BRIEFING

SUPERVISING BUSINESSES – A NEW APPROACH?

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The Treasury's recent Anti-Money Laundering and Counter Terrorist Finance Report ("the Report") emphasises the UK government's commitment to tackling these twin threats. As it highlights, such offences not only impact upon the individual firms concerned, but also undermine London's reputation as a financial centre. Effective and proportionate supervision lies at the heart of the Treasury's response. The Report stresses the benefits of adopting a risk-based approach to supervision, ensuring that resources are properly focused on the small percentage of transactions which constitute the greatest danger. In the same vein, it also emphasises the importance of supervisors and businesses collaborating and cooperating with one another. Nonetheless, the regime is not without teeth – the Report stresses the importance of "robust supervision and severe penalties" where appropriate.

WHO ARE SUPERVISORS?

The Money Laundering Regulations 2007 ("the Regulations") require businesses to use due diligence when monitoring their customer and business relationships. In this manner the UK complies with the recommendations put forward by the Financial Action Task Force ("FATF"), an inter-governmental body dedicated to combating international financial threats.

The Treasury appoints supervising bodies to monitor businesses' compliance with these Regulations. These include regulatory bodies such as the FCA, the PRA, and the Office of Fair Trading, as well as professional associations like the Association of Chartered Certified Accountants, the Council for Licensed Conveyancers, and the Institute of Financial Accountants.

In deciding whether to appoint an organisation as a supervisor the Treasury looks for bodies with:

- Experience of setting standards for its members;
- Experience monitoring compliance;
- Established disciplinary procedures and sanctions;
- Strong "public interest objectives", for example bodies with charitable status;
- Significant membership;
- Sufficient resources for effective supervision;
- Good relationships with other supervisors and relevant public bodies;
- An understanding of the risk-based approach to supervision; and
- Awareness of global standards for supervisors set by the FATF.

A PROPORTIONATE APPROACH

The Report highlights the importance of adopting a risk-based approach to supervision. The Treasury was pleased to confirm that "All supervisors have demonstrated an understanding of the risk-based approach, both for implementation by their supervised population and to inform their own supervisory activities."

Given the range of business sizes and operations the Report does not attempt to advance a 'one size fits all' model for supervision. Nonetheless, it does provide limited guidance. Compliance visits are a common means of ensuring members meet their regulatory requirements. Their use may not always be proportionate, however, and supervisors should not assume that all businesses necessarily require on-site inspections. In may be appropriate for such inspections to be triggered by particular risk factors, for example a businesses' change in annual return information, delayed or non-existence compliance with a supervisor, a failure to react to recommendations, intelligence received, or incomplete registration forms.

The Report stresses that there are effective and cheaper alternatives to such visits. For example, supervisors could rely on:

- The submission of annual returns;
- Compliance telephone interviews;
- Warning letters or requests for information.

In addition, supervisors should save time and resources in the future by working collaboratively with other bodies who visit the same businesses they supervise.

COMMUNICATION AND ENFORCEMENT

Rather than merely policing and prosecuting abuses, the Treasury encourages supervisors to promote compliance. Although the Regulations do not themselves require supervisors to offer formal advice, the Report makes clear that it is good practice to do so. Such formal guidance may then be approved by the Treasury and published on its website. Where resources allow, guidance should be targeted so that awareness is raised amongst those parties new to the sector, or deemed most likely to be non-compliant.

Supervisors have a variety of enforcement powers at their disposal. The FCA, PRA, HMRC, Office of Fair Trading and the Department of Enterprise Trade and Investment are all empowered by the Regulations to impose civil monetary penalties. Professional bodies may expel a particular business from the organisation and remove their professional accreditation. If necessary, of course, supervisors may refer a case to the appropriate authorities for criminal prosecution.

The Treasury does not require a strict or inflexible policy towards enforcement. In general, a member will be given the opportunity to correct its behaviour first. The Report highlighted the practice used by the Council for Licensed Conveyancers.

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The Council first considers an informal resolution. If that is inappropriate or unsuccessful, it begins regulatory action. This may include the member providing a report explaining how it proposes to deal with the issues identified. If this process is also unsuccessful or inappropriate, then disciplinary action is initiated.

Nonetheless, the Report emphasises supervisors should be prepared to take "robust action against those who demonstrate persistent or material breaches of the Regulations". The government had previously consulted on whether it should remove the threat of criminal penalties. It declined to do so. The Treasury considers,

> "Criminal penalties are a powerful deterrent against money laundering and terrorist financing and should be a useful tool for supervisors in tackling the worst offenders. The Government expects supervisors to use these penalties for the most egregious and serious and/or persistent non-compliance with the Regulations."

FUTURE DEVELOPMENTS

In February 2012 the FATF made a series of further recommendations for countering money laundering and terrorist financial threats. At their heart these recommendations seek to further strengthen the risk-based, targeted approach to supervision. As a result of these recommendations, on 5th February 2013 the European Commission published two anti-money laundering proposals, including a new directive. These proposals endorse the risk-based approach. More specifically, the Commission seeks to:

- Provide enhanced and simplified customer due diligence;
- Broaden the definition of 'politically exposed persons' ("PEP"). A PEP is a person who represents a higher risk of potential involvement in corruption by virtue of the political positions he holds, and is consequently the subject of particular anti-money laundering provisions. Currently the term applies only to foreign officials from outside the EU, or members of international organisations. The intention is that this term will apply to domestic officials as well;
- Provide a clear mechanism for ascertaining beneficial ownership;
- Lower the limit of cash allowed for payment of goods before triggering the provisions of the directive from €15,000 to €7,500;
- Require payment service providers to send the authorities information on fund transfer payers;
- Strengthen cooperation between national Financial Intelligence Units.

Consequently, supervisors are likely to be faced with significant further demands upon their resources in the near future. In meeting these demands, the importance of maintaining an effective and proportionate approach to supervision will be paramount.

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