



HM TREASURY

# Review of the Money Laundering Regulations 2007:

**the Government response**

June 2011





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# Introduction

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This is the Government response to the 2009/10 Review of the Money Laundering Regulations 2007 (the Regulations). It includes a series of consultative proposals to amend the Regulations.

The review followed a commitment made in 2007 to carry out this process two years after the introduction of the Regulations. It has been informed by a Call for Evidence and by a large number of sector specific meetings with interested parties.

The objective of the review was to assess the extent to which the implementation of the Regulations reflects the principles of effectiveness, proportionality and engagement in practice.

Chapter 1 of this document explains the background to the review in detail.

Chapter 2 explains the arrangements for the consultation on the proposed changes to the Regulations.

This document then addresses a range of operational or procedural issues involving supervision and enforcement, guidance; and the use of simplification or facilitation measures like reliance and equivalence.

In chapter 3 the Government response and proposals for consultation on changes to the Regulations are given, following a summary of the information and views received. The changes proposed are to ensure that the regime delivers as intended, stays up to date, and is effective and proportionate.

In chapters 4 to 9, a more detailed Government response is given to the main themes of the comments received to the Call for Evidence, following a short summary of the those views. They are in each of the following areas:

- Chapter 4 The risk-based approach;
- Chapter 5 Simplification and deregulatory provisions;
- Chapter 6 Customer due diligence;
- Chapter 7 Guidance;
- Chapter 8 Supervision; and
- Chapter 9 Engagement.

Responses about the customer experience were made in relation to many of these areas and are discussed, accordingly, in each.

There is a summary list of the consultation questions in Annex C.

## Money laundering and terrorist finance

The Regulations address the threats from money laundering and terrorist finance. For brevity reference is generally made in this paper to 'money laundering' or to the anti-money laundering (AML) regime, but that term should be understood as embracing terrorist financing.



# Executive summary

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The Government's approach is to ensure the UK financial system is a hostile environment for money laundering and terrorist finance while minimising the burden on legitimate businesses. In so doing and in order to prevent the UK being put at an economic disadvantage, the UK Government remains committed to the effective implementation of global standards (those agreed by the 36 Member States of the Financial Action Task Force) and the EU 3rd Money Laundering Directive (EU Directive).

The implementation of these requirements by the UK is underpinned by the principles of effectiveness, proportionality and engagement; and is driven by a commitment to the **risk-based approach** provided for in the Regulations. This gives businesses flexibility in their implementation of the Regulations and it helps to avoid the 'tick-box' application of the regulations under which emphasis is placed on formally discharging requirements rather than the substance of effective AML practice. It should help to minimise costs on business and to ensure the Regulations are effective and proportionately implemented on a case-by-case basis, by reflecting the considered judgement of individual businesses of the risks they face.

The risk-based approach is complemented by **self-regulation**, with as many businesses as possible (i.e. as allowed under the EU Directive) regulated by their professional body. The Government will seek to build on this where possible, including through working within the EU on future Directives.

## The review

The Government is grateful to everyone who has contributed to the review and is continuing to inform and support the Government response to this, and is grateful for the ongoing dialogue with all stakeholders to ensure the Regulations are as effective and proportionate as possible.

We welcome the reassurance the review provides, for example about the level of support in principle for the UK's approach, including the risk-based approach, the role of guidance, and Government's engagement with businesses and other stakeholders.

The review has identified where there is potential to improve the Regulations. More information on such improvements is sought through the consultation incorporated in this response.

## Assessment of the regulations

The Government's assessment is that overall the Regulations are effective and proportionate at an aggregate level. The risk to the UK from money laundering and terrorist financing remains significant.<sup>1</sup> The Government recognises that more needs to be done to communicate the benefits of the Regulations and of the wider AML regime of which they are a part and will continue to support efforts to improve this.

The joint government, law enforcement and industry body that oversees the AML regime in the UK, the Money Laundering Advisory Committee, has looked closely at efforts to provide a credible overall estimate of costs and benefits. There is wide consensus that there are inherent

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<sup>1</sup> <http://www.soca.gov.uk/threats>  
[http://www.fatf-gafi.org/documents/51/0.3343.en\\_32250379\\_32237202\\_45724403\\_1\\_1\\_1\\_1.00&en\\_USS\\_01DBC.html](http://www.fatf-gafi.org/documents/51/0.3343.en_32250379_32237202_45724403_1_1_1_1.00&en_USS_01DBC.html)

challenges in doing this and that our collective resources are best focused on improving the effectiveness of the regime.

## **The burden on business**

Businesses face difficulties separating the costs of complying with the Regulations from other costs of doing business. This includes the costs of other legislation, including sanctions, as well as commercially driven due diligence, and systems and controls designed to help protect businesses and their customers from fraud and other criminal activity. While it may not be possible to reach a useful estimate of costs, the Government continues to welcome further information on the costs faced by individual businesses as a result of the Regulations.

The benefits to the UK are considered to be very significant. They include the contribution the Regulations make to tackling and deterring all types of crime and terrorism, assisting in the seizure and recovery of criminal assets, and the wider reputational benefits to the UK and its regulated sector - which are likely to be far greater than the value of criminal assets seized or denied, but are difficult to quantify.

However the Government remains committed to building the best possible understanding of the costs of specific changes to the Regulations and to communicating the benefits of the Regulations and the wider anti-AML regime of which they are a part. This response forms part of that process. The Government will continue to work with partners across Government, law enforcement, supervisors and industry to achieve these goals.

The issues considered under the review are looked at in this response under a number of areas. They include the risk-based approach, simplification provisions, customer due diligence, guidance, supervision and engagement between the Government and stakeholders.

## **The risk based approach**

Responses to the Call for Evidence, mainly from regulated businesses, were largely supportive of the risk-based approach.

A number of specific barriers to a risk-based approach have been identified and are discussed in this document. The Government encourages the fullest possible use of the risk-based approach by businesses and is committed to reducing or removing barriers to this wherever possible.

## **Simplification issues**

Businesses cite real difficulties complying with the beneficial ownership and 'politically exposed persons' (PEPs) requirements in some circumstances, such as when dealing with trusts and large publicly owned companies.

The difficulties businesses face giving practical effect to the various simplification arrangements in the Regulations are also recognised. The Government attaches considerable importance to the practical implementation of those arrangements, as the duplication of checks can be unnecessary, costly for businesses and frustrating for customers.

## **Customer due diligence**

Many businesses reported that their customers were accustomed to the demands made of them to establish their identity and were largely accepting or understanding of the need for these.

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 identify 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.

Representations were made on behalf of British nationals living abroad and other customers who feel potentially excluded from financial or professional services as a result of the Regulations. The Regulations do not place any requirements on businesses that should lead to such customers being excluded, nor do they require businesses to discriminate against overseas customers. Financial services businesses, for example, have access to guidance that specifically encourages businesses to ensure their services are available as widely as possible to all, and to have regard to a wide range of evidential documents.

Law enforcement agencies identified the significant benefits brought by compliance with the Regulations by businesses, including supporting the identification of suspicious activity, improving the quality of suspicious activity reports (SARs) and helping ensure information is available to assist with investigations.<sup>2</sup>

## **Guidance**

On the whole, views held by supervisors, businesses and industry bodies about guidance are positive. Evidence generally supports the view that guidance promotes an effective and proportionate approach to the Regulations and it is useful that guidance is legally recognised in the UK, so that following guidance can be used as a defence against prosecution for non-compliance.

There was some criticism that guidance could be overly focussed on large financial sector businesses. Some stakeholders also find it too lengthy, and at times unhelpfully vague.

## **Supervision**

With regard to supervision, it is clear that there is a wide range of activity to support and monitor regulated businesses. On the other hand, there is a sense that more could be done, particularly around consistency of supervisors (in terms of guidance, compliance monitoring and enforcement) and to support a risk-based, proportionate and effective approach to compliance and enforcement.

## **Government – stakeholder engagement**

On balance, the level of engagement for the Regulations is generally considered to be good. There was extensive dialogue prior to the introduction of the Regulations and a good level of ongoing engagement has continued since. At a supervisor - firm level there has been considerable engagement including opportunities to contribute to the development of guidance.

There are areas where the picture is less positive, with some sectors or businesses reporting a lack of engagement. This suggests there is room for improvement. This includes engagement with small and medium sized businesses, specific groups such as intermediaries or sectors such as gaming, and scope for additional engagement and dialogue between regulated businesses and their supervisors, in some sectors.

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<sup>2</sup> <http://www.soca.gov.uk/news/298-suspicious-activity-reports-regime-annual-report-2010-published>

Extensive engagement has been a significant feature of the review itself. The Call for Evidence was distributed to a large number of stakeholders including other Government Departments, supervisors and industry associations and a large number of events held for stakeholders throughout the UK.

The Government will continue to seek improvements to the effectiveness and proportionality of the Regulations, reducing the costs faced by regulated businesses and their customers where possible. The Government will continue to report on the outcome of our work with law enforcement, supervisors and businesses on a regular basis through the public and private sector forums and channels the Government is actively engaged in. This includes the Money Laundering Advisory Committee, the Supervisors Forum, a variety of industry sector specific forums and events, as well as updates to the Treasury website<sup>3</sup> and through information available from supervisors and industry bodies.

The Government will work with other EU Member States and members of the Financial Action Task Force (FATF), to address issues affecting the UK. The evidence received during the review has already made a significant contribution to the review of the FATF standards<sup>4</sup> in areas such as the risk-based approach, simplified due diligence, beneficial ownership and PEP's.

The responses to the Call for Evidence and a summary of these were published in 2010 and are available on the National Archives website.<sup>5</sup>

## Other issues

While the review was focused on the implementation of the Regulations and did not extend to related legislation under which, for example, suspicious activity reports must be made, (Proceeds of Crime Act 2002), the Government recognises that the Regulations are part of the same regime and do not exist in isolation. In the workshops held with industry and in the written evidence received, a number of issues were raised, such as the "all crimes" approach to suspicious activity reporting, and the absence of de-minimis limits for reporting (so that all suspicions should be reported regardless of the size of the suspected crime). These are not new issues and were addressed in the Government reply<sup>6</sup> to the House of Lords inquiry<sup>7</sup> in 2009. It is also important to note that there were significant representations both in favour and against changes to the approach taken in these areas. Banks and accountants are generally in favour of the current approach.

The information gathered during the review is available to the Home Office and SOCA, for further consideration as appropriate. In addition, issues relating to the wider AML regime are the subject of ongoing focus by the Money Laundering Advisory Committee, which is co-chaired by the Home Office and the Treasury and includes law enforcement and industry representatives.

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<sup>3</sup> [http://www.hm-treasury.gov.uk/fin\\_money\\_index.htm](http://www.hm-treasury.gov.uk/fin_money_index.htm)

<sup>4</sup> <http://www.fatf-gafi.org>

<sup>5</sup> [http://webarchive.nationalarchives.gov.uk/20100407010852/http://www.hm-treasury.gov.uk/fin\\_crime\\_review.htm](http://webarchive.nationalarchives.gov.uk/20100407010852/http://www.hm-treasury.gov.uk/fin_crime_review.htm)

<sup>6</sup> <http://www.official-documents.gov.uk/document/cm77/7718/7718.asp>

<sup>7</sup> <http://www.publications.parliament.uk/pa/ld200809/ldselect/ldcom/132/13204.htm>

# 1

## Background to the review

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**1.1** The Treasury, with support from the Better Regulation Executive, has undertaken a review of the Regulations, which implemented the EU's Third Money Laundering Directive in the UK and replaced the 2003 legislation with a simplified, more risk-based approach.

**1.2** This document brings together evidence and information gathered across three distinct avenues of enquiry:

- Call for Evidence
- Stakeholder meetings and discussion forums
- Supplementary research / macro analysis

**1.3** The review has considered the Regulations in relation to the three guiding principles of effectiveness, proportionality and engagement. The aim of the review has been to assess where the Regulations are working well and identify possible areas for improvement.

### Sources of Evidence

**1.4** A Call for Evidence ran between 9 October and 11 December 2009 to seek stakeholder views on all aspects of the Regulations including guidance, supervision and the practical application of the regulations. This was published in two parts aimed at regulated businesses and other organisations, and consumers respectively. The Call for Evidence was distributed directly to thousands of stakeholders across the public, private and third sectors and responses were received from a wide range of stakeholders including regulated businesses, supervisors, private individuals, third sector organisations, academics and law enforcement agencies. It was also advertised to the public and others through the press.

**1.5** Submissions received in response to the call were published in April 2010. Statistics on who responded are provided in Annex A.

**1.6** During that same period meetings and discussion forums were held to capture the views of stakeholders on the ground, particularly regulated businesses whose views are often channelled through third party organisations such as industry bodies. These bodies play an important role, not least in reducing the burden on businesses to respond to Government across a range of issues. But since part of the purpose of the review was to understand how the Regulations work in practice, it was important to meet with the businesses and individuals that are directly affected by the Regulations.

**1.7** More than 250 stakeholders in the public, private and third sectors attended meetings as part of the review, mostly arranged through industry bodies and trade associations. This included regulated businesses, supervisors and customers (businesses and private individuals or representative bodies). Meetings were generally held under the Chatham House rule encouraging a frank and open discussion. A list of meetings held is provided in Annex B.

## Recent developments

**1.8** The launch in 2010 of a new government website, Your Freedom<sup>1</sup>, sought views on legislation that was seen as inimical to freedom of the individual or caused excessive “red tape”. A number of submissions to the site commented on aspects of the AML regime in the UK. Many of these were not directly focussed on the Regulations. However, at least one submission is addressed by a proposal for legislative change (relating to non-lending credit institutions). Issues raised in other submissions may be best addressed by education and awareness raising activities by the Government, supervisors and law enforcement agencies. This requires greater effort by all those responsible for the regime, to communicate effectively to the wider public and the large number of smaller businesses that are affected by the regime.

**1.9** The Government has introduced new measures to reduce the burden of regulations on businesses generally. While the proposals for change have the overall effect of reducing the costs on businesses, this response and the proposals it contains for changes to the Regulations have been subject to a number of new challenge functions and to scrutiny by a range of interested parties, including the Regulatory Policy Committee and the Reducing Regulation Committee.

**1.10** The improvements to the Regulations proposed in this response are subject to the ‘one-in one-out’ rule whereby any of the changes to regulation that may have the effect of increasing costs on businesses (‘ins’) can only be proposed if at the same time other proposals are made that have the impact of reducing the costs on businesses (‘outs’) by at least the same value. The Government believes that that proposals made have the overall effect of reducing the costs of the Regulations on businesses.

**1.11** The Government remains committed to a policy of not gold-plating EU Directives. This response and the proposals it contains is consistent with that policy. This has limited the extent that proposals made by stakeholders can be consulted on at this time. Examples include arguments made for the regulation of letting agents and for changes to the definition of PEPs.

## Future developments

**1.12** As noted in the ‘Other issues’ section of the Executive Summary, many responses were received about elements of the regime, other than the Regulations, and about the requirement to report suspicious activity to SOCA.

It is worth noting that in addition to the substantial effort SOCA has made to engage with the regulated sector since it was created in 2006, it has also made a substantial investment in the infrastructure required to make the best use of SARs. This will enable a step change in the use of SARs by end-users, further improving the effectiveness of the AML regime.

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<sup>1</sup> <http://yourfreedom.hmg.gov.uk/>

# 2

## About the consultation proposals

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### Summary

**2.1** This document identifies potential changes to the Regulations.

**2.2** Your views are sought on the potential changes identified. The objective of the review is to ensure the regime is kept up to date, effective and proportionate. A number of the issues addressed were raised in responses to the Call for Evidence, so this consultation exercise will provide the first opportunity for comments from interested parties in those cases. Responses to this consultation will then be used to inform final Government proposals in due course.

**2.3** There is a summary of the consultation issues in Annex C

### Who do the proposals effect?

**2.4** The proposals will be especially of interest to

- Currently regulated businesses who will continue to be regulated, because of the proposed changes to the operation of the UK regime;
- Currently regulated businesses who may cease to be regulated, such as non-lending credit institutions; and
- Currently unregulated businesses that are brought into regulation for the first time, i.e. estate agents that deal in overseas property.
- The proposals will also be of interest to others with an interest in the UK AML regime.

### Impact assessment

**2.5** An impact assessment has been separately published in conjunction with this document. It sets out our preliminary views on the costs and benefits of our specific proposals. The impact assessment is available electronically at [http://www.hm-treasury.gov.uk/fin\\_gov\\_response\\_money\\_laundering\\_regs.htm](http://www.hm-treasury.gov.uk/fin_gov_response_money_laundering_regs.htm). We welcome views on the impact assessment (see below).

### Your views are sought

**2.6** We welcome your views,

- 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?
- In policy terms, are the options appropriate and consistent with our broader priorities for an effective and proportionate AML regime?
- Will the proposals result in more or less costs for business and other interested parties? In particular, we welcome views and further information, including

estimates of costs or benefits to individual businesses, to inform credible estimates in the Impact Assessment.

**2.7** The main proposals are in areas of the Regulations where we received a significant amount of feedback and views during the review.

**2.8** In most cases there were reasoned arguments by significant stakeholders both for and against change.

**2.9** Further views would be welcomed therefore, including examples of how the proposed changes may help or hinder the AML regime in the UK in practice. This will help ensure evidence-based policy decisions in these areas.

**2.10** We welcome your views on the potential changes discussed in this paper and on the impact assessment by 30 August 2011. Comments should be sent, ideally in electronic form, to [MLR.review@hmtreasury.gsi.gov.uk](mailto:MLR.review@hmtreasury.gsi.gov.uk)

**2.11** Questions or enquiries should also be sent to that email address. Please include the words CONSULTATION VIEWS or CONSULTATION ENQUIRY (as appropriate) in your email title.

**2.12** Hard copy responses may be sent to -

The Money Laundering Review  
Room 3/15, HM Treasury  
1 Horse Guards Road  
London SW1A 2HQ

## **Confidentiality and Disclosure policy**

**2.13** Information provided in response to this consultation, including personal information, might be published or disclosed in accordance with the access to information regimes. These are primarily the Freedom of Information Act 2000 (FOIA), the Data Protection Act (DPA) and the Environmental Information Regulations 2004. If you want the information that you provide to be treated as confidential, please be aware that, under the FOIA, there is a statutory Code of Practice with which public authorities must comply with and which deals, amongst other things with obligations of confidence. In view of this it would be helpful if you could explain to us why you regard the information you have provided as confidential. If we receive a request for disclosure of the information we will take full account of your explanation, but we cannot give an assurance that confidentiality will be maintained in all circumstances.

**2.14** An automatic confidentiality disclaimer generated by your IT system will not, of itself, be regarded as binding on the Department. Your personal data will be processed in accordance with the DPA, and in the majority of circumstances, this will mean that your personal data will not be disclosed.

## **Timetable**

**2.15** The closing date for comments to be submitted is 30 August 2011.

**2.16** Subject to final decisions we would anticipate any legislative changes adopted to come into effect in 2012.

# 3

## The Regulations and proposals for consultation

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### Responses to the Call for Evidence

**3.1** There were requests for specific sectors to be included or excluded from the Regulations. Some thought that the following sectors or activities should not be subject to the Regulations:

- non-lending credit operators;
- pawnbrokers;
- debt purchase operators;
- estate agents;
- financial intermediaries; and
- very small business, e.g. small bookkeepers / sole accountancy practitioners.

**3.2** Some thought the following sectors or activities should be subject to the Regulations:

- clearing houses / London stock exchange;
- online gambling businesses;
- betting shops; and
- letting agents.

**3.3** More regulation of high value dealers is sought by some, including the regulation of those who provide services rather than goods.

### The Government Response

**3.4** Some of the arguments put forward for sectors or activities to be exempt from the Regulations centre on those not involved in cash transactions – estate agents and financial intermediaries for example. The Regulations, the EU Directive and the global standards from which they flow, are not only concerned with cash flows. They are more broadly focused on all parties to a transaction, including those that do not handle cash but play a role in facilitating the transaction and are well placed to spot suspicious activity.

**3.5** Where appropriate, the Government will continue to work with law enforcement agencies, supervisors and the regulated sectors to raise awareness of the risks and to see if more can be done to ensure the implementation of the Regulations is proportionate to those risks.

**3.6** Non-lending credit institutions are currently captured due to the way the Regulations define consumer credit activities<sup>1</sup> by the holding of a consumer credit licence as certain of these businesses do, i.e. by virtue of allowing extended payment terms. As a result non-lending credit

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<sup>1</sup> See Regulation 22(1)

institutions such as gyms who permit annual membership to be paid in instalments or veterinary clinics that allow clients to spread the cost of their bills across multiple payments, have unintentionally fallen under the scope of the regulations. These businesses do not grant credit in the form of cash loans. The Government propose to exempt these businesses from the Regulations.

**3.7** Pawnbrokers were the subject of responses arguing for an exemption from the Regulations on the basis that asset-backed, low value transactions present a low risk of money laundering and incentives already exist to refuse stolen property.

**3.8** The Government does not think excluding pawnbrokers is an option in this case. Unlike non-lending credit institutions, they do provide loans and are at risk from criminals who may seek to monetise stolen property. However the Government encourages the supervisor, the OFT in this case, to consider further what might be done to ensure that implementation of the Regulations is proportionate to the risks faced in this sector.

**3.9** Debt purchase operators argue that they operate in a low risk secondary financial market and the London Market Association argue that there is unnecessary duplication of CDD checks in this market. The Government encourages the supervisor to ensure that the Regulations are implemented in proportion to the risks faced in this sector. In addition, and as discussed later, the Government will seek to do more to encourage the use of existing provisions in the Regulations for businesses to rely on due diligence already carried out by regulated 3rd parties.

**3.10** Estate Agents in the UK argue that they should not be subject to the Regulations. They believe that the nature of estate agents' business in the UK means the sector is at low risk of being used to launder money. They argue that this is because they operate differently from the Continental European system, do not hold clients' money, and that they do not see suspicious activity. They also point to the need for other parties to the transaction to carry out checks (such as banks and lawyers), making further checks redundant and disproportionate.

**3.11** The use of property at the integration stage of money laundering is well documented. Estate Agents have been subject to the Regulations since 2003 and supervised for their anti-money laundering policies and processes since 2007. Their inclusion followed the transposition of the 2nd Money Laundering Directive, which in turn followed FATF's recommendation 12-b. FATF Recommendations do not allow for Designated Non-Financial Businesses or Professions, such as estate agents, to be exempted from the Regulations. This is because they are deemed to present specific systemic risks.

**3.12** The UK has not gone beyond the requirements of the EU Directive and hence the Regulations only require checks to be carried out on the agent's customer, typically the seller. The FATF standards require checks on both the buyer and seller. The UK was subject to criticism from the FATF in its mutual evaluation for failing to require checks on the buyer. While there is also an argument for the Regulations to be strengthened, the Government recognises that regulated businesses are already encouraged by industry guidance to carry out checks on the buyer.

**3.13** Proposals were made that certain financial intermediaries (typically those that act on behalf of principals who receive funds directly, i.e. brokers / agents) should be exempted from Regulation.

**3.14** The UK is required to regulate financial intermediaries by the EU Directive and FATF Recommendation. Agents or other intermediaries are well placed to understand the customer who they – for example – may meet face to face or visit personally and to identify suspicious activity.

**3.15** The Government does not consider it practical or appropriate to remove intermediaries from the scope of the regulations. However the Government will continue to encourage the use of existing simplification provisions such as reliance that may assist with reducing the impact of the Regulations on these businesses.

**3.16** Very small businesses were the subject of responses arguing for exemption from the Regulations on the basis of the disproportionate costs they face as small businesses. With one limited exception there are no de-minimis limits on the size of business required to be registered or supervised under the Regulations. A de-minimis limit could allow very small businesses, however they were defined, to be excluded from the specific requirements of the Regulations. But there are clearly risks created by such a policy; small businesses could become conduits for illicit activity away from supervisory scrutiny for example.

**3.17** The Government proposes to exempt some very small businesses in this response and seeks further views on how this could be achieved while minimising the risks it may introduce. There is already a tightly defined exemption for limited ancillary activities that are subject to regulation.

**3.18** Clearing houses, online gambling businesses, betting shops and letting agents were all the subject of responses from industry representatives and law enforcement calling for regulation to be extended to them. The Government considers that to introduce regulation of these sectors would be disproportionate to the risks currently present and neither the FATF Recommendations nor the EU Directive requires regulation of these sectors.

**3.19** The Government encourages supervisors and law enforcement agencies to continue their efforts to raise awareness and understanding of the risks in all sectors.

**3.20** In order to minimise the cost of compliance with the Regulations and unnecessary checks, the Government will make further efforts to encourage the use of reliance by businesses on due diligence already performed by a regulated 3rd party.

**3.21** Royal Mail was also the subject of responses that considered their current exemption for the provision of the PO Box service, as providing an unfair competitive advantage while presenting a high risk of facilitating money laundering. The current exemption for Royal Mail is based on consideration of the Universal Service Obligation and assurances provided about safeguards in place. The Government will consider further if this exemption remains justifiable.

**3.22** Some of the proposals made in the Call for Evidence are discussed in more detail below.

### **Estate agents – letting agents**

**3.23** As noted above, a range of proposals were made, either to exclude estate agents involved in house sales from regulation or to bring letting agents (who manage rented properties) into regulation.

**3.24** Law enforcement agencies made the case for the regulation of letting agents in their responses to the Call for Evidence. Estate agents (property sales agents) pointed out that unlike them, letting agents handle cash transactions and in their opinion may represent a greater risk of money laundering.

**3.25** The Government remains to be persuaded that regulating letting agents for money laundering would be a proportionate response to the risks identified.

**3.26** There is evidence that rented property is used for a wide range of criminality, the extent to which property is let specifically to launder money through rental payments is not well documented.

**3.27** The criminality that rental property is often used for such as people trafficking, counterfeiting and drug manufacture and dealing, causes real harm to people and communities

in the UK and under UK law it is likely that rental payments made from the proceeds of these crimes constitute a money laundering offence. Regulating letting may therefore help reduce the harm to the UK from a range of criminality.

**3.28** However regulating letting agents would require the UK to go beyond the requirements of the EU Directive and the Government is committed to not 'gold-plating' EU Directives.

**3.29** Further views on this issue are welcome but the Government is not proposing change at this time.

## Betting & Gaming

**3.30** Gambling in casinos is already regulated, but some respondents made a strong case that betting ought also to be regulated. A number of issues would be raised about the scope of regulation if it were extended to betting and to do so would be to go beyond the requirements of the EU Directive.

**3.31** Accordingly the Government do not propose to regulate betting shops at this time but welcomes further information.

**3.32** In addition, the Regulations only apply to businesses carried on in the UK. The Department for Culture, Media and Sport (DCMS) has separately consulted on whether offshore-based remote gaming businesses should be regulated to the extent they advertise and do business in the UK.

**3.33** Finally, suggestions were made that the €2,000 threshold for CDD in casinos was more restrictive than necessary. The €2,000 threshold is provided for in Article 10 of the EU Directive and we do not propose to raise it. Representations were also received about the requirement to carry out CDD if the threshold was exceeded when chips were bought or later exchanged. That requirement is consistent with the requirement of the EU Directive, and addresses the risks that collusive gambling with other customers might be used to effect a transfer from one person to another.

## Written policies and procedures

**3.34** Regulated businesses are required by Regulation 20 to have appropriate and risk-sensitive policies and procedures to ensure that they address the key requirements of the Regulations. There is no requirement that those should be in written form.

**3.35** Several stakeholders called for the Regulations to require regulated businesses to put in place written policies and procedures, mainly in order to improve supervision and aid enforcement efforts.

**3.36** While there may be advantages in legally requiring the adoption of written policies the real point of substance may be left unaddressed, if businesses acquire a written policy only for it to remain 'on the shelf'. The underlying purpose is to require businesses to adopt and follow consistent and appropriate risk-based policies and procedures.

**3.37** An alternative option might be to create a new power for supervisors who would be allowed to require regulated businesses to adopt written policies and procedures.

**3.38** While the Government does not propose to require written policies and procedures at present, views are welcomed on whether written policies and procedures should be considered as a statutory requirement in future. If there should be a requirement, should an exception be made for the smallest businesses? Or should supervisors be given the power to require some or all businesses to adopt written policies and procedures?

## Retention of copy documentation

**3.39** The Regulations currently allow firms to keep either copies or details of identity documents. Copies are most helpful to investigators. On the other hand there is evidence of some public disquiet about the widespread copying and retention of copies of passports or other identity documents, despite the protections afforded under the Data Protection Act 1998. There are also practical issues for businesses in managing large volumes of documentation.

**3.40** Accordingly the Government does not propose to require the retention of copy documents, and will allow details to continue to be kept either in the form of copies or by recording the relevant details.

## High value services businesses

**3.41** The Regulations currently apply to high value dealers in goods. Some responses argued that high value services, such as consultancies, present a high risk of money laundering and should be regulated on a similar basis.

**3.42** High value dealers in goods are regulated because expensive goods offer criminals the opportunity to launder criminal proceeds by buying and re-selling goods. The risks with services are less clear-cut, and regulating high value services would require the UK to go beyond the EU Directive.

**3.43** Accordingly the Government does not propose to regulate high value services businesses.

## Pawnbrokers

**3.44** Representations were made on behalf of pawnbrokers arguing that they presented a low risk of criminal exploitation for money laundering.

**3.45** A specific exemption for pawnbrokers would be difficult to justify in the light of the EU Directive and international standards and the Government does not propose to take forward such an exemption at this stage.

## Agent / principal relationship

**3.46** Some submissions drew attention to apparent difficulties with the relationships between agents and principals and the application of the Regulations. The Government is looking further at those issues.

**3.47** It is not clear from the representations received so far whether the real issue is that the application of the Regulations is unclear where, for example, one financial business is an appointed representative of another, or whether the legislation is clear but poorly understood or otherwise unhelpful.

**3.48** The position is that where an FSA regulated business (A) appoints a business (B) to act as its 'appointed representative' it is A's duty to comply with FSA rules and guidance, and A is liable for B's compliance with the regulations. Business A's duties also apply to the activities of those appointed representatives.

## Further information

**3.49** Further information or views are welcome on any of the issues discussed above.

## Proposals for consultation

**3.50** This section contains proposals from the Government for changes to the Regulations. Views are sought in relation to each of these (see Chapter 2). There are arguments for and against some of these proposals and additional consideration and analysis of the evidence will be required before they are developed further.

### Criminal sanctions

**3.51** Like most EU Member States, the UK has provided for criminal sanctions for regulatory breaches. These are separate from the money laundering offences provided for under the Proceeds of Crime Act 2002 (POCA) and the Terrorism Act 2000 (TACT).

**3.52** The Regulatory offence powers under the Regulations have not so far been widely used. There have been suggestions that anxiety about prosecution under the Regulatory offences causes businesses to be unreasonably risk-averse.

**3.53** The Government proposes to remove the criminal penalties from the Regulations in order to send a strong message to the regulated sector and their supervisors, that businesses should have confidence in implementing a fully risk-based approach. It wishes to discourage businesses from going further than necessary when complying with Regulations.

**3.54** Accordingly the Government has examined a number of options;

- Abolish the criminal sanctions under the Regulations;
- Abolish the criminal sanctions under the Regulations generally but retain criminal sanctions for the most significant offences, such as the failure to carry out Customer Due Diligence under Regulation 7;
- Abolish the criminal sanctions under the Regulations generally but retain them for certain high risk sectors; and
- Abolish the criminal sanctions under the Regulations while strengthening or creating new civil powers.

**3.55** The issues are complex. The existence of criminal offences acts as a deterrent; and may assist those in regulated businesses charged with compliance functions to ensure these responsibilities are taken seriously by senior management and staff.

**3.56** Supervisors often find evidence of actual money laundering in the course of carrying out an investigation under the existing criminal penalties in the Regulations. This leads to investigations and prosecutions for money laundering that may not otherwise have been detected.

**3.57** SOCA and the Police emphasize the importance of the current offences to supporting activity generally to detect, deter and disrupt money laundering. This is supported by recent operational activity.

**3.58** However, the existence of a large number of criminal offences is seen by many businesses and industry experts to imply a significant risk of prosecution for minor procedural irregularities or decisions taken under a risk-based approach. These concerns may cause operational staff to be disproportionately risk-averse, cutting across the risk-based approach to which we attach great importance.

**3.59** Neither the EU Directive nor the FATF standards require the UK to adopt and maintain criminal sanctions for regulatory failures, although 17 out of 27 EU Member States currently have these.<sup>2</sup>

**3.60** If criminal sanctions were to be removed, one option would be to rebalance the sanctions under the Regulations by creating additional civil powers for supervisors. These might, for example, include additional powers (where they do not already exist) to allow supervisors to direct or order a business to carry out appropriate improvements or to commission and pay for an independent report or investigation. Businesses might be required to suspend regulated activities while improvements or retraining are implemented.

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

## Reliance

**3.61** The following changes are proposed as a result of responses received from a small number of stakeholders. They all merit consideration and your views on them are sought.

### Parts 1 and 2 of Schedule 3 (professional bodies that may be relied upon)

**3.62** UK firms can, subject to certain safeguards, rely on CDD checks performed by other firms, including those supervised by bodies in Part 1 of Schedule 3, but not Part 2. That distinction reflected the position in 2006/7 that there was relatively little experience of working with some supervisors. The Government undertook to review that distinction between professional supervisors at this time.

**3.63** The Government are working closely with all supervisors to ensure they effectively and proportionately discharge their statutory responsibilities. Initial evidence suggests that supervisors take their responsibilities seriously, and that the initial distinction made is no longer appropriate.

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?

**3.64** This was not a subject of a significant number of responses received during the review, but the Government believes it would be helpful to businesses to consider removing the distinction now.

## Debt purchase

**3.65** OFT supervised retail lenders (CCFIs) may purchase debt from other OFT supervised lenders. The purchaser cannot currently rely on the CDD performed by the seller. This is because reliance cannot currently be placed on lenders that are not FSA authorised. In principle this means that where a loan is sold by one lender to another the acquiring business should repeat CDD. That appears to be unnecessary, and the Government propose to make reliance available where the normal reliance conditions can otherwise be met.

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

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<sup>2</sup> [http://ec.europa.eu/internal\\_market/company/financial-crime/index\\_en.htm#study](http://ec.europa.eu/internal_market/company/financial-crime/index_en.htm#study)

**3.66** Similar issues arise in corporate loan markets in the context of, for example, syndicated loans. Are there opportunities to reduce duplicative checks in those markets by greater confidence in the opportunities provided by reliance?

### Very small businesses

**3.67** Generally there are no de-minimis limits under the Regulations, so a business is treated as a relevant person regardless of the size of the regulated business that it conducts. This reflects a concern that criminals may seek to exploit businesses of all sizes. Some recent very large frauds in particular have been associated with the use of very small accountancy practices for example).

**3.68** Nevertheless several responses were received from firms and individuals who consider the current regulations to be disproportionate by imposing what they perceive to be unnecessary and excessive costs and bureaucracy on very small businesses. The Regulations can impose significant costs on the smallest businesses and the Government encourages a fully risk-based approach by those businesses and those that supervise them. This may include very small bookkeepers or semi-retired part-time accountants with very low annual turnover, for example less than €15,000 who may not need to continue to be considered 'in business' for the purpose of the Regulations and who might present a low risk of money laundering or terrorist finance. In addition the Regulations do provide for a limited exclusion for small levels of otherwise regulated activity under certain strict limits set out in Schedule 2 Paragraph 1.

**3.69** The Government welcomes views on where the balance of advantage lies, whether such people should be considered to be 'in business' for the purpose of the Regulations and how they might appropriately be defined.

**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?**

### Non-lending credit institutions

**3.70** The Government proposes to remove from the list of relevant persons (i.e. regulated businesses) those businesses that have consumer credit licences because they allow their customers credit in the form of extended 'time to pay' arrangements for goods or services.

**3.71** This would apply, for example, to sports clubs with annual subscriptions that members are allowed to pay in monthly instalments, opticians and other businesses that allow for goods or services to be paid for using credit terms and who have a consumer credit licence. To limit the scope of this measure the Government proposes it will apply where the period of credit granted is no longer than one year.

**3.72** The effect would be to only regulate for AML purposes consumer credit lenders who make loans, i.e. those making advances to their customers, rather than those who grant credit in the form of 'time to pay'. All other credit regulation requirements in this area would remain unchanged.

**3.73** This change removes a small group of businesses from the scope of the Regulations, and in our view reflects the intentions of the FATF and the EU Directive.

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

### Estate agents – overseas property

**3.74** We propose to add to the list of relevant persons (i.e. regulated businesses) UK based estate agents who deal in overseas properties. These businesses are not currently regulated under the Regulations. The OFT would supervise these businesses.

**3.75** This change corrects a minor exclusion from regulation as a result of the definition of estate agency which uses UK land law terminology. The current approach has the effect of excluding estate agents who deal in overseas property while carrying on their business in the UK.

**3.76** The Government considers that the risks of these businesses facilitating money laundering are sufficient to justify their being brought into UK regulation. This is because they deal in potentially high value overseas property, and which may otherwise be outside the oversight of UK law enforcement bodies. This approach is wholly consistent with FATF Recommendations and EU Directive.

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

### Safety deposit boxes

**3.77** We received views from both the BBA and the FSA on the Regulations as they affect safety deposit box providers. While “safe custody services” are regulated activities, “safe custody” is not otherwise defined in detail.

**3.78** 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.

**8. Do you agree that “safe custody services” should be more clearly defined, and if so, how?**

### HMRC Fit and proper tests

#### Right to appeal

**3.79** Certain regulated businesses are subject to a fit and proper test applied by HMRC before they can be registered under the Regulations. These proposals relate to the operation of the fit and proper test for money service businesses, and trust and company service providers.

**3.80** At present there is no explicit right to appeal against a decision by HMRC that a person is not “fit and proper” under Regulation 28(2).

**3.81** While any representations against a decision to deny that a person is fit and proper under Regulation 28(2) would be carefully considered by HMRC, and might for example be challenged by Judicial Review proceedings, we propose to create a new formal right of appeal so that all appeals can be dealt with on a uniform basis. This right of appeal will be available to all the persons listed in Regulation 28(1).

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

#### Previous criminal conduct

**3.82** The Regulations currently specify that persons previously convicted of financial and terrorist related offences should not be considered by the supervisor of Money Service Businesses (MSB’s) to be fit and proper. This has been questioned by law enforcement, HMRC and the Justice Minister in Northern Ireland as insufficient to properly regulate this sector as it allows persons previously convicted of other serious offences to be treated as fit and proper.

**3.83** The EU Directive allows for all criminal conduct to be taken into account. Given the significantly high risk presented by MSB’s and the cases made for enabling the fit and proper test to take into consideration all previous criminal conduct, the Government proposes to change the definition accordingly. This is not expected to increase the burden on business and

the supervisor believes that it would make the MSB sector less vulnerable to illicit finance and criminal exploitation.

**9. Do you agree that HMRC should be able to consider all previous criminal conduct under the fit and proper test for MSB's?**

**Supervision**

**3.84** A number of detailed issues were raised about supervision or the powers of supervisors, mostly by supervisors themselves. The following questions arise, on which your views are sought

**3.85** Supervisors were concerned that while there is overall an appropriate range of powers that allow them to effectively discharge the responsibilities that the Regulations place upon them, there is a small number of areas where their powers are apparently limited, or unclear, or ambiguous. Accordingly we propose to address:

- A lack of powers to penalise the unreasonable refusal to admit a supervisor to business premises, (which means that a business cannot be effectively supervised);
- A lack of powers to obtain information in all cases;
- A lack of powers to compel the payment of fees or charges, which means that a business can continue to be regulated without making the same financial contribution as its competitors, where a business cannot be de-registered for non-payment of those fees. There is similar uncertainty over the ability to de-register a business that obtained its initial registration on the basis of misleading information, or where for other reasons a registration is no longer in the public interest; and
- There is some uncertainty about the ability to conduct enquiries with persons who are not registered but reasonably appear to be relevant persons.

**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?**

**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?**

**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?**

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

**3.86** At present supervisors can share information with SOCA under the Serious Organised Crime and Police Act 2005. However supervisors may wish to share information between themselves to minimise costs on businesses and to alert other supervisors to knowledge or suspicion about a regulated business or other persons, where for example a business moves from one supervisor to another. At the same time, any new disclosure power would need to be limited to material that is strictly relevant to AML supervision.

**3.87** This power would allow supervisors to share both negative and positive data or information that relates to a regulated person generally (their name and address etc) and to their regulated business activities, to the extent that such sharing was appropriate and proportionate.

**3.88** There are two major aims here; the first is to ensure that one supervisor can make information available to their colleagues where a business chooses to move from one supervisor to another. This should help reduce administrative burdens on the business that moves, as it does not have to re-supply information to the new supervisor. The power may also be relevant where a business is, for example, expelled by one body, or under threat of expulsion; this power would allow new supervisors to have appropriate background information drawn to their attention.

**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 new 'gateways' to allow for the exchange of information?**

**3.89** Concerns were expressed that some businesses might misleadingly imply, by describing themselves as "supervised by HM Revenue and Customs" that HMRC acted as a supervisor of their professional competence. That is not the case – HMRC are not a competency supervisor. There are already general prohibitions on misleading behaviour, advertising or other business communications, that may be relevant in these circumstances; but they may not provide the most certain or straightforward remedy.

**3.90** Some supervisors (such as the FSA) already control how the businesses they supervise can refer to that supervision, to ensure that disclosure is clear and appropriate.

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

## Updating the Regulations

**3.91** The Government believes the following changes are necessary to update the Regulations. While views are welcome, these changes are not expected to attract significant objections.

### Regulation 18

**3.92** Regulation 18 of the Regulations currently contains powers allowing HM Treasury to issue directions, for example to require a relevant person not enter into or cease business with certain non-EEA persons. These powers were superseded by new arrangements in the Counter-Terrorism Act 2008. The Government proposes to remove Regulation 18 as this power is now redundant in practice.

**3.93** Schedule 7 to the Counter Terrorism Act was used in 2009 to issue two directions.

**3.94** This change eliminates a redundant provision in the Regulations.

### Home Information Packs (HIPs) and Home Reports in Scotland

**3.95** Given the Government's announced commitment to discontinue HIPs the Government proposes to remove relevant references in the current exemptions.

**3.96** The Government proposes to exempt the preparation of Home Reports in Scotland, in the same way that HIPs preparation in England and Wales has been excluded from regulation.

**3.97** The Government does not believe that the preparation of a HIP or Home Report falls within the definition of a regulated business, but accepts there may be some ambiguity on the point, and is happy to make the position completely clear.

**3.98** This change updates the regime to reflect the introduction of Home Reports in Scotland and removes any ambiguity on this point.

**3.99** Energy Performance Certificates (EPCs) will continue to need to be prepared. The Government does not consider the preparation of an EPC could possibly constitute a regulated activity.

### **Northern Ireland Credit Unions (NICUs)**

**3.100** Proposals were published in 2010<sup>3</sup> to reform the regulation of credit unions in Northern Ireland.

**3.101** As part of that process the supervision of NICUs would move to the FSA from the Department of Enterprise, Trade and Investment in Northern Ireland. If those changes are to go ahead in the light of the consultation the Government will undertake the necessary legislative changes to the Regulations as part of this process. That will require NICUs to be supervised by the FSA from an appropriate date.

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<sup>3</sup> Proposals for regulatory reform of credit unions in Northern Ireland, March 2010, jointly published by HM Treasury and the Department of Enterprise, Trade and Investment in Northern Ireland.

# 4

## The risk-based approach

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### Introduction

**4.1** The risk-based approach is central to the UK anti-money laundering regime. It means that the steps required of a regulated firm should be proportionate to the risk perceived by the business. The Government strongly advocates the risk-based approach in the development of international standards by FATF, at EU level and within the UK.

**4.2** The Regulations contain a number of references to risk, for example in identifying a beneficial owner, in carrying out ongoing monitoring, or in establishing and maintaining risk assessment and management policies and procedures. There is a general requirement that a regulated business must “determine the extent of customer due diligence measures on a risk-sensitive basis...”

**4.3** In addition, the Regulations require or permit enhanced or simplified due diligence in certain higher or lower risk situations specified in the Regulations. For example, simplified due diligence (SDD) may be applied in dealing with regulated credit or financial institutions; enhanced due diligence may be required, for example, for customers who are not physically present or are PEPs.

**4.4** There is a much fuller exploration of the risk-based approach in useful material produced by the Financial Action Task Force<sup>1</sup>.

### Responses to the Call for Evidence

**4.5** Responses to the Call for Evidence were mostly supportive of the adoption of a risk-based approach in principle. A trade body noted “anything other than a risk-based approach would be inappropriate; ineffectively prescriptive and generally cumbersome”. Others noted that the risk-based approach provides for more flexibility than the 2003 regulations. One large firm noted that the approach has allowed their clients to “shape their anti-money laundering systems and controls on the basis of the specific risks that they are vulnerable to”.

**4.6** Another firm, supportive of a risk-based approach, highlighted a number of areas (beneficial ownership and PEPs) where they feel the risk-based approach is not adequately reflected and would like to see more done to make these aspects of the Regulations more explicitly risk-based.

**4.7** Some respondents, businesses in particular, wanted more prescription in the Regulations and/or guidance. For example, some smaller trade bodies indicated that some of their members do not like a risk-based approach or find it difficult to apply. Customers of regulated businesses were another group that were particularly critical of what they see to be a lack of a risk-based approach.

**4.8** Other respondents highlighted the difficulties of trying to operate a risk-based approach while also satisfying other requirements in the sanctions context where the requirements in domestic and overseas regimes are ‘absolute’.

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<sup>1</sup> <http://www.fatf-gafi.org/dataoecd/43/46/38960576.pdf>

**4.9** Isolated responses took the view that given the challenges of the risk-based approach it might be simpler to abandon it all together.

**4.10** Many stakeholders commented positively on the role of, and access to, guidance in assisting them to apply the regulations in a risk-based way. They drew attention to a variety of other communications channels including training seminars and newsletters.

**4.11** However, a number of stakeholders commented on the need for more sector specific guidance, and requested consideration be given to providing prescription in some areas. One large trade body argues that the absence of a publicly available UK national risk assessment specific to money laundering undermines industry confidence.

**4.12** A number of potential barriers to the application of a risk-based approach were cited in responses and are discussed below. These include criminal sanctions, the impact on customers, feedback on SARS and other related legislation.

**4.13** There are criminal sanctions in the Regulations, which may be imposed on conviction for regulatory offences. There were considerable representations, mostly from law businesses, that the effect of the possibility of a criminal prosecution was to discourage a broad adoption of the risk-based approach; fear of prosecution may be encouraging an overly risk-averse approach in practice. This is despite the general absence of prosecutions under the Regulations.

**4.14** Other stakeholders argue that criminal sanctions serve useful purposes, for example in emphasising the importance of compliance, ensuring senior management take their corporate responsibilities seriously and by supporting law enforcement. The arguments are finely balanced.

**4.15** There are a number of concerns that the risk-based approach is not as fully supported as it might be by supervisors and their supervision and enforcement policies. More specifically, stakeholders suggested that there were differences in approach to the supervision of the application of the risk-based approach.

**4.16** Similar issues were raised about uncertainty as to how Supervisors might use their supervisory powers in instances where the application of the risk-based approach might be open to challenge. The challenges of applying the risk-based approach include limitations imposed by other professional rules<sup>2</sup> and a fear of regulatory failures and potential criminal liability.

**4.17** Stakeholders also felt there was a lack of advice or guidance on the practical application of the risk-based approach in specific circumstances. And a number of respondents drew attention to cases where Supervisors were alleged to request or advise businesses to go beyond the minimum statutory requirements. HM Treasury discourages unnecessary or disproportionate measures being taken, which may include going beyond statutory requirements.

**4.18** Several responses were critical of the impact of the Regulations on customers, where customer-facing staff use the Regulations as the reason for refusing business or requiring additional or unreasonable checks.

**4.19** These representations were made on behalf of two main groups, British nationals living abroad or non-UK residents, and potentially excluded customers including those who for a range of reasons have little or no credit history, have difficulty in establishing a long-term address, or may not have typical documents used to help establish identity, such as driving licences or passports. This may include the elderly and or other more vulnerable members of society, who do not travel abroad, do not drive and whose wife, husband or partner may pay utility and other bills.

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<sup>2</sup> Such as legal profession Accounts Rules.

**4.20** Even though it was made clear during the Review that the SARs regime was outside the scope of the Review, regulated businesses systematically drew attention to the need for more feedback on the information they provide in the form of SARs and on the use made of SARs more widely. Supervisors echoed these comments, as they feel greater feedback from law enforcement helps their monitoring activities by allowing them to focus resources on high-risk areas, with similar impacts on the effectiveness and proportionality of the Regulations. However many calling for improved dialogue acknowledged that there were practical concerns faced by law enforcement, including the need to protect reporters and the information they submit, and that SOCA had made real advances in this area since its creation.

**4.21** A final issue is that of other and related legislation as noted previously. Businesses may want to adopt a risk-based approach but also find themselves subject to ‘absolute’ legislation for some activities or customers that in turn may lead to a more ‘absolute’ approach across all activities. One trade body was supportive of a risk-based approach both in principle and in delivery, but were critical of the lack of a more consistent approach between asset freezing sanctions and the Regulations.

## The Government Response

**4.22** The Government is pleased that the risk-based approach is broadly welcomed, and is seen to be at the heart of the Government’s approach. The formal adoption of the risk-based approach in the 2007 Regulations conformed to previous UK good practice. The risk-based approach of the Regulations is also consistent with the Government’s stated objective of ending the culture of ‘tick-box’ regulation. The Government recognises the risk-based approach can be challenging for some businesses. It nevertheless considers that is appropriate as a fundamental part of an effective and proportionate regime.

**4.23** Some comments point to areas where the risk-based approach is seen to be less effective. These criticisms may partly overlook the existing legislative flexibility, but they nevertheless point to a need to further elaborate how the risk-based approach does apply for example in identifying a beneficial owner.

**4.24** A risk-based approach accordingly places greater responsibility on businesses to know their customers and the risks they present, and to tailor the measures they apply accordingly. Our view is that the risk-based approach is nevertheless justified because:

- So-called ‘tick-box’ systems are ineffective, not responsive to the risks presented, are vulnerable to evasion or being circumvented (as criminals concentrate on meeting limited known tests) and tend towards imposing higher costs in all cases;
- Risk-based approach systems vary the checks carried out, only apply higher-level checks where necessary, and benefit from the knowledge and expertise of the business concerned; and,
- In the longer term the risk-based approach should deliver a more effective and proportionate regime, and better results.

**4.25** There are good reasons for adopting a risk-based approach and these seem generally understood and supported by stakeholders. In relation to beneficial ownership, Regulation 5(b) permits a regulated firm to take “adequate measures, on a risk-sensitive basis”, to verify the beneficial owners identity.

**4.26** The Government is working with other countries to strengthen the risk-based approach within the global standards and the responses to this review are informing that work.

**4.27** The Government is consulting in this response on removing the criminal penalties from the Regulations in order to send a strong message to the regulated sector and their supervisors to

have confidence in implementing a fully risk-based approach. It also wishes to discourage businesses from going further than necessary when complying with Regulations.

**4.28** The Government concludes that further effort is required to understand and address, typically through supervisory engagement and industry discussion and guidance, the obstacles that exist to a greater take up of the risk-based approach.

**4.29** While apparent differences in supervisory approach might arise for quite legitimate reasons, the Government will work with supervisors to strengthen as far as possible a common approach to the supervision and enforcement of the risk-based approach. Supervisors and others should seek to ensure that guidance provides useful advice on the application of the approach. But by its very nature it is difficult for guidance to anticipate every possible circumstance.

**4.30** In terms of the impact on customers, businesses are generally concerned both to meet the regulatory requirements and to have clear and unambiguous policies for their staff to follow. The tendency appears to be for those internal policies to seek to minimise the discretion (or opportunities for error) for front line staff. The effect therefore appears to be that staff can be relatively constrained by internal systems from, for example, accepting reasonable proof of identity that is nevertheless not acceptable internally.

**4.31** A further reason is that businesses may 'screen' their customers for potential future products and services, not simply current ones. This enables the firm to expand its relationship with the customer, without having to go back to the customer to request more identification each time a new product is 'sold'. But this can mean more information is demanded from the customer up front.

**4.32** The Government has discussed the question of overseas customers with the banking industry. There is no legal or regulatory barrier to banks providing services to non-residents, but many banks and building societies have decided not to do so. This is largely on commercial, not regulatory grounds, and is driven chiefly by concerns about fraud prevention, notably identity fraud, and the additional administrative costs in dealing with people abroad. Opening a new account for a non-resident calls for specialist expertise, and running it is more expensive than a domestic account.

**4.33** The Government propose to work with supervisors and others to explore these difficulties; to emphasise that the risk-based approach is central to our approach and to the Regulations; and to explore what opportunities there are for ensuring front line staff are empowered and supported to deliver a risk-based approach.

**4.34** The British Bankers Association offers an account finder service through its website at [www.bba.org.uk](http://www.bba.org.uk). It is intended to help those who have difficulty in finding a suitable onshore account. However, the terms on which an account may be offered will not necessarily be the same as the terms offered to residents. For example, a minimum account balance may be required.

**4.35** The difficulties experienced by potentially excluded customers appear to be a combination of commercial and regulatory related issues.

**4.36** To address these issues the Government has encouraged banks to offer Basic Bank Accounts, and to approach any identification issues flexibly and sympathetically. Specifically, the Treasury has approved guidance for the banking industry<sup>3</sup> that encourages businesses to have regard to a wide range of documents that can help to prove identity.

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<sup>3</sup> Prepared by the JMLSG

**4.37** The Government is also aware of useful guidance on identity produced for advice agencies by Toynbee Hall, and which is available at [www.toynbeehall.org.uk/core/core\\_picker/download.asp?id=1521](http://www.toynbeehall.org.uk/core/core_picker/download.asp?id=1521)

**4.38** The Treasury additionally intends to improve its own website that will, inter alia, reinforce public access to Approved Guidance and other resources and information.

**4.39** With regard to greater feedback from law enforcement, the Government will continue to work with SOCA and the police to support existing initiatives that aim to increase understanding of the value and benefits of SARs within the regulated sector and to devise new ways to share relevant information with businesses and supervisors.



# 5

## Simplification and deregulatory provisions

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### Introduction

**5.1** Regulated businesses and their customers incur costs in complying with the Regulations. To minimise additional costs the Regulations provide for a number of changes to the 2003 regulations in the form of simplification procedures and businesses are encouraged to make use of them.

**5.2** Leaving aside the risk-based approach that is separately addressed, and the other measures<sup>1</sup> that exclude certain types of business or organisation from legislative scope, the simplification measures are

- Simplified due diligence under Regulation 13
- Reliance on checks performed by certain other persons under Regulation 17
- The equivalence arrangements that apply in Regulations 13 and 17.

**5.3** Reliance and equivalence are specific simplification measures that are designed to allow one business to rely on other businesses that have carried out identity checks.

**5.4** Under the Regulations a UK firm can rely on certain other UK businesses, similar businesses in EU Member States or similar businesses in certain other (“equivalent”) jurisdictions.

**5.5** The reliance regime requires that the business relying upon another remains liable for the discharge of its responsibilities. Businesses relied upon also agree to certain conditions, for example to provide records to the relying firm.

**5.6** Many of the day-to-day comments on the Regulations focus on apparently unnecessarily repetitive process of customers (private individuals and businesses) demonstrating their identity to several different parties engaged in what is seen as essentially the same transaction. The simplification measures were intended to minimise those impositions, but there is evidence that the facilities offered are not being used widely.

### Responses to the Call for Evidence

**5.7** Though stakeholders generally seem to understand the intent behind the simplifications, many were critical of uncertainty about the circumstances in which they could be used or are constrained from doing so for legal and/or commercial reasons.

**5.8** Responses to the Call for Evidence were, generally, implicitly supportive or neutral in principle, on the simplification options. Some businesses reported significant existing use of reliance; other sectors (e.g. casinos) looked to significantly expand their use of reliance.

**5.9** On the other hand, isolated responses suggested that given the apparent difficulty in using reliance, the simplest step might be to abolish it. And a number of businesses expressed difficulties with the practical application of equivalence, particularly given that they remain liable

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<sup>1</sup> For example in Regulation 4

for the checks carried out by others and many are unwilling to take this risk. In addition businesses receiving requests to be relied upon may simply not respond to such requests.

**5.10** There is clearly a lack of consensus; some but not all businesses see worthwhile benefits in the simplification arrangements.

**5.11** Stakeholders were frequently critical of the extent to which the simplification arrangements were made clear or practical. For example, a number of businesses requested more assistance with identifying equivalent jurisdictions; others raised concerns about how to use reliance in situations where the firm being relied upon may not exist in the future.

**5.12** A number of responses drew attention to limitations in the domestic reliance regime – specifically that reliance can be placed on businesses in the UK supervised by certain but not all professional supervisors. Other responses endorsed further clarification of the reliance regime.

**5.13** It was also noted that some businesses were prevented, for copyright and commercial reasons, from granting reliance to another party when they had used third party services to satisfy their own CDD requirements. This was especially true of checks on PEPs, which are routinely undertaken using proprietary information or subcontracted to third party information providers.

**5.14** We noted in the barriers to a risk-based approach section earlier that stakeholders have drawn attention to inconsistency of supervision, uncertainty of supervisory enforcement and a lack of supervisory support. These also affect the uptake of simplification options. As noted previously, at least one supervisor discouraging businesses from the use of reliance is another example.

**5.15** In addition, the distinction between Part 1 and Part 2 bodies under Schedule 3 may make it difficult for some businesses to rely upon one another.

## **The Government Response**

**5.16** The Government has made a major commitment by adopting all the various simplification options allowed in the Third Money Laundering Directive, and in the Regulations.

**5.17** Reliance has the potential to deliver major savings. Indeed, reliance was expected to potentially deliver major savings when the 2007 Regulations were implemented but there are clearly impediments to the widespread use of the reliance provisions.

**5.18** Based on the views from businesses, both at events and in response to the Call for Evidence, there is scope to improve the confidence of businesses in this area.

**5.19** While ‘reliance’ was the subject of a large number of responses received during the review and we are keen to encourage a much wider use of these provisions, there are not significant changes to the regulations available to improve the regime. The Government will work with supervisors to improve guidance in this area and believe that take-up may be more greatly influenced by changes to other parts of the regulations, as proposed here, such as removal of the criminal penalties.

**5.20** That said, the Government proposes to make this provision available to the widest possible extent and is consulting in this response on the removal of the current distinction between Part 1 and Part 2 Supervisors (professional bodies) and on the use of reliance by debt purchasers.

**5.21** Regulated businesses should apply policies and practices to take full advantage of the opportunities contained in the simplification measures and these could lead to reduced costs for some businesses. And, they should be supported in that by appropriate guidance and support from supervisors. Applied successfully, these simplification provisions should result in consumers experiencing less repetitive or unnecessary checks for AML purposes.

**5.22** There are operational measures that help to constrain administrative costs (such as the opportunity to use electronic verification). One response specifically reinforced the benefit of electronic verification and argued for its retention. The Government does not propose to reduce the extent to which electronic verification can be relied upon. Indeed attention has been drawn elsewhere to the apparent ease by which electronic verification can be carried out in some cases compared to the costs and risks of taking and posting copies of documents.

**5.23** Many of the issues identified as tending to restrict the take up of the simplification provisions are similar to the issues discussed in the risk-based approach section of this paper. The appropriate solution to those challenges therefore follows, in part, the strategy we propose to follow to address the challenges to the risk-based approach.



# 6

## Customer due diligence (CDD)

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### Introduction

**6.1** In this section, the CDD requirements of the Regulations are considered; the benefits of, and barriers to, effective CDD identified and some ideas for improvement discussed.

**6.2** The requirement for businesses to identify their customers underpins the Regulations. This requirement is known as customer due diligence (CDD) and has been common practice since the 1980's. The purpose of the Regulations is to ensure that businesses take practical steps to ensure they verify the identity of their customer, assess the level of risk they represent, and put in place appropriate measures to monitor, measure and manage this risk.

**6.3** Recognising that different types of customers represent different levels of risk, the Regulations provide for simplified due diligence (SDD) in specific circumstances. The Regulations also require enhanced due diligence (EDD) on customers who represent a higher level of risk. PEPs are identified as a group representing a higher risk. In addition to identifying the customer, businesses are required to identify the beneficial owner, that is, the natural person rather than the legal entity who ultimately benefits from the account, policy or transaction.

### Responses to the Call for Evidence

**6.4** The Call for Evidence received many contributions from businesses and individuals about CDD. These varied widely and as well as indicating the benefits of these requirements for businesses, respondents took the opportunity to reiterate issues and difficulties they experience in practice.

**6.5** The effectiveness of CDD was questioned by some stakeholders and there is a common perception that false or fraudulently obtained identity documentation is readily available at low cost and that criminals would not consider CDD checks a real deterrent.

**6.6** SOCA's response noted that "CDD measures are one of the main strands of an effective AML/CTF system. Those businesses who conduct risk-based CDD are able to work with SOCA and law enforcement to deny and frustrate criminal acts". Furthermore, "the UKFIU receive better quality SARs as a result of this (CDD) scrutiny. Accurate and full CDD enables the reporting of SARs which can provide information that supports existing investigations and identifies and locates criminal proceeds."

**6.7** Most, but not all businesses agree that a level of CDD would be carried out as 'business as usual' regardless of the regulations, and in the view of one supervisor, "the benefits outweigh the costs because MLR 2007 has been the catalyst in encouraging our members to run more professional and disciplined practices. It has raised their awareness to the risks that they might face from their clients in respect of ML and TF and more importantly, has made them look at the bigger picture."

**6.8** That said, many businesses disagree about the extent of CDD required and a wide variety of approaches are evident. Many businesses state that the requirements of the Regulations are over and above what they may carry out as business as usual.

**6.9** Businesses have indicated that many customers are now familiar with, and understanding of, the need to produce documentation to verify their identity. However there are some sectors and circumstances where businesses think this is either unnecessary or upsetting for their customers.

**6.10** Identifying the beneficial owner is an important element of the CDD requirements since disguising ownership through complex layers is a main money laundering typology. This view is supported by SOCA: “The requirement to identify the beneficial owner improves transparency which helps to deter financial crime. Experience of Financial Investigation tells us that nominee owners and shareholders in trusts and company ownership increasingly are being used to shield money laundering activity.” A similar view is held of PEPs. In general, law enforcement agencies, international organisations such as the World Bank and anti-corruption NGOs such as Global Witness and Transparency International, see benefits in requiring businesses to do more.

### **Beneficial Ownership**

**6.11** Many businesses cited difficulties in establishing beneficial ownership and are keen for greater guidance on how far they are expected to take these checks; businesses spend considerable time working through beneficial ownership chains. One of the challenges faced by businesses is access to data to verify beneficial owners, particularly by independent means. There have been recent changes to remove data on the Companies House register that was previously being used by businesses to verify beneficial ownership information. A supervisor pointed out that “most of the sources which are used to verify beneficial ownership are in fact only verifying legal ownership” making the point that the true beneficial owner may still be hidden. On a different note, law businesses raised particular practical difficulties regarding the beneficial ownership of trusts.

**6.12** The inclusion of specific prescriptive requirements within the regulations regarding PEPs was a common theme, with many stakeholders presenting views on the effectiveness and proportionality of these requirements, the difficulties in implementing them and the costs of systems and access to sources required to do so. The need for more information on the risks presented by PEPs and the typologies employed by corrupt PEPs was identified by many as necessary to inform their efforts and compliance with the regulations. And some businesses would like greater clarity about the measures they are expected to take when they identify that a beneficial owner is a PEP.

### **Politically Exposed Persons (PEPs)**

**6.13** There is a perception, by some firms, that ‘PEP risk’ is the risk of having a PEP customer, rather than the risk of the firm being used for money-laundering purposes by corrupt PEPs. As a result, some firms spend disproportionate resources on identifying PEP customers (e.g. screening all customers irrespective of risk) and not enough on normal CDD – this means that in some cases, firms have failed to detect higher risk PEPs who are not the customer or beneficial owner, but are otherwise associated with or connected to a customer and who are in a position to materially affect the business relationship.

**6.14** There appears to be an over-reliance on commercial PEP databases for PEP identification purposes. While PEP database checks will be sufficient to meet the legal and regulatory obligations in most cases, it will not be enough where the risk associated with the business relationship is increased. There is an associated problem of firms not understanding the parameters used by the database (e.g. exclusion of certain categories of PEPs) or setting the wrong parameters (e.g. no fuzzy matching).

**6.15** The difficulty in checking the family and close associates of PEPs was cited as a particular challenge by many, with advice being sought on what might be considered reasonable in the efforts made by businesses to identify and verify these.

**6.16** There were several specific calls for domestic PEPs to be included in the regulations, with stakeholders citing both cost efficiencies and heightened risk as reasons for this. On the other hand, key stakeholders such as the British Bankers' Association made it clear that they do not support the inclusion of domestic PEPs, expressing a preference for industry to take a risk-based approach.

## The Government Response

**6.17** CDD is at the core of FATF Recommendations and has a pre-eminent place in the 3rd Money Laundering Directive. As the Regulations reflect FATF recommendations and transpose the 3rd Money Laundering Directive in UK law, CDD is a central pillar of the UK anti-money laundering regime. It is the Government's view that CDD remains of central importance to an effective anti-money laundering regime.

**6.18** Implementing CDD requirements helps inform businesses of the risks they face. While insufficient on their own, they complement other information and processes that businesses have in place to protect themselves and their customers from money laundering and financial crime more generally.

**6.19** CDD can improve the quality of customer information available to assist with detecting money laundering and terrorist financing activities as well as deter criminals from these and other activities such as fraud.

### Beneficial ownership

**6.20** Establishing beneficial ownership is an important part of the Regulations. More communication on why this is the case may help alleviate concerns that too much time is spent on it. The Government will work with supervisors to explore ways to increase certainty for businesses as to how far they need to go in certain circumstances, for example through guidance.

**6.21** In addition, the Government is working with other countries to review and improve international standards on beneficial ownership, to make them more effective and where appropriate to reduce the costs on the regulated sector of undertaking checks in certain low risk circumstances. This is part of the wider programme to review the FATF Recommendations by October 2011.

### PEPs

**6.22** The Regulations require firms to establish and maintain appropriate and risk-sensitive policies and procedures to determine whether a customer is a politically exposed person. Where a customer is a PEP firms have to undertake additional checks and procedures in addition to the normal CDD requirements.

**6.23** There is a widespread perception that the PEPs checking provisions lack any risk-based element. The Government believes that understates the practical flexibility the Government would expect to see. Regulation 14, which contains the main PEP provisions begins with a clear reference to the need to apply enhanced due diligence "on a risk sensitive basis".

**6.24** Businesses are expected to apply appropriate and proportionate checks on PEPs. This means, for example, that large and sophisticated financial businesses, dealing with high net worth individuals from around the world would be expected to recognise that they are more likely to encounter a PEP than a small provincial business dealing with customers of modest means based in the local community. Businesses would be expected undertake checks appropriate to the risks they are realistically likely to face.

**6.25** Where a smaller firm does take on a new customer it should often be apparent from the initial engagement, the basic facts about the customer, or discussion of the customers' wants and needs whether any more sophisticated PEP screening is required.

**6.26** Fundamentally it is for each business, having regard to the nature of its business, to assess whether its services are likely to be relevant to PEPs and check its customers in the light of that assessment. The Government believes this approach is wholly compatible with a risk-based approach.

**6.27** As with beneficial ownership requirements, the Government is working with other countries to review the global standards on PEPs and the responses to this review have informed that work.

**6.28** The Government believes there is a case for improving guidance in this area and will work with others including FATF on this.

**6.29** There are also areas where changes to the regulation of PEPs may need to be considered in future and further views sought. These are set out below.

### **Foreign & Domestic PEPs**

**6.30** There were several specific calls for domestic PEP's to be included in the Regulations, with stakeholders citing both cost efficiencies and heightened risk as reasons for this - as it is often cheaper and easier to treat all PEP's equally and not seek to distinguish between them. On the other hand, key stakeholders such as the British Bankers' Association, made it clear that they do not support the inclusion of domestic PEPs and stressed the importance of a risk-based approach.

**6.31** The UK has committed to implementing the United Nations Convention on Corruption (UNCAC), which does not distinguish between foreign and domestic PEP. In addition, FATF has recently consulted publicly on revising its recommendations to require enhanced due diligence on domestic PEPs on a risk-sensitive basis.

**6.32** The recently published UNODC review of the UK's implementation of the UN Convention against Corruption<sup>1</sup> states that "Although there is no explicit requirement in UK legislation for UK institutions to undertake enhanced due diligence on all domestic politically exposed persons, Regulation 14 and the FSA's rules on anti-money laundering effectively require firms in the financial services industry to consider, on a risk-sensitive basis, whether enhanced due diligence measures on their domestic PEP customers would be appropriate. This is in line with the UK's risk-based approach to anti-money laundering and with FATF and EU requirements."

**6.33** To change the Regulations to make this more explicit now would 'gold-plate' the current EU Directive and the Government has a policy of not gold-plating. As a result no change is proposed at this stage. However the case for change will continue to be considered in the light of developments to international standards, EU legislation, the nature of the risks present and the views of stakeholders.

**6.34** The Government welcomes further views on the merits or otherwise of removing the distinction between foreign and domestic PEPs, including in particular the costs on smaller, UK only businesses that might incur additional costs.

**6.35** In order to help ensure that the measures taken remain proportionate the Government wishes to re-emphasise the relevance of the risk-based approach to PEPs.

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<sup>1</sup> <http://www.unodc.org/unodc/en/treaties/CAC/pilot-review.html>

**6.36** This means that in practice regulated businesses are required, on the basis of a risk-based approach, to scrutinise their business dealings with persons who they consider present a high risk, and which may include those entrusted with prominent public functions in the UK or abroad.

### **The one-year limit.**

**6.37** Under the Regulations, a PEP is, briefly, defined as a person who holds or has held a prominent public function within the last year. Many responses were critical of the one-year limit in the definition of PEPs, arguing that PEPs are likely to conceal, and continue to seek to transfer the proceeds of corruption many years after ceasing to hold prominent public functions.

**6.38** As such there is a case for removing the one year limit, and consider whether it would be appropriate to replace that with a longer limit (perhaps five or ten years). A longer limit appears to suffer from similar difficulties; it provides for an arbitrary limit to the enhanced due diligence required for PEPs. Removing the one year limit would create an open ended but risk-based commitment to vigilance in the case of all former PEPs.

**6.39** As with the distinction between foreign and domestic PEPs, to remove the one year limit now would be to gold-plate the EU Directive and the Government has a policy of not gold-plating. As such, no changes are proposed now, but further views are welcome, particularly on the costs and benefits of making this change in the future.



# 7

## Guidance

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### Introduction

**7.1** Approved industry guidance plays a central role in the Government's anti-money laundering and counter terrorist financing policy. Policy is expressed in high-level and principles-based Regulations, supported by guidance, which is developed by industry or supervisory bodies and approved by the Treasury.

**7.2** This approach provides greater detail and context for sector-specific implementation and the risk-based approach in the necessarily different contexts in which such a wide range of regulated businesses exists. In addition, guidance can provide a reasonable legal defence for a regulated firm if they are unwittingly subject to money laundering activity despite having adhered to the guidance to the best of their ability.

**7.3** For this reason the review has sought stakeholder feedback on guidance - the role and use of guidance as well its accessibility, and the opportunity for different stakeholders to engage in its formulation. Guidance in this context means guidance approved by HM Treasury unless otherwise noted.

### Responses to the Call for Evidence

**7.4** On the whole, views held by supervisors, businesses and industry bodies about guidance are positive.

**7.5** Evidence generally supports the view that guidance promotes an effective and proportionate approach to AML and it is useful that Guidance is legally recognised in the UK and that following Guidance must be taken into account in considering whether an offence has been committed under the Regulations, or whether a person has failed to comply with the Regulations for the purposes of imposing a civil penalty.

**7.6** The JMLSG Guidance was frequently mentioned and appears to be the mostly widely used amongst the stakeholders we spoke to.

**7.7** Comments on JMLSG Guidance are mostly very positive. Businesses note the quality and accessibility of the guidance and their ability to be engaged in its formulation. Though written by the JMLSG, a group made up of financial industry trade bodies, praise comes from smaller businesses and even businesses from non-financial sectors and private individuals.

**7.8** There were also some criticisms of the JMLSG Guidance for being overly focussed on and dominated by large financial sector businesses. Some stakeholders also find it too lengthy, and at times vague or non-definitive.

**7.9** Some of these criticisms may actually stem from a need for more sector specific guidance. This theme came up regularly at stakeholder events. In other words, many users of the JMLSG guidance find themselves using it in the absence of a better fit for their non-financial sector, or niche within the financial sector.

**7.10** That does not mean there is a complete absence of other guidance. On the contrary, many other bodies provide guidance. The Law Society guidance was mentioned as an excellent source,

as was the guidance issued by the Consultative Committee of Accountancy Bodies (CCAB), both of which have been used to inform the content of Guidance provided by other supervisors.

**7.11** There are examples of sector specific guidance too, for example for notaries and auditors, and some of HMRC's guidance is approved. In addition guidance of a general nature (i.e. not approved) also exists. For example, a supervisor of smaller practitioners provides guidance and has issued an AML Compliance Manual to all members including checklists, risk assessments and other forms. While not 'approved' guidance in a legal sense, this sort of guidance is useful to, and appreciated by, regulated businesses.

**7.12** Comments on vagueness were generally in relation the risk-based approach. Guidance promotes a risk-based approach so does not give specific instructions. Some businesses value the flexibility that this offers, but others find it unhelpful and would like more in the way of templates and advice. Comments also suggest that a lack of specificity leaves businesses unsure as to what supervisors expect and how they will respond to compliance issues.

**7.13** In the medium term, when guidance is updated as part of regular revision cycles, inconsistencies could be addressed. Consideration could be given to offering more specific advice through guidance, perhaps in the form of templates that maintain a risk-based approach or greater clarity on compliance and enforcement policies to give businesses more certainty over what is expected of them.

## **The Government Response**

**7.14** HM Treasury has an important part to play in ensuring approved guidance is consistent and helpful to a wide range of users. We will keep the views reported here in mind in future guidance work.

**7.15** We make a series of short recommendations to all of those involved in the drafting of guidance to have regard to:

- Supporting appropriate risk-based outcomes, promoting the adoption of simplification measures, and within the context of a risk-based approach discouraging businesses from going beyond the legislative requirements;
- Securing the participation or input of small businesses in drafting guidance; and
- The particular needs of small businesses that use guidance.

**7.16** Finally, we acknowledge the very positive views of guidance and urge those who draft guidance to continue to provide high quality material informed by peer and wider stakeholder input.

# 8

## Supervision

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### Introduction

**8.1** In this section evidence is drawn from regulated businesses, supervisors themselves, and other parties to the Regulations including the Treasury's own interactions with supervisors.

**8.2** There are 28 supervisory bodies across seven broad sectors: financial institutions including credit institutions; auditors, external accountants, tax advisers, insolvency practitioners; legal professionals; trust or company service providers; estate agents; high value dealers; and casinos. Supervision of businesses subject to the Regulations takes place in two main ways: (1) monitoring of, and guidance on, compliance with the Regulations; and (2) enforcement of the Regulations.

**8.3** The role of supervisors is defined in the Regulations at a high level, which is to effectively monitor the relevant businesses.

**8.4** To give supervisors more clarity on their role, the Treasury has been working with supervisors since October 2008 on effective AML/CTF supervision. The overall objective of this work is to develop a 'regular, systematic and transparent mechanism' that (1) demonstrates that supervisors are meeting their legal obligations and are carrying out responsibilities in an effective, risk-based and proportionate manner; (2) formalises a process, which encourages best practice; and (3) creates and maintains public confidence in the effectiveness of the AML supervision regime.

**8.5** Through that process a number of indicators of effective supervision were drawn up which can be distilled into four overarching aims:

- The provision of clear guidance, support, outreach and education on legal obligations;
- Cooperation between supervisors to improve consistency and encourage best practice;
- A risk-based, proportionate and effective approach to compliance monitoring, enforcement and guidance, and encouraging supervised businesses to employ a risk-based approach; and
- Cooperation and collaboration with other relevant bodies across the AML regime.

### Responses to the Call for Evidence

**8.6** Overall the responses show that a considerable level of guidance, support, outreach and other 'engagement' take place. On the other hand, there is a sense that more could be done, particularly around consistency of supervision (in terms of guidance, compliance monitoring and enforcement) for industry sectors with more than one supervisor and strengthening a risk-based, proportionate and effective approach to compliance and enforcement.

**8.7** In general, regulated businesses were positive in their comments about all aspects of what might collectively be termed 'engagement'. Businesses and supervisors provide ample evidence

of a range of support provided and channels through which opportunities to feedback views and contribute to policy making are made. This includes provision of advice and guidance, educational seminars, helplines, online guidance, newsletters, advisory panels and discussion papers.

**8.8** A number of forums currently exist to facilitate cooperation between supervisors to improve consistency, encourage best practice and more generally share experiences and communicate views to bodies such as the Treasury. An example is the Supervisors Forum, which provides a platform for supervisors to discuss a full range of issues, and feed into policy thinking.

**8.9** The Money Laundering Advisory Committee (MLAC) meets under the leadership of the Treasury and Home Office, and includes supervisors, regulated businesses and industry bodies and provides an opportunity for the exchange of views on the AML regime and for private sector input to the development of international standards.

**8.10** Many supervisors have panels or other forums with regulated businesses, which enable supervisors to hear from its supervised population directly. Examples include a range of technical, expert and advisory bodies or committees that allow supervisors to draw upon the experience and expertise of their members. This further strengthens the capacity of supervisors to improve consistency and encourage best practice.

**8.11** That said, there is evidence to suggest that improvements to a variety of aspects of supervision could be made. Some accountancy bodies feel that the distinction between Part 1 and Part 2 bodies under Schedule 3 is no longer necessary since it means their respective supervised populations are treated differently. Another concern is that some accountancy bodies feel the supervision of accountancy service providers ('ASPs') by HMRC is not in line with other accountancy supervisors in terms of the powers available but also the lack of 'fit and proper tests'. In addition, concerns were expressed that some businesses are misleading clients into thinking that HMRC has endorsed them as professionally competent, rather than simply supervising them for AML purposes.

**8.12** The supervisory framework itself was created to facilitate a risk-based approach by giving supervisory powers to bodies already familiar with the sectors they supervise (e.g. FSA for financial institutions, accountancy bodies for accountants, law societies for lawyers). In general, stakeholders are supportive of this approach. They highlight the benefits of supervisors knowing their sector and where risks lie, which allows them to tailor their approach to the sector more effectively and proportionately. That said, a number of responses suggest that these benefits do not exist for sectors where supervisors did not have an established relationship with their supervised population.

**8.13** Evidence about compliance monitoring and enforcement was limited. Few businesses indicated they have received a visit since the Regulations came into effect but there is insufficient evidence to indicate if this is because a risk-based approach by supervisors is being adopted, or if too few resources are being allocated to compliance. This does not prevent some businesses from believing that supervisors focus too much on those businesses which are registered - and therefore more likely to be compliant - than on chasing businesses which are not registered - and are less likely to follow the requirements of the Regulations.

**8.14** Enforcement powers vary across supervisors. Failure to comply with certain requirements can result in criminal sanctions, which all supervisors can recommend to the relevant authorities. In addition, the FSA, HMRC, OFT and DETI have powers to obtain information and enter and inspect premises and the ability to administer monetary civil penalties. Professional bodies have access to additional sanctions such as withdrawal of professional status to enforce compliance.

**8.15** The general feeling from stakeholders seems to be that supervisors have an appropriate range of enforcement powers. However, it was suggested that HMRC may not have a sufficiently flexible range of powers to discharge its duties as a supervisor effectively and proportionately.

**8.16** Businesses that have received compliance visits note that often the visits are combined with other duties the supervisor has to perform rather than conduct multiple visits. For example, the FSA incorporates AML compliance within its ARROW assessments - the risk assessment framework that the FSA uses to rate businesses in terms of their riskiness against the FSA objectives.

**8.17** A number of comments suggest that firm's feel supervisors do not always take a risk-based approach, and can fail to give advice or assistance to the firm so that it knows what steps it needs to take to ensure compliance. Others point to differences in general approach, from a consultative, pragmatic and practical approach on the one hand to a 'tick-box' approach to supervision on the other.

**8.18** This issue is reinforced by views on how well, or otherwise, supervisors understand the businesses they supervise. In many cases regulated businesses feel their supervisory body does not understand the business sufficiently to understand where risks lie. And this is despite the use of supervisors relevant to the sector. These issues impact on general communication with the supervisor but also affect compliance visits on the ground. Businesses ask the question: how do supervisors make risk-based judgements and comment on my firm's risk-based approach if they are less well placed to understand the risks? Some stakeholders felt that some supervisors take an asymmetrical approach to updating their risk assessments, as they readily include new areas of risk but seem reluctant to exclude other areas or activities.

**8.19** Generally these comments related to supervisors new to their supervised population, but they also applied in some cases to well-established supervisors.

**8.20** There are useful examples of cooperation and collaboration under the Regulations. However supervisors and businesses have overwhelmingly expressed a desire for more information from law enforcement agencies to help them understand how the information they provide is used, see evidence of the benefits of the regime, and to inform their risk models.

## The Government Response

**8.21** The Government are working with supervisors to further promote a consistent, risk-based approach to supervision. The Government will continue to work with law enforcement, supervisors and others to strengthen the delivery of feedback to regulated businesses, while recognising that security considerations and the scale of UK reporting activity precludes individual feedback in all cases.

**8.22** The Government commends SOCA for the significant effort it has made to provide feedback and information to reporters and agree Memorandums of Understanding (MOUs) with supervisors following the Lander Review<sup>1</sup>. Due to the large number of reports submitted each year, the importance of maintaining the integrity of the regime and protecting reporters, the Government understands it is not always possible to provide case specific feedback. The Government will continue to work with SOCA, the police, supervisors and industry to promote a better understanding of the benefits of the wider AML regime.

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<sup>1</sup> In Sir Stephen Lander's Review of the Suspicious Activity Report Regime in 2006, a number of recommendations were made. This included SOCA agreeing a Memorandum of Understanding with each supervisor.

**8.23** HMRC is a supervisor under the Regulations but not a wider professional competence body, and it does not examine the wider competence of the businesses it supervises. Businesses supervised by HMRC should not give a misleading impression of the role fulfilled by HMRC.

**8.24** In a few cases, businesses undertake activities that fall under the jurisdiction of more than one supervisor – for example, a financial institution that also offers accountancy services through a subsidiary. Though multiple supervision cases are few and far between, they do exist and cause uncertainty for the businesses concerned, particularly given the differing approaches to supervision that are highlighted above and elsewhere. Supervisors do work to resolve these issues but there is a sense among some stakeholders that more could be done to resolve these cases in a timely fashion. Where multiple supervisors have jurisdiction, the Government will work with supervisors to ensure agreement is reached on a methodology for assigning a single lead supervisor

**8.25** A number of detailed issues were raised about supervision or the powers of supervisors, mostly by supervisors themselves. The Government is consulting on several of these proposals in this response document.

# 9

## Engagement

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### Introduction

**9.1** The Government is committed to evidence-based policy making and engagement with stakeholders underpins this. In this section we look at the evidence concerning the breadth and depth of engagement, and offer some thoughts on areas for future focus. The evidence given here is not exhaustive but identifies a wide range of activities that have been undertaken since 2007, including regular forums with industry groups, supervisors, and law enforcement and a range of outreach activities between supervisors and regulated businesses, and to a lesser extent regulated businesses and their customers.

**9.2** The Government response in this area is given in relation to the following

- engagement by the Treasury
- engagement by supervisors
- engagement with customers
- other engagement

**9.3** The Government's objectives for engagement are

- to listen carefully to the views of those affected by the measures it introduces;
- to maximise feedback and information sharing between Government, including supervisors and law enforcement and the regulated sector;
- for stakeholders to have clear roles, but also work coherently across departments and sectors; and
- that engagement with international partners needs to be robust, advancing operational and policy goals alike.

### Responses to the Call for Evidence

#### Engagement by HM Treasury

**9.4** In summary, the level of engagement for the Regulations is generally considered by respondents to be high. There was extensive Treasury-stakeholder dialogue prior to the introduction of the 2007 Regulations and a good level of ongoing engagement has continued since.

**9.5** A large number of responses to the Call for Evidence draw attention to and provide evidence of the Treasury's engagement with supervisors, businesses and the wider AML community through these and other forums. The general view is positive.

**9.6** Stakeholders generally feel they are able to participate in the development of the regime. For example, one response noted that: "HM Treasury engages with us well, in the development of the Regulations, both in our capacity as a representative of our members and member businesses and as an AML Supervisor." Supporting this view, another supervisor notes "HM

Treasury have certainly been pro-active in respect of communication, input and by providing explanations regarding issues relating to MLR”.

**9.7** There is frequent mention of the Treasury’s engagement with businesses through trade bodies such as the British Bankers’ Association, Investment Management Association and Association of British Insurers, both in terms of the Treasury disseminating information to businesses, and businesses’ views being communicated to the Treasury. Another supervisor says the Treasury “have always engaged very helpfully and promptly”, while a further supervisor says “HM Treasury has consulted effectively”.

**9.8** Feedback on the level of engagement during the review itself has also been positive. Stakeholders were pleased to have the opportunity to discuss issues and provide specific examples to illustrate their experiences. Holding meetings outside of London was also appreciated.

**9.9** There are areas where the picture is less positive, with some sectors or businesses reporting a lack of engagement and suggesting room for improvement. This includes engagement with small or medium sized enterprises (SMEs), and specific groups such as intermediaries and the gambling industry. Limited resources and the genuine desire to minimise the cost on individual businesses mean that most industry engagement is through trade associations and professional bodies. However, these groups can, on occasion, be dominated by the voices of larger businesses which have the resources to take an active involvement in government dialogue and policy formation. Large businesses also recognise that although there are multiple channels for involvement, “a considerable investment of time is needed which tends to put this beyond the reach of many smaller businesses.”

**9.10** The gambling sector was brought into the scope of the regulations in 2007 and the sector itself was only brought under a single regulatory regime under the Gambling Commission in 2005. As such the sector’s relationship with the Commission (its supervisor for AML) and the Treasury continues to develop. A number of gambling industry representatives have indicated a desire for more engagement by the Treasury, and the Treasury has recently begun to engage more with various industry fora.

**9.11** Given the relative immaturity of the gambling industry regulatory regime at the time the Regulations were implemented, and developments in offshore online gambling, greater engagement with the industry could usefully continue to be undertaken.

**9.12** Intermediaries ‘introduce’ potential clients to product providers. For example independent financial advisers match customers (private individuals or businesses) with product providers (e.g. life insurance, pensions) and mortgage intermediaries make connections between borrowers and mortgage lenders. Evidence from intermediaries suggests increased dialogue with them would help the Treasury to understand better the role they play and where money laundering risks may lie. Some intermediaries feel that their issues have not been considered to date: “mortgage intermediaries have clearly been forgotten, overlooked or not engaged in this piece”. A number of intermediaries feel they should be exempt from the regulations on the grounds that the product provider conducts CDD to detect suspicious activity making, in their view, the intermediary’s role in CDD superfluous. Intermediaries also feel that the formulation of guidance, JMLSG in particular, is formed by and written for large banks, which make it less useful for them.

**9.13** There have been a number of requests that the Treasury raise its profile in terms of providing regular updates to supervisors and businesses on developments in the EU and internationally, providing money laundering advisories on high-risk overseas jurisdictions, providing information about PEPs and equivalent jurisdictions and holding regular forums to facilitate feedback from practitioners and promote professional engagement.

**9.14** A number of stakeholders drew attention to the need for the UK to push for other EU Member States to transpose the EU Directive equally to ensure a level playing field. Some businesses argued that the UK's relatively rapid transposition of the EU Directive leaves them at a disadvantage in terms of international competitiveness across Europe and beyond in the absence of a uniform compliance with international standards

**9.15** In summary, evidence for the level of engagement by the Treasury supports a generally positive view. A wide range of stakeholders is regularly engaged with, information on the regulations is shared and opportunities are provided for stakeholders to give their views and provide input to the regime.

### **Engagement by supervisors**

**9.16** There is considerable evidence of engagement by supervisors with regulated businesses, including opportunities to contribute to the development of guidance.

**9.17** Feedback on engagement between supervisors and regulated businesses including trade associations and professional bodies is mixed however. There is a generally positive view that engagement is taking place and through a variety of channels including technical committees, newsletters, road-shows and online communications. Feedback has come from supervisors, regulated businesses and industry bodies. For example a large bank made numerous references to the FSA's communication and engagement, and another large firm noted that the "ICAEW provides comprehensive on-line information, email updates, roadshows, helplines and guidance." Most businesses / bodies that make reference to these sorts of channels appear to be happy with the level of engagement, their ability to inform / contribute to development of the regime and access to information about the regime.

**9.18** Some of the less positive comments arise from differences between supervisors in terms of consistency of guidance, compliance monitoring and enforcement; and strengthening a risk-based, proportionate and effective approach to compliance and enforcement.

**9.19** At least two responses noted that the FSA runs tailored annual seminars, one day events and manages relationships on a "close and continuous" basis with many of its supervised population. It also conducts themed AML reviews, which a trade body noted its members find useful in clarifying the FSA's expectations. Another supervisor holds AML road-shows and training events and encourages feedbacks through professional reviewers.

**9.20** A further supervisor recently held a number of road-shows in conjunction with SOCA and the police to promote understanding and obtain feedback (there are plans to make this an annual occurrence) and notes that results and recommendations from compliance visits are discussed on site with businesses as well as formally documented, and a feedback form is available. A further supervisor with small business members, in addition to using its compliance visits for general outreach, ran a series of seminars throughout the country in 2008 and again in 2009.

**9.21** One area of concern raised by businesses was that supervisors often will not give a definitive response to questions asked, particularly during or subsequent to compliance visits where the supervisor has identified a problem. As a result it can be difficult for businesses to get advice on what specific action to take. Businesses supervised by the FSA and the Gambling Commission noted this issue in particular.

**9.22** FSA publications and papers including regular Financial Crime Newsletters and online updates as well as help-lines were highlighted. One large supervisor runs a Money Laundering Helpline and offers help sheets and news items through its website – the value of these was confirmed by a large member firm.

**9.23** HMRC runs Money Service Business (MSB) Forums and Trust and Company Service Providers Forums for regulated businesses at regular intervals during the year. External speakers present on AML topics and businesses have the opportunity to meet and share experience and knowledge with other practitioners in their sector. At least one business, noted its membership of the MSB forum through which it has had the opportunity to help shape the regulations and guidance.

**9.24** A large bank noted that the FSA draws on industry views through their contribution to its Consultation and Discussion Papers. The FSA also runs a Practitioner Panel and a Small Businesses Practitioner Panel, which cover the full range of FSA issues including AML.

**9.25** Non-supervisory industry associations and professional bodies are a further source of information for regulated businesses, and provide a conduit for businesses' voices at supervisor and Government level.

**9.26** There were some requests for more general engagement. For example, a trade body would welcome engagement "more fully on an on-going basis in the UK". In particular it notes that its members find the approach between supervisors to be quite different, and would welcome more opportunities for engagement including "a more formal structure in order to allow regular exchanges of intelligence and views between supervisors and the representatives of regulated businesses". Another business would welcome more communication generally to help educate the supervised population, including a request that supervisors themselves become better acquainted with the agent-principle business model.

**9.27** A supervisor noted a recent series of road-shows held in conjunction with SOCA and the police to promote understanding of the AML regime by businesses and to obtain industry feedback. A firm makes reference to SOCA's industry outreach efforts.

**9.28** Once again, there may be more scope to engage SMEs. For example, one firm noted that although it has had a positive experience of engagement through HMRC's MSB Forum, it felt that smaller, independent businesses may struggle to attend the forum because they cannot leave their shop unattended, or simply through a lack of awareness.

**9.29** It was suggested that HMRC could improve website access and noted that MSBs would benefit from greater distribution of information via the website including a blog or other channels to promote knowledge sharing.

**9.30** A few responses noted displeasure with registration processes for a number of the supervisors. These included comments on the registration overlap with the optional London Borough's registration scheme for mail handlers that impact on some of HMRC's supervised population. Also the OFT's current process for registration of Estate Agents received a number of comments, more broadly linked to a sense by businesses that the OFT has taken a long time to get up to speed and engage with its supervised population.

### **Engagement with customers**

**9.31** On the issue of CDD, a number of responses highlight differences between institutions, and suggest some disproportionate or unreasonable requirements are in place. They indicate that if customers were better informed of their rights, particularly in relation to what alternative forms of identification are permissible, they could challenge industry to take a more risk-based approach at the customer interface.

**9.32** A number of forums exist for customer contribution to the regime, including the FSA's consumer panel and via third sector organisations. However, the review found little evidence of broader engagement on the part of regulated businesses. This may be because there is limited communication, or it could be that during our engagement with businesses they were more focussed on the impact the regulations have on themselves.

**9.33** The evidence submitted was mostly critical and came from third sector organisations as well as private individuals responding to the call for evidence.

**9.34** The main criticism we heard was over the flexibility of frontline staff (and their willingness to accept a range of identity documents) or the clarity of any explanations given into AML or other checks. At an event hosted by Toynbee Hall at which a number of organisations active on behalf of various potentially financially excluded groups were represented, it was stated that vulnerable clients often feel like they are not given any explanation of why ID checks are being done or why there are problems with the evidence they have provided. This can often lead to them feeling ‘unwanted’ by the banks. More generally, private individual responses to the call for evidence noted difficulties with businesses in relation to CDD as well as inconsistencies between businesses, mostly banks.

**9.35** Criticisms were also made in relation to difficulties for expatriates who no longer have residence in the UK. Problems with access to existing financial and legal services were noted by a number of people as expatriate customers reported specific difficulties in satisfying potential suppliers in some cases. Again, lack of consistency between businesses was a common theme.

**9.36** That said, a number of businesses noted that customers are less vocal than in the past and they heard fewer complaints now; to some extent this was attributed to a growing familiarity with identity checks made by financial businesses.

**9.37** At an event with third sector consumer organisations, they noted that the JMLSG guidance is good and it addresses financial exclusion issues and states that banks should be flexible. However, they also noted that problems exist with banks’ interpretation in practice. That said, credit unions were praised as having a better approach to the regulations and look to enforce them in a way that is not detrimental to clients.

### **Other responses**

**9.38** Many responses called for greater information from SOCA and the police as the end-users of SARs submitted by the regulated sector. However several responses also drew attention to various efforts by SOCA to provide feedback and information, including through participation in industry events, forums and newsletters, through the provision of bulletins and alerts and through a new initiative to provide feedback on the first SAR submitted by new reporters.

**9.39** A third-sector body notes an “atmosphere of positive cooperation between the departments and agencies involved in work related to the processes of corruption, AML and PEP’s” though they had some concerns about how their cooperation functions as a whole.

**9.40** Disappointment was expressed by a number of stakeholders in relation to lack of engagement on other non-HM Treasury aspects of the AML regime such as the Home Office’s Counter-Terrorism Act 2008, the Department for Work and Pensions’ Child Maintenance and Other Payments Act 2008, and the extension of financial investigation powers for bodies other than the police.

## **The Government Response**

**9.41** The Government considers it important that following this review it continues to engage with stakeholders, to feedback its response to those views and seek their input into any changes to the Regulations.

**9.42** Prior to the 2007 Regulations coming into effect the Government met with and consulted a wide range of stakeholders including:

- other government departments and agencies;

- industry associations and professional bodies;
- third sector organisations including anti-corruption NGOs and those representing vulnerable members of society;
- businesses that were regulated under the existing 2003 legislation;
- and businesses that would likely be regulated under the 2007 legislation (based on the content of the EU Directive).

**9.43** Meetings provided the opportunity for feedback and information sharing including gathering views on the specific provisions in the Regulations.

**9.44** Since then, the Treasury has continued to engage with these groups to share information, provide feedback and solicit stakeholder views. With the Home Office it co-chairs the Money Laundering Advisory Committee and attends the Supervisors Forum, which are held three and four times a year respectively. Officials attend various seminars and conferences to talk about the Regulations and to listen to the views of others.

**9.45** The review itself has been an opportunity for stakeholders to share their views with the Treasury; and for the Government to listen carefully to what stakeholders across all sectors have to say. This has taken place through both the Call for Evidence, and stakeholder events across the country.

**9.46** Other areas of Government, SOCA and Police in particular need to continue to engage with stakeholders and get more information out to the regulated sector. Businesses believe that more detailed and sector specific feedback would be very helpful. HM Treasury will continue to encourage this.

**9.47** Since the review began, Government officials now attend gambling sector meetings for both the casino and online gaming sectors on a periodic basis.

**9.48** The Government will work with law enforcement agencies and supervisors to improve engagement with SMEs or facilitate their participation in engagement, in order that the Government understands their issues and helps identify ways to overcome some of the barriers they face.

**9.49** The Government encourage supervisors to maintain open dialogue with their supervised population and other interested parties. Subject to any changes identified or already underway, we encourage HMRC to find a solution that eliminates registration fee duplication with the London Borough's scheme.

**9.50** Regulated businesses should ensure communications with customers are clear and helpful. More support and training for branch staff could be useful and greater consideration of issues around financial inclusion may be required. The Government will continue to use suitable opportunities to engage on financial exclusion issues and promote examples of good practice.

**9.51** There is scope to raise awareness of the various ways in which the Government engages with supervisors and the regulated sectors, including the Supervisors Forum or supervisor chaired panels for their supervised populations. It may also be desirable for supervisors to review attendance and content, and consider other forms of communicating issues, to ensure a good mix of stakeholders is engaged. Given the size of the regulated sector, a greater degree of engagement will always be desirable.

**9.52** Generally HM Treasury relies on professional bodies to undertake the majority of this level of engagement. It could consider taking a more active role, but there would be significant resource implications. HM Treasury already operates an email subscription service that it uses as a means of circulating advisory statements based on FATF warnings and other relevant

information. It may be helpful to remind regulated businesses of that service. (See [www.hm-treasury.gov.uk/fin\\_crime\\_mailinglist.htm](http://www.hm-treasury.gov.uk/fin_crime_mailinglist.htm) for advice on how to subscribe)

**9.53** In response to those that argued that the UK implementation of the EU Directive and international standards creates a competitive disadvantage for UK businesses by going further and through being implemented quicker than in other countries; it is important to point out that the UK has not done any more than properly implement the Directive as required and on time, including all the various simplification and deregulatory provisions. We have also worked with the EC and other Member States to encourage the same approach by all countries

**9.54** By July 2010 all EU Member States had notified the European Commission that they had fully implemented EU Directive.

**9.55** If presented with evidence of where UK businesses are being put at a competitive disadvantage by other countries failure to implement international standards, the Treasury will ensure that this is raised directly with the country or countries in question.

**9.56** The Treasury leads the UK delegation to the Financial Action Task Force (FATF), which is the international standard setter for money laundering and the financing of terrorism controls. The UK is an observer to Moneyval, the European regional AML/CTF body and a co-signatory to the Caribbean Financial Action Task Force. The UK is an active participant in the FATF peer review process, and has provided assessors for mutual evaluations; both for FATF members and more broadly, examples include Nigeria in 2008 and Greece in 2007.

**9.57** Within the FATF, the Treasury promotes the development of a strong working relationship with the private sector, and a key legacy of its 2007/2008 Presidency was the establishment of the private sector consultative forum, a group that discusses policy matters within the FATF to represent the broader view.

**9.58** It is intended that this review will inform the Treasury's domestic and international policy development. It provides evidence to support any changes that the Treasury may wish to advocate or more generally inform discussion at these forums.

**9.59** In addition, the Money Laundering Advisory Committee will become more active in seeking views from the private sector on international policy developments and provide a channel for industry concerns and views to inform the UK position in international negotiations.



# A

## Statistics on responses to call for evidence

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### Type of respondent

**A.1** The Review team received 91 written responses to the Call for Evidence. Respondents were asked to identify themselves as one of the following categories:

- Government department / law enforcement agency
- Supervisor
- Regulated Firm
- Non-Regulated Firm (customer firm)
- Private individual customer
- Other (professional bodies, non-governmental organisations, consumer groups, academics and professionals working with the Regulations but responding in a personal capacity)

**A.2** The following table shows the breakdown of respondents by categories, on the basis of the information provided by respondents.

**Table A.1: Table**

<b>Respondent type</b>	<b>Number</b>
Government department	2
Supervisor	17
Regulated Firm	26
Non-Regulated Firm	0
Private individual customer	10
Other	36
<b>Total</b>	<b>91</b>

### Regulated businesses by sector

**A.3** We also asked Regulated Businesses to classify themselves as belonging to one of the following sectors:

- Credit institutions
- Financial institutions
- Auditors, external accountants, tax advisers, insolvency practitioners
- Independent legal professionals
- Trust and company service providers
- Estate agents

- High value dealers
- Casinos
- Multiple sectors

**A.4** The following table presents the breakdown by sector of activity of the 26 Regulated Businesses that responded to the Call for Evidence.

**Table A.2: Table**

<b>Regulated Businesses by sector</b>	<b>Number</b>
Credit Institutions	1
Financial Institutions	8
Auditors, external accountants, tax advisers, insolvency practitioners	6
Independent legal professionals	6
Trust and Company Service Providers	2
Estate agents	1
High value dealers	0
Casinos	1
Multiple sectors	1
<b>Total</b>	<b>26</b>

## Regulated Businesses by size

**A.5** We asked Regulated Businesses to provide information on the number of staff they employ. Using this information, we have classified Regulated Businesses that provided a response into the following categories:

- Micro companies (businesses employing 5 or fewer people)
- Small companies (businesses employing between 6 and 50 people)
- Medium companies (businesses employing between 51 and 500 people)
- Big companies (businesses employing more than 500 people)

**A.6** The following table presents the breakdown by company size of the 26 Regulated Businesses that responded to the Call for Evidence.

**Table 9.A: Table**

<b>Regulated Businesses by size (Full Time Employees)</b>	<b>Number</b>
Micro	2
Small	4
Medium	5
Big	8
No data	7
<b>Total</b>	<b>26</b>

# B Events held during the Call for Evidence

**B.1** The following table lists the meetings held by the Review team during the Call for Evidence to publicise the Review and gather stakeholder views.

**Table 9.B: Table**

Number	Description	Date	Location
1	Meeting with Professor John Walker	26-Oct-09	London
2	Meeting with Serious and Organised Crime Agency (SOCA)	27-Oct-09	London
3	Meeting with the Financial Services Authority (FSA)	28-Oct-09	London
4	Meeting with businesses supervised by the Law Society	29-Oct-09	London
5	Meeting with Money Services Businesses (MSB) Forum	30-Oct-09	London
6	Meeting with the Crown Prosecution Service	09-Nov-09	London
7	Meeting with the City of London Police	09-Nov-09	London
8	Meeting with the British Bankers Association	10-Nov-09	London
9	Meeting with members of the International Association of Money Transfer Networks	11-Nov-09	London
10	Meeting with businesses supervised by the Law Society of Scotland	12-Nov-09	Edinburgh
11	Meeting with businesses supervised by the FSA in Scotland	13-Nov-09	Edinburgh
12	Meeting with businesses supervised by the Office of Fair Trading	16-Nov-09	London
13	Meeting with businesses supervised by Chartered Accountants Regulatory Board	18-Nov-09	Belfast
14	Meeting with businesses supervised by the Law Society of Northern Ireland	18-Nov-09	Belfast
15	Meeting with members of the Institute of Directors	19-Nov-09	London
16	Meeting with businesses supervised by HMRC: MSB, Accountancy Service Providers (ASP) and High Value Dealers (HVD)	20-Nov-09	London
17	Meeting with the Supervisors Forum	23-Nov-09	London
18	Meeting with members of the Association of British Insurers	25-Nov-09	London
19	Meeting with members of the Association for Financial Markets in Europe	25-Nov-09	London
20	Meeting with the Home Office	25-Nov-09	London

21	Meeting with members of the Building Society Association	26-Nov-09	Manchester
22	Meeting with businesses supervised by the Gambling Commission	27-Nov-09	Birmingham
23	Meeting with the Gambling Commission	27-Nov-09	Birmingham
24	Meeting with members of the Investment Managers Association	30-Nov-09	London
25	Meeting with members of the Association of Independent Financial Advisers (AIFA) & the Association of Mortgage Intermediaries (AMI)	01-Dec-09	London
26	Meeting with representatives of customers at Toynebee Hall	02-Dec-09	London
27	Meeting with businesses supervised by HMRC: Trust and Company Service Providers (TCSP)	03-Dec-09	London
28	Meeting with members of the Association of Private Client s Investment Managers and Stockbrokers (APCIMS)	04-Dec-09	London
29	Meeting with the Institute of Chartered Accountants in England and Wales (ICAEW) Technical Panel	09-Dec-09	London



# List of consultation questions

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C.1 This is a list of the consultation questions.

1. Should the existing criminal sanctions be wholly or partly repealed?
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?
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?
4. Should a debt purchaser be able to rely on CDD previously performed by the seller in this situation?
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?
6. Do you agree that non-lending credit institutions should be exempt from the Regulations?
7. Do you agree UK estate agents who arrange for the sale and purchase of overseas property by their clients should be regulated?
8. Do you agree that “safe custody services” should be more clearly defined, and if so, how?
9. Do you agree that all previous criminal conduct should be considered under the fit and proper test for MSB’s?
10. Do you agree a right of appeal should be introduced for decisions under the fit and proper test by HMRC?
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?
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?
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?
15. Should supervisors have clear powers to make enquiries of persons who reasonably appear to be relevant persons?

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 new 'gateways' to allow for the exchange of information?

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

### HM Treasury contacts

This document can be found in full on our website at:  
[hm-treasury.gov.uk](http://hm-treasury.gov.uk)

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