

ICAEW Representation

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HOUSE OF LORDS SELECT COMMITTEE ON THE EUROPEAN UNION SUB-COMMITTEE F (HOME AFFAIRS)

INQUIRY INTO MONEY LAUNDERING AND TERRORIST FINANCING

Written evidence submitted in February 2009 to the House of Lords Select Committee on the European Union Sub-committee F (Home Affairs) in connection with their inquiry into EU and international cooperation to counter money laundering and the financing of terrorism. This evidence was prepared for the Committee, and is its property.

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INTRODUCTION

The Institute of Chartered Accountants in England and Wales (ICAEW) welcomes the opportunity to provide written evidence to the House of Lords Select Committee on the European Union Sub-committee F (Home Affairs), in connection with their Inquiry into Money Laundering and the Financing of Terrorism.

The ICAEW has been a leading contributor to the debate on developing anti-money laundering legislation, since the development of the Proceeds of Crime Act, before it was passed in 2002. Karen Silcock, the chairman of the ICAEW's Money Laundering Committee is a member of SOCA's Suspicious Activity Reporting Regime Committee, selected by SOCA to represent the accountancy sector in this high level group established by the SOC A board which oversees the operation of the regime, and the ICAEW's Head of Business Law, Felicity Banks, represents the Consultative Committee of Accountancy Bodies on the Treasury's Money Laundering Advisory Body. The anti-money laundering guidance, issued by the CCAB, has been approved by the Treasury for application by all accountancy service providers.

This response is mainly aimed at the implementation of the Third Money Laundering Directive, no 2005/60/EC, which directly impacts ICAEW members in practice and practising firms.

Unless clear from the text, in this paper the term "money laundering" should be read to encompass terrorist funding.

MAIN POINTS

Differences in Implementation – Predicate Offences and Definitions of Money laundering

1. There are significant differences in the implementation of the money laundering directives in the UK, as compared to other EU member states.
2. The ICAEW believes that the UK has been exemplary in its speed and thoroughness of implementation. The directives have also been implemented in the UK in a way which has led to a very large number of money laundering suspicious activity reports (SARs) having been made to SOCA, with an expensive and sophisticated system for their recording and use. For example, through our work with the European Federation of Accountants (FEE – www.fee.be) we understand that although practising accountants in the UK submit over 8,000 SARs a year, the accountancy professions in other member state have submitted no more than 100 in any year, and some much less.
3. Some other member states have been slow and reluctant to implement the money laundering directives. However, the ICAEW does not believe that inadequate implementation represents the most significant differences in the operation of the systems in the UK and other member states. Rather, the differences lie in the rigour and enthusiasm with which the implemented directives are interpreted and enforced, in the ways in which options in the directive are implemented and the underlying criminal offences are framed. The greatest differences seems to lie in two particular characteristics of the UK legislation, which are often not reflected elsewhere. These are:
 - All crimes reporting.
Under the directives, the definition of "criminal activity" is limited to involvement in the commission of a serious crime, with the effect that the laundering of the proceeds of

less serious crimes can be left out of the SARs reporting regime. That is not the case in the UK.

- Proceeds of own crime.
The definition of money laundering in the directives is framed firstly in terms of conversion or transfer of criminal property, and secondly in its concealment or disguise. The third element of the definition is the acquisition, possession or use of property, knowing, at the time of receipt, that such property was derived from criminal activity. Many jurisdictions have interpreted this as indicating that at least one transaction in the criminal property must take place for money laundering to exist. In the UK, the simple and passive possession of the proceeds of an offender's own crime also represents money laundering. This draws into the money laundering reporting net many instances, like much tax evasion, where no active concealment or laundering takes place.

Cost Effectiveness, and its Measurement

4. The costs of the anti-money laundering regime in the UK are undoubtedly very high. However, the exact quantum of the costs that are incurred exclusively on anti-money laundering are difficult to judge. The client due diligence procedures which are performed primarily for anti-money laundering compliance purposes are, for example, undoubtedly also useful in reducing risks for accountancy firms in accepting inappropriate clients, or those whose business rationale is unclear, with consequent reputational risks.
5. Probably, over the profession as a whole, more costs are incurred in the area of client acceptance procedures and due diligence than in the systems for suspicion evaluation and reporting. Since implementation of the directives appears to have been less variable in requirements for client due diligence than in the definition and reporting requirements for suspected money laundering, costs are likely to be high throughout Europe.
6. The benefits of the anti-money laundering reporting regime are even more difficult to judge. If effectively fed into the law enforcement process, and used efficiently, SARs will provide useful intelligence and thus enable criminal investigations to be carried out more cheaply and with better outcomes. An efficient law enforcement system has significant benefits in terms of better public trust and safety, fairer commerce and economic progress and improved international reputation. Partly due to the secrecy necessary to much criminal investigation, however, the benefits are likely to be difficult to assess with accuracy, even in a single case. This is even more the case for suspected terrorism. However, the overall cost/benefit balance in the UK does appear to be improving over time, as shown by the increased use of reporting intelligence across a wide range of serious and violent crime as well as being used for restraint and confiscation of criminal proceeds (evidenced by the most recent report from SOCA on the operation of the reporting regime). Given the high cost to the regulated sector of compliance with the directives, an all crimes reporting system feeding into law enforcement teams focussed on extracting value from the data would seem better to justify the cost and extract real benefit for the community than a system that requires a massive investment in systems and procedures but produces little of intelligence value.
7. SOCA are conscious of the importance of feedback about its work, and continue to discuss this issue with members of the accountancy profession and other stakeholders on improving it. The ICAEW's perception of the situation is that with the increased resources being made available to SOCA, and the improvements made to their systems, the effectiveness of the system has improved and with it its cost effectiveness.

8. It is the ICAEW's belief that, although the costs of implementation in the UK, for the accountancy profession at least, may be higher than in other jurisdictions, the very significant improvement in the control of illegal activities that results makes the regime cost effective. Though costs may be less in other jurisdictions, the ICAEW believes that the costs which are incurred are more likely to be wasted, due to the much lower benefit in terms of the control of crime. That is, the higher benefits justify the higher costs incurred.
9. Ultimately, the benefit of averting even a single serious terrorist outrage is extremely high.

RESPONSES TO SPECIFIC QUESTIONS

Cooperation with and between Financial Intelligence Units (FIUs)

How effective is cooperation among FIUs, and between FIUs and other authorities?

What are the practical results of this cooperation?

How does the private sector feed into this cooperation? To what extent is satisfactory feedback to the private sector required by international standards, and what happens in practice?

10. The ICAEW can provide little evidence on the effectiveness of cooperation between FIUs, though we are aware of the existence of the Egmont Group of FIUs and we believe it to be operating satisfactorily. For example, we have received assurances from SOCA that sensitive reports of suspicions provided by ICAEW members will only be released to overseas jurisdictions through a member of the Egmont Group, with the result that ICAEW members need not fear irresponsible disclosure or misuse of their confidential information.
11. Cooperation between the UK FIU and other authorities appears to be extensive, and the evidence of our own relationship with SOCA supports this conclusion. Feedback operates in both directions, increasing trust between the various parties involved, and hence the efficiency and effectiveness of the system.
12. The private sector feeds into this cooperation through:
 - the Money Laundering Advisory Committee, led by HM Treasury and the Home Office, which includes representatives of key elements of the regulated sector, law enforcement and Government Departments;
 - the Anti-Money Laundering Supervisors and Regulators Fora, where AML supervisors (including both public bodies and private professional bodies) discuss matters of consistency and concern with each other and with SOCA and Government Departments.
 - the inclusion of trusted individuals from the private sector in SOCA consultative bodies headed by the Suspicious Activity Reporting Regime Committee but also encompassing the "Vetted Group" which works with SOCA to share sensitive intelligence with the reporting community, and special focus groups such as those set up to provide private sector input into the development of information management systems within SOCA.
13. In addition, SOCA run their own training events for members of the private sector, and provide speakers for privately run training events. These events promote two way communication, with questions from the floor allowing concerns and comments on effectiveness to be expressed.

14. An example of the effectiveness of feedback and cooperation is in the area of the confidentiality of SARs. In the early years after the implementation of the Money Laundering Regulations 2003, we received fairly frequent reports of the disclosure to the clients of our members that their accountant had made a SAR, revealing a suspicion that the client had acted illegally. This most frequently occurred through administrative carelessness, or to assist the effectiveness of questioning (by indicating the seriousness of evidence of wrongdoing to a suspect). The effect on the client/accountant relationship could be catastrophic, and led to marked reluctance in other accountants to report their suspicions when these instances were revealed in the press. However, since feedback was given of the serious effects that these lapses could have on cooperation by the accounting profession, and (we believe) a more effective relationship between SOCA and the Law Enforcement Agencies, the reports of breach of confidentiality have radically reduced and are now very rare.
15. Both EU Directives and the FATF "Recommendations" require feedback to the private sector, but are not specific about how or what feedback should be given. Members of the accountancy profession would prefer more feedback, at a number of levels, both to help firms and the accounting professional bodies to manage risk and to provide feedback on the usefulness of reports. The ICAEW is aware that SOCA is working on increasing the amount and usefulness of the feedback that can be given.

What is the extent of the feedback and input on terrorist financing issues from intelligence and security services?

16. The ICAEW understands that SOCA has good links with the intelligence and security services, and that terrorist and financing issues form a sizeable section of their work.
17. Feedback given to the ICAEW by SOCA (for dissemination to selected members) includes information on areas of growing illegal activity which could be associated with terrorism, and where it is believed that higher awareness of these by our members could improve the intelligence available to Law Enforcement Authorities, by the making of more and better relevant SARs.

To what extent are alternative remittance systems appropriately covered by obligations of cooperation in this context? What will be the impact of the implementation by Member States of the relevant provisions of Directive 2007/54/EC in this regard?

18. Alternative remittance systems are by their nature informal, and not highly organised. Many money service businesses are not members of trade bodies and many may not be aware of their obligations under the Money Laundering Regulations. HMRC, as well as SOCA, are acting to increase awareness in this sector. The ICAEW has no specific views on the likely impact of Directive 2007/54/EC in this regard.

EU internal architecture

19. The ICAEW has no views on this matter.

International cooperation

What have been the results of the third round of mutual evaluations of EU Member States to date carried out by the FATF and MONEYVAL, with particular reference to the effectiveness of international cooperation (including as between FIUs)?

20. The ICAEW's experience of the process of mutual evaluations is limited mainly to our contribution to the FATF evaluation of the UK. This leads us to believe that the evaluations are taken seriously by both the jurisdiction subject to the evaluation and the team of evaluators, with great effort made to justify the ways in which compliance has been achieved and to understand this justification. This gradually spreads understanding of differing approaches, adoption of the best and consequently increased trust and cooperation. This is, however, a slow process.

To what extent has the formal framework for criminal justice cooperation in this area been effective?

21. The ICAEW has no views on this matter.

To what extent are these systems used to enforce compliance with national tax obligations?

22. The ICAEW's knowledge of the use of the AML system to enforce compliance with tax obligations is mainly limited to the UK, where SARs are submitted in relation to suspected tax evasion, and are used by HMRC.
23. Not all jurisdictions consider tax evasion to be a predicate offence for money laundering purposes.

EU-UN cooperation

24. The ICAEW has no views on this matter.

Monitoring implementation

What EU mechanisms exist for monitoring implementation of the relevant legislative measures, and what results in terms of formal compliance and effective implementation have so far emerged from the use of those measures? What are the implications of those results for cooperation within the EU, and more broadly?

25. Besides the formal EU mechanisms for monitoring compliance with the money laundering directives, the professions and some trade groups have pan-European associations which also monitor implementation, particularly as it affects their members or stakeholder groups. An example of this is the ICAEW's work with FEE.
26. Global professional associations also work to monitor compliance in various jurisdictions on a global basis and advise their members on expectations, when acting overseas or in a cross border context. A good example of this is the useful site that the International Bar Association has set up at <http://www.anti-moneylaundering.org>, which gives a comprehensive guide to anti-money laundering legislation and compliance, throughout the world.

Has consideration been given within the EU or by the FATF to whether the overall results derived from the present system justify the burdens placed on the private sector?

27. The ICAEW is not aware of comprehensive exercises which have been undertaken by either the EU or FATF to measure the cost effectiveness of the present system, but see above under our main points, for our comments on the difficulties of measuring cost effectiveness, and the value of the system in the UK.

Are there plans to review the existing EU legislation or international standards in a manner which would be more sensitive to the position of the private sector?

28. FATF has recently introduced guidance on the application of a risk based approach to compliance with its requirements, by the private sector, whereas previously a more bureaucratic system has been applied in its interpretation of its requirements and in mutual evaluations. The ICAEW supports this move, and the further extension of a risk based approach to implementation, which we believe will lead to a more cost effective system.

Compliance and equivalence

What are the powers and procedures with respect to those third countries which fail properly to implement international standards in these areas? Are these adequate? Does the 2005 Directive adequately encourage non-EU States which have introduced equivalent systems to counter money laundering and the financing of terrorism?

29. The main powers and procedures that the ICAEW is aware of, to put pressure on countries to implement international standards in this area, are adverse publicity and additional systems and controls requirements on those dealing with them, or with their citizens. Positive affirmation is also given, by membership of FATF itself, or by membership of a regional FATF style body.

30. Under the 2005 Directive, European financial institutions are required to apply European anti-money laundering standards to their branches in non-equivalent jurisdictions, or to inform the appropriate authorities if this is not possible. This will help to spread compliance with European standards elsewhere. However, both financial institutions and professional firms working in an international context should be motivated to apply good standards everywhere anyway, to protect their global branding and reputation. It is therefore difficult to say whether this is an effect of the Directive, or would have occurred in any case.

31. Jurisdictions are generally improving their anti-money laundering systems and requirements, so we believe that these procedures are adequate, though there is clearly a great deal further to go.

How does the system for determining equivalence operate in practice?

32. Whatever the underlying jurisdiction with which financial institutions or professionals carry out commercial or advisory business, it is important for them to ensure that they understand the identity of the person with whom they are transacting, and the likely risks of the relationship. This is so whether or not the jurisdiction from which the contractual

partner is operating has equivalent anti-money laundering systems and requirements. Though overall risks will be higher in non-compliant jurisdictions, there will nevertheless be higher risk clients in lower risk jurisdictions and vice versa.

33. The systems for determining equivalence within Europe and elsewhere are not entirely transparent, but provided that they do not result in injustice for poorly assessed jurisdictions, and they assist in improving systems overall, we do not consider that this is the most important issue in anti-money laundering policy development.

ABOUT THE ICAEW

The ICAEW operates under a Royal Charter, working in the public interest. As a world leading professional accountancy body, the Institute provides leadership and practical support to over 132,000 members in more than 140 countries, working with governments, regulators and industry in order to ensure the highest standards are maintained. The ICAEW is a founding member of the Global Accounting Alliance with over 700,000 members worldwide. Our members provide financial knowledge and guidance based on the highest technical and ethical standards. They are trained to challenge people and organisations to think and act differently, to provide clarity and rigour, and so help create and sustain prosperity. The Institute ensures these skills are constantly developed, recognised and valued.

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