be investigated.

   c) review the circumstances of the case with other experienced staff members.

   d) have reasonable grounds for believing that a person is involved in money laundering.

5) A bank cashier notices that a customer is paying an unusually large sum of money into their account in cash. The cashier advises the customer that they regard the transaction as suspicious and calls a supervisor to discuss the matter further with the customer. What offence has the cashier potentially committed?

   a) Data protection breach.

   b) Tipping off.

c) Failure to disclose.

d) Arranging.

6) When accepting an investment into a savings account at what transaction value will it become necessary to obtain evidence of the customer's identity?

a) €15,000.

b) €10,000.

c) £10,000.

d) £15,000.

7) The EU Fourth Money Laundering Directive contains a provision requiring member states to maintain a register of the beneficial owners of legal entities. A beneficial owner is one who controls what percentage of a legal entity?

8) A new client has invested £12,000 in the forms of stocks and shares in an ISA product offered by Forward Bank. The bank did not carry out any client identification procedures. This is most likely to have been because:

a) investments into ISAs are exempt from money-laundering identification requirements.

b) the client is only temporarily resident in the UK.

c) investment amounts of less than £15,000 are exempt from money-laundering identification requirements.

d) the client was introduced by an intermediary who obtained the necessary evidence.

9) If a money laundering reporting officer (MLRO) suspects a case of attempted money laundering, to whom must this be reported?

10) A firm's senior management is required to request a report from the money laundering reporting officer at least once a year. What action should they take on receiving the report?

a) Forward it to the FCA.

b) Include the total number of SARs in the firm's annual report and accounts.

c) Review and if necessary improve the firm's processes and training.

d) Retain the report indefinitely.